



**SCOTTISHPOWER**

Smart Metering Implementation Programme  
Regulatory Design Team  
Department of Energy & Climate Change  
3 Whitehall Place  
London  
SW1A 2AW

19 July 2012

Dear Sir/Madam,

**SMART METERING - DCC DRAFT LICENCE AND LICENCE APPLICATION  
REGULATIONS**

We are pleased to respond to the Government's consultation on the Draft DCC Licence and Licence Application Regulations, dated 5 April 2012.

We responded to Questions 15 to 18 in our letter of 16 May. Our responses to Questions 1 to 14 are given in the attached annex.

We are in broad agreement with the Government's proposals relating to the drafting of the DCC Licence. However, we believe it must be a key objective of the DCC once the roll-out is delivered to increase efficiency over time and bear down on costs. To that end, we would reiterate our view that as respects the major functions, the DCC should confine itself to contract management of service providers and should not get involved in service provision in its own right. Any material service provision undertaken by the DCC itself should be subject to prior approval.

Should you wish to discuss any areas of this initial response in more detail, please do not hesitate to contact me

Yours faithfully,



## Annex 1

**Question 1: Do you agree with the structure and content of parts 1 and 2 of the licence?**

Yes. The structure and content of Parts 1 and 2 are largely as expected and generally seem appropriate and consistent with the position on other licences.

However, we note that Part 1 proposes that the Authority may grant a licence extension of up to six years, any time after 31st March 2018. We are concerned that such a milestone should occur quite so early in a twelve-year licence term, and would suggest that such a decision should not be possible earlier than 2021 (i.e. 4 years before the licence would be due to expire). In our view, this would provide adequate time for succession planning, or for the incumbent to prepare to meet the requirements of the extension.

Care should be taken to ensure that the provisions for extending the licence do not create any unintended constraint on the incumbent DCC supplier's commercial freedom in bidding in a subsequent re-tender.

**Question 2: Do you agree with the proposed list of licence revocation events, in particular do you agree with the inclusion of revocation triggers linked to:**

- i. A failure of the DCC to comply with an enforcement notice issued under Section 40 of the Data Protection Act;
- ii. A contravention of the licence condition or statutory requirement in a manner so serious as to make it inappropriate for the licensee to continue to hold the licence;
- iii. A contravention of the independence Condition 9; and
- iv. The licensee no longer being, or never having been, a fit and proper person to carry out the Authorised Activity?

We broadly agree with the list of licence revocation events proposed in the consultation document, but would make the following observations:

- With specific regard to a failure of the DCC to comply with an enforcement notice issued under Section 40 of the Data Protection Act, we would be concerned if this automatically triggered revocation. While prospective DCC bidders may take some comfort from the statement in the consultation document that it would be for the Authority to decide on revocation in such an event, they might also note the absence of any requirement for objective measurement of matters such as materiality.
- Although we particularly welcome the proposal to include a contravention of Condition 9 in the list of revocation events, as this should guarantee the on-going independence of the DCC, similar concerns about materiality arise.

It may be appropriate for both of these to be subject to the criterion that the breach or failure is so serious as to make it inappropriate for the licensee to continue to hold the licence.

**Question 3: Do you agree that the DCC licence should be issued for a fixed-term only?**

Yes. However, while we fully support the principle of a fixed term licence, we would question the proposed duration of the term. While we initially said that too short a term could make it difficult to attract bidders to act as DCC, an excessive but fixed term could provide insufficient competitive tension. A key driver for a longer licence term is the need to maintain consistency and certainty throughout mass roll out and into a steady state, which must be balanced against the competition issues. We think this implies a contract length of no more than 8-10 years.

**Question 4: Do you have any comments on Chapter 1 of the licence conditions, in particular do you have any comments on the drafting of the definitions?**

The definition of "Licence" does not reflect the fact that it is really two licences (see para 1 of Part 1 for the correct treatment of this issue). It may be that the definition could refer to that text.

In the definition of Price Control Condition, the parenthetical reference to Chapter 9 may not be helpful. If a subsequent condition change meant that another condition, not in Chapter 9, had the character of a Price Control Condition, the definition might not work as intended.

Smart meters and smart metering systems are defined as follows (Part 3, Chapter 1):

**Smart Meter** - means an Energy Meter and any devices that:

- a) are associated with or ancillary to that meter; and
- b) enable information to be communicated to or from the meter using an External Electronic Communications Network, and the related term "Smart Metering" when used as part of another defined term is to be read accordingly.

**Smart Metering System** - means a system installed at premises for the purposes of the Supply of Energy to the premises that, on the date on which it is installed, as a minimum:

- a) consists of the apparatus identified in;
- b) has the functional capability specified by; and
- c) complies with the other requirements of, the Smart Metering Equipment Technical Specification that is applicable at that date.

We read the definition of "Smart Meter" as being a generic and wider definition than the definition of "Smart Metering System" since it includes non-SMETS compliant meters such as advanced meters (and SMETS 1 meters) and possibly some prepayment meter systems. The Government has acknowledged that at least the first two types needed to be exempted from the prohibition order.

We are not sure that the two terms are used correctly throughout the licence. For example, in condition 22.17, which sets out the content of the SEC, the references are to the broader Smart Meters not the compliant Smart Metering Systems. Similarly, it is not clear to us that it is correct to use the words "(and includes a Smart Meter)" in the definition of Relevant Energy Meter in condition 3.13.

In addition, we also note references to 'SEC Service Provision' in Condition 13, which has the appearance of a defined term, yet it does not appear in Condition 1.

**Question 5: Do you have any comments on Chapter 2 of the licence conditions, in particular do you have any views on:**

**i. The general objectives of the DCC;**

We are broadly satisfied with the general objectives of the DCC.

**ii. The way in which the Mandatory and Permitted businesses of the DCC have been constructed;**

**iii. The interaction between the mandatory and permitted businesses;**

We are broadly satisfied with the approach to mandating the provision of core, elective and enabling services, while permitting the DCC's provision of value-added and Minimal Services. With regard to the Minimal Services, however, we note that they "must not, in total, exceed a turnover value of £500,000 in any Regulatory Year."<sup>1</sup> We understand that 'in total' means an aggregate of all Minimal Services, rather than, for example, the total turnover arising from any one particular Minimal Service that might have been provided to more than one User during the relevant Regulatory Year.

**iv. The proposed general and security controls for the DCC?**

We welcome the proposed approach to security controls and to information security. In particular, we support the requirement for the DCC to be certified to ISO 27001 and 27002, rather than the weaker option of simply requiring demonstration of its compliance with these standards.

We would question why in the text of the licence ongoing approval of changes to the internal control document (condition 7.7) and risk management arrangements (condition 7.12) is for the Secretary of State and not the Authority. The consultation document seems to say that it would indeed be for the Authority to give these approvals.

**Question 6: Do you have any comments on Chapter 3 of the licence conditions, in particular do you have any comments on:**

**i. the independence requirements of the DCC and the interaction with the revocation provisions;**

We fully support the principle that the DCC Licensee must be independent both of its users and of its service providers. In general, we are satisfied that the content and structure of the proposed licence conditions will satisfy this requirement. However, we would prefer that, if the Authority exercises its discretion under paragraphs 9.12 and 9.13 to consent to alternative arrangements to secure independence, it should first engage with industry stakeholders, perhaps through a formal consultation process.

As discussed above, there should be an appropriate materiality test linked to revocation for any breach of condition 9. The existence of such a materiality test for other breaches could in itself indicate that there was not even an implicit materiality criterion. Given that revocation would be complex for DCC users and its threat likely to affect willingness of DCC bidders, we think a materiality test would be in the interest of all parties.

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<sup>1</sup> Condition 6 (Authorised Business of the Licensee), paragraph 6(b)

**ii. the broad condition on protection of confidential information;**

The proposals around the protection of confidential information appear to offer a suitably robust approach that is in line both with requirements and our expectations.

**iii. the scope and nature of the role of the compliance officer?**

While we support the principles behind the proposal to appoint a Compliance Officer, we would expect that matters such as the nature and role of the compliance officer would be under the remit of the SEC Panel, albeit through delegated powers to the compliance / assurance committee. Such a committee would be well placed to scrutinise the annual statement of compliance that the DCC will be obliged to produce under Condition 10 of its licence, and to determine whether there is need for a more detailed investigation / audit of practices.

**Question 7: Do you have any comments on Chapter 4 of the licence conditions; in particular do you have any comments on the drafting of:**

**i. the transitional obligations on the DCC, possibly as part of a wider transition scheme;**

We think the requirement for unambiguous transitional arrangements is self-evident. However, the question remains as to whether these arrangements are best managed as a function of the SEC, or via a wider framework that encompasses such matters as the establishment of the DCC, the SEC itself and the market readiness of the broad range of other likely participants.

In considering this point, we note the work to-date of the Foundation work stream in setting out the SMIP's approach to the period prior to the DCC Licence Award. Clearly, arrangements need to be in place to support the transition from Foundation to DCC, but we also believe these arrangements need to consider the impact of the initial establishment of the SEC. We also note that Paragraph 16 of Condition 22 of the proposed DCC Licence allows for a transitional use of SEC governance.

We would, therefore, propose that the transition arrangements be managed as a standalone document, under SMIP governance until such times that it becomes a schedule to the SEC. This latter phase would afford a proportionate level of regulatory oversight and, where needed, intervention. Use of a sunset clause could effectively close down such a schedule in line with the completion of mass rollout.

**ii. the proposals for how the DCC would set out its future business development objectives;**

Regarding the DCC's future business development objectives, we support the approach to having the DCC provide a Development Plan for approval by the Authority. However, we think that much of the detail to be reported would, or should be, covered by the price control reporting obligations, particularly if the business development plan is intended to set out expected growth.

**iii. the proposed inclusion of a licence condition that would facilitate future transfer of registration to the DCC?**

We fully support including, from the outset, a condition in the DCC licence that will facilitate future transfer of registration from network operators to the DCC. We regard the transfer of

registrations as a first step in the DCC's evolution into a central data management role and a key component of smart metering benefits.

**Question 8: Do you have any comments on Chapter 5 of the licence conditions; in particular do you have any comments on:**

- i. The procurement obligations, including the balance between what the DCC must competitively procure and what it may self provide;**

We generally take the view that the DCC should be obliged to procure the vast majority of services, rather than meeting the requirements from its own resources. The consultation document states that the principal data and communication service contracts will be defined as "fundamental" and not open to self provision, although the way the licence is drafted, this seems only to apply to the initial contracts being procured by the Secretary of State.

We therefore consider that the licence should be clarified to indicate that the principal data and comms contracts should not be open to self provision whether or not they are the legacy ones agreed by the Secretary of State.

Beyond that, the scope for self-provision seems rather wide and we would suggest that there needs to be a prior approval process for self provision that is above a minimal scale.

- ii. The most appropriate role, if any, for the Authority in influencing how the DCC should balance various competing public interests, when preparing for future procurements of Fundamental Service Capability;**

We think it is vitally important that core services continue to be provided on a 'postage stamp' basis and would welcome regulatory intervention if this principle proved to be at risk during a future procurement.

- iii. Do you have any evidence from other sectors about how the public interest is taken into account by regulated bodies when making major procurement decisions;**

No.

- iv. The obligations on the DCC in relation to provision of services, recognising that these conditions will need to be reviewed in light of a more detailed definition of services; and**

Please refer to our response to Question 5.

- v. The charging methodology provisions, particularly the objectives of the methodology?**

The charging methodology provisions, proposed as Condition 18 of the DCC licence in the consultation, largely appear to satisfy the requirements. However, we would expect to see the specific inclusion of DCC Users in the list, set out in paragraph 18.9, of those persons with whom the Secretary of State will consult ahead of designating a charging methodology. With particular regard to the charging methodology objectives, we are also satisfied that they are in line with our expectations and the industry's requirements.



**Question 9: Do you have any comments on Chapter 6 of the licence conditions, in particular do you have any comments on:**

- i. The scope of the SEC as set out in the SEC condition and the SEC objectives;**

While we have no comment on the scope of the SEC as set out in the draft licence condition, we welcome the statement, at 4.158 of the consultation document, that "the SEC is not intended to be a DCC-only document". It is our view that the SEC should develop into a much broader document that considers all aspects of the 'smart market'.

- ii. Whether the DCC should have a licence obligation to maintain and keep in force the SEC;**

The DCC licence is just one of a number of possible vehicles for delivering on-going operation of the SEC (others might include a requirement in all energy licences), but we consider it to be the most appropriate, given the broad nature of organisations anticipated to accede to the SEC.

- iii. The proposal to allow the Secretary of State to block SEC modifications in the period up to 31 October 2018; and**

We have no specific objection to the proposal to grant the Secretary of State the power to block modification of the SEC before 31 October 2018.

- iv. The way in which interoperability should be addressed through the SEC objectives?**

While conditions of other licences already serve to reinforce the need for commercial interoperability, we believe a clear and unambiguous requirement to maintain technical interoperability and, moreover, interchangeability might yet be needed. Nonetheless, we do not consider the SEC objectives in the DCC licence to be the appropriate place to introduce a more detailed requirement, which we would prefer to see in the SEC itself.

**Question 10: Do you have particular comments on how best to ensure the consumer interest is met in the SEC Objectives, in particular:**

- i. Can you identify any potential scenarios where a modification might be proposed which would be in the interests of consumers but which would not be supported by the objectives set out for the code; and**

We are unable to identify any scenario where a modification might be proposed which, though in the interests of consumers, would not be supported by the code objectives.

- ii. If you think the objectives could be set out to better capture the interests of consumers, as opposed to the proposed approach for SEC objectives to be balanced in the round with due regard for energy consumers' interests, how do you think this could be done?**

We consider the approach for SEC objectives to be balanced with due regard for energy consumers' interests to be the appropriate one.

**Question 11: Do you have comments on the proposed condition allowing the Authority to put forward code modifications and for this power to be limited to specific areas defined in the SEC?**

Although we support the Significant Code Review approach to major code modifications, which is the means by which the Authority brings its influence to bear in the raising of modifications to other codes, we note the absence from these proposals of any requirement for the Authority to conduct any formal assessment prior to bringing forward a modification. This would seem wholly inappropriate as it would be likely to prejudice any subsequent assessment of such a modification by SEC Parties, the SEC Panel or Ofgem itself. We would also question whether it is the role of an economic regulator to drive market change, or to merely respond to proposed change in the interests of the market and, therefore, of the consumer.

In our view, the Significant Code Review process potentially affords the Authority a much greater opportunity to undertake a detailed analysis of all relevant issues than might be offered under the narrower code modification process.

**Question 12: Do you have any comments on Chapter 7 of the licence conditions, in particular do you have any comments on:**

- i. **The proposals in relation to financial security, in particular the requirement to provide a performance bond in addition to financial security?**

We agree that a performance bond could be desirable to ensure that the DCC's shareholders show an appropriate degree of commitment to a body that could have quite limited assets. Clearly, such a bond will not be without cost, and so there will be a balancing exercise in considering the amount.

**Question 13: Do you have any comments on Chapter 9 of the licence conditions; in particular do you have comments on:**

- i. **The need for the revenue restriction conditions in the DCC licence to evolve as the DCC's role changes;**

We agree that the focus should initially be on programme delivery, with more focus on cost reduction at a later date.

- ii. **The need to incentivise the DCC to concentrate on achieving programme milestones at the beginning;**

We would agree that the DCC is appropriately incentivised. Initially, any incentives should be put in place to ensure the timely rollout of smart meters.

- iii. **The proposal that the DCC's internal costs should be passed through with a £/annum margin applied;**

No comment.



- iv. **That incentives on reduction in the DCC's internal costs and on output measures should be applied later;**

We generally agree that it would be inappropriate to apply estimated values without access to reliable data on which they could be based. However, we would support the application of incentives as soon as relevant costs can be reasonably estimated.

- v. **That the DCC should be subject to an element of bad debt risk unless it takes reasonable measures to recover such debt; and**

Clearly, the DCC should be encouraged to recover debts wherever possible, rather than simply passing their costs through to users. However, there is no natural incentive to do so. Hence, to promote confidence among the user community, it is important that an appropriately transparent incentive regime is established to make sure that the DCC conforms to the requirements.

- vi. **Particular KPIs that could be applied to the DCC after it starts to deliver services?**

While we would not put forward any detailed proposals at this time, we wish to draw attention to the on-going development work of the service catalogue which will include performance standards. We think these should form the basis of initial KPIs. We would also suggest that the DCC must ensure that its CSPs roll out their communications networks efficiently. More generally the DCC should ensure it places suitably robust KPIs on all service providers through the terms of its service provider contracts.

**Question 14: Do you have any comments on Chapter 10 of the licence conditions, in particular do you have any comments on:**

- i. **The proposed arrangements applying to Management Orders, including the scope of the powers of the Authority in such circumstances;**

We understand that the provisions relating to Management Orders are intended to provide a set of provisions akin to Special Administration, but without statutory authority and with the Authority in the role of Administrator.

We think that there are general reasons why significant caution should be used in this area:

- (a) There does not appear to be a power for the licensee to challenge the imposition of a management order except by judicial review. This runs the risk of expropriation;
- (b) The Authority (and any directors it appoints) would be in a difficult position as they would owe duties to shareholders and/or creditors and not to the public.

In the circumstances, we recommend that these powers be dropped and DCC special administration provisions inserted in the current Energy Bill. That should gain Royal assent in 2013 and therefore the powers would be ready for go-live.

- ii. **The arrangements proposed in relation to the Business Handover Plan and the process for resolution of matters between the outgoing and incoming DCC;**

In our view, the requirement to elicit views from stakeholders should apply equally to the annual review of the Business Handover Plan as to its original development.

**iii. The scope of matters that the Business Handover Plan should provide for;**

We agree with the proposed scope of matters to be contemplated in the initial Business Handover Plan (BHP). However, in line with our response to Question 14(ii), we consider that stakeholders should be involved in any subsequent review of the contents of the BHP to ensure that they remain suitably aligned with the emerging requirements of the industry.

**iv. The scope of the matters that may need to survive for a period of time to continue to ensure a smooth handover to the DCC's successor and whether the two year timeframe is appropriate; and**

We agree that the proposed list of licence conditions should be subject to a two year period of survival, following the transfer of the licence to a successor DCC. The timeframe should also ensure that the incoming DCC does not inherit unforeseen problems, and that the outgoing DCC does not need to retain relevant working knowledge within its business.

We would be grateful to know the statutory basis upon which the conditions will survive revocation of the licence. The legislation provides for enforcement powers against the holders of licences and it is not within the powers of a licence to alter that unless the legislation provides the necessary *vires*.

If, on examination, there is a gap here, there may be an opportunity to close it through the Prohibition Order or the current Energy Bill.

**v. The proposed approach to Intellectual Property Rights?**

We welcome the approach to the transfer of intellectual property rights. Continuity, both of service and value, will be paramount to benefits realisation, as loss of service could seriously undermine consumer engagement as well as compromising users' operating models. It will also be important to subsequent DCC or service provider procurements that bidders can have the comfort that IPR associated with any systems and processes will be transferred.

ScottishPower  
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