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Smart Meter Implementation Team – Regulatory Design Team
Department of Energy and Climate Change
3 Whitehall Place
London
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01 June 2012

Dear Sir / Madam,

Re. Smart Metering Implementation Programme: Consultation on the Draft DCC Licence and Licence Application Regulations (05 April 2012). Reference: URN: 12D/030.

ElectraLink welcomes the opportunity to respond to DECC's consultation on the Draft DCC Licence and Licence Application Regulations. As the central provider of regulated data transfer services to the retail electricity market, and a provider of code administration services to both the gas and electricity industries, ElectraLink has focussed its response on those areas we believe will be most important in determining the optimal licensing arrangements for the DCC.

In ElectraLink's view it is critical that the Licence governing the operation of the DCC reflects the fundamental rationale underpinning its formation, namely that the provision of a common communications framework for smart meters will reduce the risk, cost and complexity of this major transition in the GB energy market whilst enabling Government policy objectives for carbon reduction to be achieved through consumer engagement and energy efficiency.

ElectraLink considers that the draft Licence goes some way to achieving these objectives.

ElectraLink fully supports the creation of a "thin" DCC and is broadly supportive of the independence requirements within the draft Licence. However, it is critical that the independence regime is not too onerous or wide ranging so as to preclude well qualified bidders. Furthermore the regime should not limit DCC shareholders from providing non fundamental service capability to the DCC. ElectraLink considers that DCC shareholders should be able to provide these service capabilities to the DCC either through the secondment of employees with relevant skills or through a service or 'draw down' contract.

The DCC Licence provides for a regime which is comparatively low risk allowing cost pass through, recovery of the DCC's own costs from Licence award and transparent margins. It places risks with those who are best able to manage them and will help to ensure the DCC's service and financial continuity. ElectraLink wholly supports the DCC maintaining a strong balance sheet/investment grade credit rating and complying with an extensive and regular reporting

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requirement to DCC Users and the Authority. This combination of these factors, plus the brand impact on DCC Shareholders of DCC failure, are in ElectraLink's view sufficient to ensure that DCC Shareholders will retain the necessary equity and interest in the DCC to ensure its ongoing performance. To this end, ElectraLink does not support the proposed requirement for the DCC to lodge a performance bond or other such financial guarantees. Our response below outlines some alternatives to this approach.

ElectraLink continues to advocate the principle, as outlined in our September 2011 consultation response, that until it is robust and stable the DCC should focus on the delivery of Core services to support the mass roll of smart meters. Once this stability has been achieved the DCC should facilitate innovation through the efficient and effective delivery of Elective Services. Thereafter Value Added Services could be considered. However, at this stage critical details such as the quantum of the incentives, the alignment of DCC incentives to both DSP and CSP incentives, margins allowed on Elective Services and more general roll out incentives have yet to be clearly articulated.

There are a number of other areas of regulatory uncertainty in the consultation and to ensure bidders can fully assess the role of DCC, and not include unnecessary risk premiums in their bids, DECC should provide clarity on these as soon as possible. Confirmation is required on the ownership of and responsibility for the communications hub, how registration will be integrated into the DCC, the definition of the Security Standard, who will have responsibility for security assurance and the obligations on the DCC for legacy communication contracts. Finally, clarity on how the DCC is expected to deal with the impact on its profitability and cash-flow of material variances to the expected smart meter roll out forecast is required.

ElectraLink is fully committed to supporting the SMIP and would be happy to discuss any element of this consultation response in more detail with DECC as required.

Yours sincerely

Stuart Lacey

Chief Executive Officer

ElectraLink Ltd

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Questions and Responses

1. *Do you agree with the structure and content of parts 1 and 2 of the Licence?*

ElectraLink broadly agrees with the structure and content of parts 1 and 2 of the Licence. A fixed term licence period is a workable approach. The ability for extensions provides the necessary flexibility to deliver continuity where it can be demonstrated that it is economically advantageous for such extensions to be enabled as well as ensuring the continuity of the knowledge, experience and understanding of the DCC role necessary to support any service provider procurement exercises. Any extensions to the initial fixed term should be achieved through dialogue and negotiation between the Licensee and the Authority, rather than a unilateral extension decision regardless of the notice periods provided.

Regulatory risk is a key element in the assessment of the attractiveness of the DCC Licence and the ability of the Secretary of State to make modifications at any time to October 2018 with similar provisions available to the Authority thereafter creates a regulatory and commercial risk for the Licensee, specifically the potential for changes to the price control arrangements and associated incentive schemes. This high degree of uncertainty could lead to substantial risk premiums being included in bids or in extremis, deter bidders

ElectraLink supports the principle of enduring or surviving provisions. This is a common feature in most commercial contracts

2. *Do you agree with the proposed list of License 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 License 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?*

ElectraLink supports the inclusion of a range of revocation triggers reflecting events of varying degrees of severity

The Licence also details the notice periods which must be given to trigger a revocation ranging from 24hrs notice to 30 days. The notice periods for Emergency Revocation Events and Grant Revocation Event, being 24 hours and 7 days respectively, are reflective of the potentially serious industry impact of the event. For Other Revocation Events the notice period should be extended to allow for the Licensee to take steps such as necessary to remedy the breach. The Licence needs to be clear that should the Revocation event be remedied in the notice period then the revocation is withdrawn

Some of the revocation triggers have implied remedy periods e.g. Revocation Event 2, while others do not reflect any remedy period. ElectraLink would suggest that Revocation Event 5, being ii) above, and Revocation Event 6, being iii) above, should allow for a remedy period before Revocation is triggered.

The boundaries, interaction with and circumstances which would give rise to the Authority exercising its Revocation Rights for Revocation Event 5 rather than exercising its step in rights under a Management Order will need to be clearly defined. What degree of service failure would qualify as a revocation event rather than an event where the Authority would parachute into the DCC any necessary resource to realign service delivery with SEC requirements?

Equally the interaction between any financial security provided by the Licensee (“Relevant sum”) and the Revocation Events will need to be clearly identified and articulated. Will any Revocation Event automatically trigger the payment of any performance bond?

Given the central nature of DCC and its role in handling large volumes of personal data ElectraLink fully supports the ability to revoke in the event of an enforcement order under S.40 of the DPA

3. Do you agree that the DCC License should be issued for a fixed-term only?

Yes as detailed in our response to question 1.

4. Do you have any comments on Chapter 1 of the License conditions, in particular do you have any comments on the drafting of the definitions?

Condition 3 – As highlighted in our response to question 1, the ability to make changes to the Licence, albeit recognising that the exercise of such powers would be subject to caution and following discussion with the Licensee, nonetheless does create a significant regulatory risk within the Licence. The ability to change Condition 5 General Objectives of the Licensee and Condition 18 Charging Methodology for Service Charges are of particular importance as respectively they define the scope of the objectives of the Licensee and the manner in which it can recover costs from DCC users. A change to either of these could significantly impact the risk profile and financial stability of the Licensee. It is critical therefore that proposed changes to either of these conditions are fully impact assessed and allowances are made where necessary.

Condition 4 - ElectraLink agrees with the principles defined in the Licence for the calculation of the fees payable to the Authority as the fees are designed to reflect the regulatory cost of supporting the Licence and are explicitly recoverable at cost as part of the allowed Revenue Calculation.

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

- i) 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;*
- iv) The proposed general and security controls for the DCC?*

The two general objectives echo the ElectraLink position outlined in response to the September 2011 consultation, being that the DCC should be a service provider focussed on the delivery of an efficient and economic service to support the roll out and operation of smart metering (mandatory business) while facilitating the benefits which will be gained from the development, implementation and operation of Smart Networks. The ability to develop elective and value added services should not compromise the primary purpose and paramount nature of the Mandatory Business.

The construct and interaction between Mandatory and Permitted businesses reflect, to a large degree, existing arrangements under other Licensed arrangements and recognises the intent that the DCC should focus on the provision of services to support the smart meter and related energy market. The continuing interest and requirement for Authority approval of Value Added Services will ensure there is an arrangement in place whereby DCC's focus is maintained on its core objectives. It is critical that in the early stages of rollout that the DCC is wholly focussed on the initiation and delivery of the core services within Mandatory business. Once these are established, innovation can be facilitated through Elective Services, both DCC users initiated and DCC initiated. These elective services will be a key component in supporting market initiatives to engage consumers and drive the benefits identified in the Governments business case for smart metering.

ElectraLink supports the inclusion of Minimal Services as this provides a suitable mechanism to allow for the delivery of ad hoc commercial services which do not materially impact the resource necessary to the core functions of DCC.

The DCC will be responsible for ensuring the effective and efficient coordination of the roll out of metering equipment, including the communications hub. An early decision on the ownership and provision of the Communication Hub is necessary as the inclusion of responsibility for this within the Mandatory Business, with delivery via the CSP's, will have a fundamental impact both on the structure of the DCC Balance Sheet and on its enduring service obligations. It is critical that this position is resolved before the Proposal Stage of the bidding process.

The general controls are appropriate to the DCC given its activities and role in the market. The implementation of a risk management and internal control regime will provide the necessary operational assurance to DCC Users that the company is being managed in accordance with good corporate practice. It is noted that the Part A of Licence Condition 7 applies to the DCC as if the DCC were a quoted company. ElectraLink fully supports this approach with regard to corporate governance, risk management and internal control.

ElectraLink would also highlight that the level of reporting as defined in the SEC consultation and the condensing of that into a 4 month period following the end of the financial year could create

a potential bottleneck in DCC. Consideration should be given as to whether this reporting period could be elongated or whether the regulatory reporting requirements could be phased more evenly through the year.

The security controls identified in the Licence in respect of protecting and securing the physical, organisational and information assets of DCC are appropriate and necessary including the obligation to hold ISO 27001 and ISO 27002 accreditation. It is noted that the Authorised Security Standard is still being developed and Government is considering further the associated governance regime thereto. This Standard will need to provide the right level of protection and security of assets but not to such a degree that day to day compliance would impact organisational flexibility and stifle innovation. Further, it is critical that Government has included in the DSP and CSP contracts the parallel security, organisational and control regimes necessary to deliver the ultimate security obligations which DCC will be required to deliver.

The SEC consultation indicates the obligation for delivery of the assurance and compliance framework for the end to end smart meter system will be the obligation of the SEC Panel. It is likely that this will be discharged through the Code Administrator and delivered through a blended approach of in house Code Administrator resource and out-source subject matter experts. ElectraLink supports this approach.

The DCC will be a service provider and will have a number of obligations with regard to its services, which in the main will be delivered through sub contractors, to being wholly compliant with the assurance, specifically the security standard, regime within SEC. This will be particularly pertinent when assessing any changes, or the introduction of new components, to the smart metering system. This will be a key component of the Technical Design Authority role of the DCC.

6. *Do you have any comments on Chapter 3 of the License conditions, in particular do you have any comments on:*
- i) the independence requirements of the DCC and the interaction with the revocation provisions;*
 - ii) the broad condition on protection of confidential information;*
 - iii) the scope and nature of the role of the compliance officer?*

The General Prohibition of any unrelated business or activity and the associated permitted exceptions thereto are resonant of the existing ring-fence obligations within existing licence arrangements in the energy industry and are a workable arrangement.

DCC is likely to be a relatively “thin” organisation with a core set of staff and systems supplemented by bought in resource which will need to flex to meet specific operational needs over its lifetime, for example trialling and testing expertise in the early years. It may wish to secure this necessary resource from its shareholders / consortia members.

The current proposed Licence drafting, specifically the definition of Related Undertaking and Clause 9.9, would appear to limit DCC Shareholders / DCC Consortia members being able to self provide Relevant Service Capability, other than Fundamental Service Capability, through External Service Provider Contract to DCC. However, this prohibition would appear to be relaxed through

Condition 16 whereby self provision is allowable in instances where the Licensee is satisfied that it would be most economical and efficient to do so. We would encourage Government to clarify what criteria would need to be met to demonstrate such obligation. It is crucial that any such obligation should not result in unnecessary cost or delay in the provision of services.

During the bidding process the successful bidder will be chosen as it can demonstrate that it provides the ideal mix of experience, skills and knowledge to deliver DCC's service obligations in the most cost effective and efficient manner. This may be a consortium with members delivering component parts of the composite service requirement.

Bidders will be required to provide a competitive price as part of the procurement process. To ensure competitive advantage in their bid, and reflecting the annuity nature of some of the services, the consortia members are likely to provide better rates than would normally be achieved in an open market environment.

To subsequently preclude the consortium members from providing resource, either through secondment of staff or through a service or "draw down" contract would appear to conflict with the intent of the initial procurement process, being to secure the best candidate to deliver DCC. A structured and transparent contracting arrangement between consortia members will ensure the most cost effective, efficient and timely delivery of services.

Equally, such a committed contracting structure will ensure that consortia members devote significant effort in ensuring the right resource is available at the right time. This would mean that DCC is not open to the risk of the necessary resource not being available in the market when needed. Please refer to our response to Q12 regarding reputational damage on consortia members of not being able to deliver DCC services as and when they are required.

Government will need to be equally specific about the treatment of significant issues of scope which may be unresolved at Licence grant.

ElectraLink supports the arrangements proposed for the appointment of Independent Directors. ElectraLink would propose that the appointment and terms of office for Independent Directors should comply with good practice compatible with that of a quoted company.

ElectraLink supports the condition with regard to protection of Confidential Information. The condition is broadly compatible with those included in commercial contracts.

7. *Do you have any comments on Chapter 4 of the License 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;*

ElectraLink has no comment on this question.

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

ElectraLink support the need for a development plan for the DCC. Providing users and stakeholders with visibility of planned future services and operations will benefit all parties. Whether the time period for the plan is 3 or 5 years, the key will be the need to continually monitor and adjust the plan, especially in the early days of the DCC. The plan must, in the early stages of roll out, focus on providing support to the mass meter rollout in preference to the introduction of new services that may destabilise and detract parties from achieving their rollout plans.

iii) the proposed inclusion of a License condition that would facilitate future transfer of registration to the DCC?

ElectraLink has stated in previous consultations that the incorporation of the Energy Registration Services in to the DCC should be accompanied by the transfer of existing obligations on networks operators to deliver data transfer services. ElectraLink would also like to emphasise that registration should only move to DCC as and when there is demonstrable benefit to end consumer in providing an improved switching process and there is a definitive 'single version of the truth' with regards to registration data items. It must also be noted that there will be an ongoing requirement for legacy registration systems which support smart meter systems not supported by DCC, e.g. non domestic, and given the integrated nature of registration systems within network operators in support of revenue and billing purposes.

8. Do you have any comments on Chapter 5 of the License 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;

ElectraLink fully supports the requirement for the DCC to procure both the DSP and CSP service requirements. These contracts form the key components necessary, as well as the material cost element, to deliver the smart metering system and therefore should be open to full competitive procurement. This will ensure that best value is achieved but equally will allow the market to provide the most appropriate technical and service solutions to support mass roll out and ongoing service delivery as well as innovation. As noted in our 2011 consultation response, best value is achieved through placing risks with those most appropriate to manage such risks.

ElectraLink supports the requirement for DCC to demonstrate that it complies with best practice procurement objectives. ElectraLink fully supports Government's recognition that DCC may be best placed in some instances to provide key elements of the Relevant Service Capability, either through in house resources (i.e. employees and internal systems) or through bought in services from its consortia members. The Licence will require the DCC to demonstrate that in such instances that it is satisfied it is more economic and efficient to do so than competitively procure.

The consultation recognises a number of corporate structures which the DCC Licensee may take including a single organisation capable of delivering all the functions or a joint venture. In each scenario the bidder will need to demonstrate that it, either solely or through its consortia partners, has the ability to deliver all the service requirements of DCC. Central to any consortium bid will be a contracting framework between the consortia members which allows for each consortia member to provide services to the DCC. This contract would provide the necessary

governance to ensure such services are provided to the requisite quality, service levels, and expertise requirements as well the rates and prices for such resource and services. These would be “draw down” contracts. This contract structure will provide the necessary governance to ensure services are provided commensurate with market conditions as well as assure and provide evidence to the other consortia members that a fair and equitable position is maintained between consortia members.

Please refer to our response to question 6 where we discuss how the potential legal drafting may inadvertently exclude consortia partners from providing services to DCC. We would again reiterate that there are significant benefits from allowing consortia members to provide services to DCC without encumbrance. Any dilution of this could lead to well qualified bidders from choosing not to bid.

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;

ElectraLink has no comment on this question.

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;

ElectraLink has no comment on this question.

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

ElectraLink supports the categorisation of services into which the DCC will be required to deliver and those it will be permitted to deliver, with the latter subject to the necessary permissions being given by the Authority. Two key areas which are still under consideration are the provision of service to non compliant meters and the obligations for provision of the communications hub. These will have significant impacts on the overall service delivery obligations of DCC and as such it is critical these are resolved prior to the Proposal stage of the procurement process.

ElectraLink believes that the timeframes outlined in the response for first and second stage responses to requests for Elective service appear reasonable recognising that flexibility exists for any service requests of a complex nature.

ElectraLink also supports the ability of DCC to provide Value Added Services subject to a number of criteria being achieved. The initial focus of the DCC will be on establishing a robust operating platform to enable the roll out and ongoing support and delivery of the smart meter system. It is only when this necessary robustness and stability is achieved that Value Added Services should be contemplated.

ElectraLink believes that Elective service provision will allow a channel for innovation, be it promoted by SEC Parties or the DCC. Such services and their associated innovation must not be hampered by an overly restrictive governance regime and the proposed regime of defining base terms within the SEC supplemented by bilateral contracts is a workable solution. This governance

model exists in relation to the Data Transfer Network provided by ElectraLink to the energy market, for example allowing for elective additional services to be provided to individual or sub sets of Data Transfer Service Users.

The initial focus of DCC must be on delivering Core services with Elective services only initiated once the operating platform is stable and scalability has been demonstrated. However, Elective services could be initiated in a much sooner timeframe than Value Added Services.

ElectraLink continues to endorse the position that DCC should act and operate as a service provider to the industry and exhibit the necessary culture and commercial behaviours commensurate with that.

v) The charging methodology provisions, particularly the objectives of the methodology?

We are in general agreement with the principles underlying the charging methodology and statement. We note that in order to avoid undue risk to DCC the structure of its costs under the DSP and CSP contracts currently under negotiation, which are likely to be the majority of its costs, need also to be as consistent as possible with the proposed charging methodology and any prospective charging statement constructed to conform to that methodology. We note that postage stamp charging for domestic users is the specific instance where this consistency may be more difficult, and early sight of DSP and CSP charging structures will be essential to achieving a full understanding of their potential impact on DCC.

9. Do you have any comments on Chapter 6 of the License 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;*
- ii) Whether the DCC should have a License obligation to maintain and keep in force the SEC;*
- iii) The proposal to allow the Secretary of State to block SEC modifications in the period up to 31 October 2018; and*
- iv) The way in which interoperability should be addressed through the SEC objectives?*

The SEC objectives as set out in the draft DCC Licence appear to strike the balance between ensuring the effective and efficient operation of the DCC and Smart Metering processes, the need to facilitate and promote competition and protect the interest of consumers.

There is a need for regulatory oversight of the Smart Energy Code and its ongoing development and it would seem appropriate that this is delivered through the DCC Licence conditions. It is also important that no one party or class of parties has undue influence within the governance arrangements, restricting the DCC to a non-voting member of the SEC Panel ensures this is not the case.

We agree that it is pragmatic to allow the Secretary of State to block SEC modifications in the period up to 31st October 2018 in the limited circumstances set out in the draft licence. However, it is difficult to see how any modification that would have a detrimental impact on the

wider smart metering programme and therefore require these powers to be used would have gained Authority approval as better serving the SEC objectives.

ElectraLink believes that the SEC objectives as currently drafted are sufficient to cover the issue of interoperability. The combination of objective 1 (to facilitate the efficient provision, installation, and operation of Smart Metering Systems at Energy Consumers' premises within Great Britain) and objective 3 (to facilitate effective competition between persons engaged in, or in Commercial Activities connected with, the Supply of Energy under the Principal Energy Legislation) provide adequate scope for the consideration of interoperability issues when assessing modification proposals.

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*
- 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?*

ElectraLink has no comment on this 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?

The consultation document rightly highlights that the licence condition 23.12 as currently drafted would give the Authority broad powers to bring forward modifications. The use of those powers in circumstances other than following a Significant Code Review could give rise to conflicts with the Authority's role as decision maker under the SEC modification process. This will require careful consideration during the legal drafting of the SEC modification process to ensure the intent of the licence condition is maintained.

12. Do you have any comments on Chapter 7 of the License 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?*

The size and nature of the guarantees required is clearly an important issue in avoiding deterring otherwise well qualified licence applicants.

Ultimately, financial stability depends on the forecast relationship between cash flow uncertainties and balance sheet strength; this is equivalent to a major element of any Rating

Agency assessment. Shareholders should have a strong interest via the balance sheet. The cash flow projections and the assumptions on which they are based must be available to DECC as the licence competition proceeds. The forward looking certificates of financial adequacy and other licence provisions, which go considerably beyond those normally given by companies without such a unique and vital role, should give adequate assurance that an initially financially sound licensee remains so. Depending on the quantum of forecast cash flows following this assessment, and given shareholders' ongoing financial commitment within the company's balance sheet, it may emerge that no further guarantees are required.

ElectraLink supports the requirement for DCC to be subject to an external financial stability assessment and the requirement to obtain, or demonstrate equivalence with, an investment grade rating standard. Clarification of the allowed revenue formula, giving cost pass through, a cap and collar on margins and performance incentives switched off until after Go Live or beyond have all successfully contributed to what may be argued as a relatively low-risk business, given the context of significant uncertainties within the overall programme. Information on DSP and CSP contracts should be available later in the bidding process. Each of these will contribute to the achievement of such a rating.

The remaining obstacles to making a reasoned assessment on the size of necessary guarantees would be decisions on major issues of scope (and how to treat any still outstanding on licence grant), albeit the proposed regulatory arrangements also go some way towards dealing with these uncertainties.

ElectraLink does not believe there is a need for an additional financial security requirement, specifically the need to provide a Relevant Sum through a performance bond and notes that neither the Draft Licence nor the consultation gives any indication as to the value of such bond or the circumstances in which it can be claimed as well as who can claim it. The Licence as drafted does not contain any termination for convenience provisions nor does it allow the Licensee to walk away from its obligations. However, as part of their consideration of this opportunity, bidders will place significant negative value on reputational damage to established brands should they fail to deliver their service obligations. ElectraLink would encourage Government to consider alternatives to a performance bonds, for example the provision of negative pledges in respect of balance sheet strength.

Given the cost pass through arrangements, and the protections elsewhere in the conditions that allow regulatory interventions against wilful or less culpable DCC management shortfalls that could lead to licence revocation, it is very difficult to envisage any circumstances in which revocation is likely. Having had sight of the current draft licence, and given an ongoing equity interest in the company ensured under the licence terms, which could be forfeit in the event of licence revocation, our view would be that no additional guarantees relating to the costs of securing an alternate DCC provider are required.

13. *Do you have any comments on Chapter 9 of the License conditions, in particular do you have comments on:*

i) The need for the revenue restriction conditions in the DCC License to evolve as the DCC's role changes;

We believe the structure of the price formula is appropriate, in particular the separation of pass through costs and baseline margin from incentives which can be switched off or on at appropriate times during the programme.

ii) The need to incentivise the DCC to concentrate on achieving programme milestones at the beginning;

It is right to maintain DCC's initial focus on activities that contribute to meeting go live in this way.

iii) The proposal that the DCC's internal costs should be passed through with a (£/annum margin applied

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

It is also right to allow pass through of costs in the early stages of the programme where unit costs and service scope and volumes are uncertain and largely out with its control. This lifting of uncontrollable risk from DCC also helps to ensure its ongoing financial stability.

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

The potential for bad debt clearly needs to be managed, principally by managing late payers to ensure such overdue debts do not turn into bad or doubtful debt. Amongst DCC's larger users there have been few instances of catastrophic financial failure and an accommodation for the continued provision of services is quickly reached, although the loss of a few months' revenues from the largest users may be significant in DCC's terms. Individual small users are unlikely to result in material bad debt. Whilst acknowledging that it would only be applied if DCC had failed to apply prescribed credit management measures, the weighting or a capped value for this in 'K' and specific instances of excluded bad debts, e.g. administration or liquidation, should be made explicit rather than at Ofgem's absolute discretion and need only be larger than the costs incurred by DCC in properly managing User's credit in order to provide an incentive.

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

ElectraLink is accustomed to operating contracts with its users in the gas and electricity industries and with its suppliers that feature a large range of KPIs and usually carry liquidated damages for non performance. These fall into the more obvious generic subheadings below

technical, governance and company services, as enumerated by DECC, but need to be detailed to be meaningful – we have contracts with several hundred individual KPIs, of varying importance to users. We anticipate such a schedule will exist under SEC, but are unclear how this would be simplified for the purposes of the regulatory formula except under a ‘totting up’ of failures under weighted headings of timely provision of service availability following request, timely delivery of data traffic, % availability of service, and timely turn-around of change requests and regulatory reporting. In broad terms the two critical KPIs which should apply are a measure of the availability of the smart meter system and the responsiveness of the smart meter system to service requests.

In general, incentives within DCC’s pricing formula should not place any, or any significant, weight on programme roll out timings and patterns beyond go-live where it has little influence; DCC ‘volume’ incentives should be based on the timely provision against demand for individual services rather than volumes per se, and then as a separate item only if not already captured alongside other service quality metrics in KPIs. Although it is understood that there may be a general sense of ‘we’re all in this together’ gained from an overall volume incentive, the weighting should not be great as DCC has little control over roll out as a whole. In particular, DCC’s incentive penalties on milestones prior to go-live must be aligned with those of its main suppliers in the DSP and CSP contracts.

Although greater knowledge of some costs will be gained during the bidding process, major uncertainties are likely to remain. It is unclear how the take on of legacy contracts, any involvement in managing the Communications Hub and other aspects of the HAN, and most obviously perhaps, registration, will affect DCC’s scope and activity levels. Although internal cost pass through helps with risk, specifying DCCs role in such matters as soon as possible will help in the assessment of the reasonableness of DCC bidders profit expectations in the ‘BM’ term, given a £/annum figure is expected. Alternatively, DECC may wish to remain open to a tiered submission of £/annum figures depending on the final scope of DCC.

One key area in pricing risk will be the calculation of charges based on expected meter enrolment volumes and the corresponding infrastructure build profile. Any material deviation from the forecast roll-out numbers will significantly impact costs, both for the DCC and its sub contractors. This in turn will have working capital and cash flow impacts. ElectraLink would recommend that this matter is given further consideration.

The take on of Registration is acknowledged as a particular uncertainty, to be dealt with by an Ofgem Review. We believe such a review may be materially simplified if Registration is dealt with by a separate regulatory term; such a term may well have components that mirror those of the current formula relating to cost pass through, margin and incentives, but would be particular to registration which is a distinct activity. The remaining terms of the primary regulatory formula could thus be left undisturbed barring any review of KPIs for the initial services prior to their switch on, the appropriate time for which may vary from that of registration take on.

In respect of External Contract Gain Share, the Consultation refers to DCC setting out the details

of the gain and a proposal in terms of sharing, but refers to reductions in costs only arising from DCC's initiative rather than service providers' contractual conditions. The contracts negotiated with both the CSPs and the DSP must make provision for efficiencies to be gained, specifically the trade off between cost and universal service provision / coverage. DCC's initiatives may aim precisely at changing service providers' contractual conditions by agreement prior to their re-procurement, as well as at re-procurement. We suggest that DCC's proposal should be able to include any benefits, short or long term created through their negotiations i.e. enhanced services or new services at no price increase, or reduced services through deleting redundant service lines with a cost reduction.

"Communication Services are provided by the Licensee under paragraph 17.2 of the draft License (including, in particular, as to price and volume) are to be those that are prescribed by the SEC for the provision of Core Communication Services". Ditto under 17.13 for the enrolment service. It should be made clear that the SEC Panel has no veto on prices, which would be inappropriate given that DCC must fix prices in accordance with a charging methodology and charging statement and so as to recover its allowable revenues, all of which will have received advance notification to Users and/or Ofgem. It does seem appropriate that the SEC Panel should be able to raise any dispute with DCC on prices and charging structure with Ofgem on behalf of users, with users retaining the right to raise a dispute individually if the SEC Panel declines to do so.

14. *Do you have any comments on Chapter 10 of the License 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;*
 - ii) The arrangements proposed in relation to the Business Handover Plan and the process for resolution of matters between the outgoing and incoming DCC;*
 - iii) The scope of matters that the Business Handover Plan should provide for;*
 - 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*
 - v) The proposed approach to Intellectual Property Rights?*

ElectraLink has no comment on this question.

15. *For the initial License application, do you agree with the Government's intention to apply the BAFO stage in all circumstances, so as to mitigate the risks associated with the changing requirements and improve the competitive outcomes?*

ElectraLink has no comment on this question.

16. *Do you agree with the proposal not now to include a fast-track process to appoint a temporary DCC, but instead to rely upon the provisions for intervention to keep the DCC's service functioning whilst a standard licensing application process is conducted to appoint an enduring successor DCC?*

ElectraLink has no comment on this question.

17. *Do you have any comments on the proposed competitive application process for the DCC License and, in particular, on the Government's stated intention to operate an extensive 'best and final offer' stage for the first License competition?*

ElectraLink has no comment on this question.

18. *Do you have any comments on the draft DCC License application regulations and, in particular, whether they effectively implement the proposed competitive application process described in this consultation document?*

ElectraLink has no comment on this question.