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20/12/2023

Dear Ayena,

DCC review: Phase 1 Consultation

Thank you for the opportunity to respond to Phase 1 consultation for the review of the regulatory arrangements for the Data Communications Company (DCC).

We welcome Ofgem's review of the regulatory arrangements for the DCC for the period 2025 to 2040 and the opportunity to participate in any workshops. Electricity Distribution Network Operators (DNOs) collectively pay towards 6% of the DCC costs, and we are a key stakeholder in both the roll out of the Smart Metering Implementation Programme (SMIP) and Switching Programme. As an existing user of DCC services for the DCC smart metering network and the Central Switching Service (CSS), it is vital these core DCC services that we and our customers receive are effectively delivered and are value for money, now and in the future.

Achieving Net Zero will involve transformational changes to what customers and stakeholders need from Ofgem regulated entities. Regulation will need to be able to accommodate meeting these developing needs, as well as factors such as technological evolution, so this proposed DCC review is timely.

We recommend the following transformational changes for the future role of the DCC whereby Ofgem:

1. investigate separating out the core mandatory services (smart metering, switching and any other significant code reform changes) into individual licences each independently competitively tendered – to better promote competition, encourage innovation and improve cost efficiency for customers; and
2. allow DCC (or other nominated parties) to schedule retrieval of all half hour consumption from meters, store this data securely, and then provide services to allow all parties to access the data from a central repository without the need to actually contact the smart meter itself. This would have the significant advantage of reducing Communications Service Provider (CSP) network congestion in all regions, improve data retrieval success rates and

potentially reduce the amount of new DCC investment required to meet future network capacity needs.

Appendix 1 provides our detailed responses to each of the consultation questions.

I hope these comments are helpful. Please do not hesitate to contact me or Catherine Duggan (07775 547624) if you would like to follow up on any particular aspect of our response.

Yours sincerely,

Paul Auckland
Digitally signed by Paul Auckland
Date: 2022.12.20 14:47:31 Z

Paul Auckland
Head of Economic Regulation

Appendix 1 – ENWL detailed responses to each of the consultation questions

The following table includes our views on the call for evidence:

<table>
<tr><th>Ref</th><th>Question</th><th>View</th></tr>
<tr><td colspan="3">Section 1.10 – Alternative regulatory models</td></tr>
<tr><td>1</td><td>Which of the two broad models do you think we should adopt as the basis for our design of the future regulatory framework for DCC and why? What are the features of your preferred option that lead to you to this choice?</td><td>We recommend Option A is adopted, whereby, the DCC is owned by a third-party shareholder appointed by competitive tender (a similar approach to the current DCC regulatory framework) but with a redesign of the current model to introduce changes to some of the following key parameters by introducing:
• <u>an ex-ante price control</u> for established ongoing operational costs of sufficient certainty – which is a similar model for Distribution Network Operator price controls.
• <u>improved accountability to DCC customers</u> via governance reform with customer representation on the DCC Board.
• <u>new financial incentives</u> – so the DCC is focussed to:
– deliver quality and cost-effective services,
– anticipate and manage change to its network capacity and capability; and
– share in pain or gain based on the extent to which users' needs are met or not.

The features of this option that lead us to this choice are:
• improved value for money through reform of the price control and incentives,
• accountability to Ofgem under the licence and through price control; and
• allowing the DCC role to evolve in an uncertain environment and to best navigate towards a pathway to net zero carbon – flexibility built into a new price control via ex-ante re-openers.</td></tr>
<tr><td>2</td><td>Do you agree with the way we have applied the principles in our analysis of the options? Please state your reasoning.</td><td>Yes. We agree with the way the principles have been applied to the analysis of the options.</td></tr>
<tr><td>3</td><td>With regard to Option A, to what extent do you think that changes to the DCC licence alone could provide incentives that result in a third party investor-controlled DCC Board providing the quality and cost of service that DCC customers require, and managing DCC effectively?</td><td>Whist changes to the DCC licence to introduce an ex-ante price control approach is a significant improvement and appropriate, this would not be enough of a catalyst on its own to provide the quality of service that DCC customers require. A fundamental hearts and minds shift is required from the owners of the DCC to be more customer-centric and consumer focused. Active holding of the DCC licence holder to account by its stakeholders and Ofgem, including Ofgem undertaking effective monitoring and taking enforcement action where appropriate is all required.

We are particularly concerned about the lack of responsiveness to customers and poor stakeholder engagement, which we believe an evolved licence and regulatory framework would address. We give examples of poor stakeholder engagement in our response to the Ofgem's DCC Price Control RY21/22 consultation.</td></tr>
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4	**With regard to Option B, how effective do you think a non-profit-making, stakeholder-controlled or independent DCC Board would be in providing the quality and cost of service that DCC customers require, and managing DCC effectively?**	Whilst we recognise there could be some benefits in a non – profit publicly owned model with a stakeholder-controlled or independent board, there is also the risk of weak incentive to control costs borne by all users equally. Also, a public body may struggle to effectively protect all groups of DCC customers, so no one group of stakeholders can exercise undue control or influence. Whilst a private body we expect will be able to make more optimal decisions for stakeholders and tend to act more quickly. On balance we believe Option A will be more effective than Option B, in providing the responsiveness, quality and cost of service that DCC customer require, for the reasons set out in our response to Q1.
5	**Do you have any views on the details of Options A and B?**	Yes, if Ofgem determine Option B is the preferred approach we would recommend that Ofgem take the same approach to the current Elexon ownership review and the DCC is owned by a subset of funding parties. For the DCC, we recommend the Electricity and Gas Suppliers would be the owners as is appropriate as the core funders of the Smart Energy Code (SEC) and the Retail Energy Code (REC). However, to protect against the risk referred to in our response to Q4 (regarding no one group of stakeholders can exercise undue control) that (as is the model for the REC) that Ofgem approve budgets and should have power of veto if they aren't satisfied that the costs are being incurred efficiently.
Section 1.11 – Transition period considerations		
6	**What are your views on the options identified and the associated trade-offs for a possible licence extension?**	Our preferred approach is Option 1 for a new framework and successor Licensee to be in place by September 2025. This will ensure the benefits of the new framework can materialise early. However, we recognise there could be allowances for an extension of up to 6 months to a year which would fit better with Option A (our preferred model) to allow for a more competitive retender and a lower risk change from business handover and to effectively close out the last price control period. We do not recommend an extension of beyond one year as set out under Option 2 and 3 as this would have a negative impact on continued effective governance, would excessively delay the realisation of benefits from the new framework and would likely require the introduction of interim changes. We suggest much more urgency and priority be accorded to reforming and executing the change process for these arrangements. For example, this consultation was we think unduly long, particularly compared to the draft determination consultation on the whole ED2 price controls which was only 8 weeks over summer 2022. We support Ofgem having resources to take this DCC review process forward.
7	**What are your views on the assumptions we have made for Options A and B transition periods?**	We agree that an Option B type framework could require a longer period to facilitate transition than Option A and gives further weight to the recommendation for Option A to be adopted. We also agree under Option A it is possible to phase in elements of the future framework within the extension period but recommend the target should be for full phasing by a maximum of 1 year. See our response to Q6 for the relational for not exceeding a transition period of 1 year.
8	**In your view, which of the considerations we have identified for the transition period are**	Yes. Another dependency that should be considered is for the introduction of market-wide half hourly settlement as part of the Ofgem Signiant Code Review. Whilst we recognise the plan is for the outputs from the MHHS SCR to be live before the start of the new

	the key dependencies and why? Are there any other dependencies that should be considered?	license period, lessons learnt from the Switching SCR could result in delays to the go live data and/or an early life support period which could overlap with any DCC transition period.
9	**What is your view on implementing incremental changes to the regulatory framework during a transition period? Which parts of the regulatory framework would be most suitable for such changes and why? Do you have suggestions for their implementation?**	Yes. We would welcome ensuring that interests of both current and future SEC parties are protected if the SEC Panel is disbanded under energy code reform and industry code parties no longer have a decision-making role. We recommend caution before disbanding the SEC Panel. After a period of bedding down, and following concerns raised and feedback from industry parties, the RECCo have listened and now reinstated a REC Issues Forum (previously a similar group was adept at discussing party issues and raising changes which benefits users and customers at the MRA Issues Resolution Expert Group under electricity codes). In general, reviewing the experience through other code reforms should be a consideration into this DCC review.
Section 1.12 Future role of DCC		
10	**Do you agree with our proposed scope of future DCC's Core Mandatory Business?**	No. The mandatory business of the DCC should go beyond just delivering smart metering. We believe the core services should be defined as: • smart metering, • switching, and • potentially half hourly (dependent on the final design from the SCR) and any other mandatory service as a result of a Significant Code Review in the future. We see no rational for why services instructed by the Authority of the Secretary of State should not be categorised as a core mandatory business. We recommend Ofgem investigate separating out these core mandatory services into individual licences each independently competitively tendered – to better promote competition, encourage innovation and improve cost efficiency for customers.
11	**Should the future framework permit DCC to carry out any services additional to its Core Mandatory Business? What are your views on the concepts of 'mandated services', 'ancillary services' and 'additional services to users'?**	Yes. We agree the DCC should be able to carry out additional services to its Core Mandatory Business, but this should be based on the following provisos and prioritised in this order: 1. the DCCs focus should be on delivery of their core mandatory business services and ensuring this works whilst addressing any imbalances (in technology or capacity) between the regions, so as to create an even playing field. 2. introduction of new DCC incentives and any checks and balances on the DCC developing new services should be reviewed. Including how non-core activities to develop other revenue streams are funded and delivered and what if any benefits flow back to core service DCC customers, if these new services are successful. 3. there must be appropriate and significant benefits likely to accrue to existing service users, and it must not cause additional costs to pop up on core mandatory business services funded by users.

12	**Do you agree with our proposed drivers for a controlled change in DCC's role? What are your views on the ways in which evolution of DCC's role can be managed?**	Yes. We agree with the inclusion of an uncertainty mechanism in the framework to allow for a controlled evolution in DCC's role. We strongly recommend in parallel the DCC is also incentivised to anticipate and manage change to its network capacity and capability both now and as its role evolves. See our response to Q13.
13	**Do you agree that the future framework should enable exploration of re-use of DCC's infrastructure? What are your views on the specific conditions and measures that may need to be in place to enable it?**	It has been acknowledged by the DCC, BEIS and Ofgem that there are performance constraints with the provision of the CSP North service when dealing with peak usage loads and also when attempting to retrieve large payloads of data from meter devices. Unless whole system requirements are considered as part of developing the solution for future use (such as the introduction of MHHS) there is a high risk that contention for data and CSP network resources will result in further degradation of CSP North network performance. The current archaic framework encourages large volumes of data to be sent and requested by multiple parties across a network relying on outdated communications technology. The optimal model would be to allow DCC (or other nominated parties) to schedule retrieval of all half hour consumption from meters, store this data securely, and then provide services to allow all parties to access the data from a central repository without the need to actually contact the smart meter itself. This would have the significant advantage of reducing CSP network congestion in all regions, improve data retrieval success rates and potentially reduce the amount of new DCC investment required to meet future network capacity needs.
Section 1.13 price control change considerations		
14	**Do you consider that a hybrid model, where some costs are regulated under an *ex-ante* regime and some under an *ex-post* regime based on the level of cost uncertainty, would be appropriate for DCC?**	Yes. We consider the core mandatory business services for smart metering and switching to be certain and as such be subject to an ex ante regime. We would welcome Ofgem setting out which costs it considers uncertain and as such would fall under the ex-post regime.
15	**What elements of DCC's Allowed Revenue are stable (with low risk of forecasts being either under- or over-estimated) and would benefit most from an *ex-ante* approach by 2025?**	See our response to Q14. We consider the core mandatory business services for smart metering and switching to be certain and as such be subject to an ex ante regime.
16	**What are your views on the different ways in which risk (ie the benefit of underspending and the cost of overspending) can be shared between the DCC and its customers under an *ex-ante* regime?**	In the absence of a better regime we recommend the DCC is modelled on the RIIO-2 price controls whereby an efficiency incentive rate or 'sharing factor' in order to determine how the risk of any overspend or underspend is shared between the regulated entity and its users.

17	**What are your views on whether DCC can be effectively incentivised to reduce costs at scale under an *ex-ante* regime?**	Despite, the DCC business activity being asset light and predominately the management of large external contracts with service providers we believe there is sufficient scope for a revised model to effectively incentivise the DCC to reduce costs due to the scale of operation of the DCC and exponentially increasing costs.
18	**Do you think that moving to an *ex-ante* regime could adversely affect the quality of service? What mechanisms could be used to reduce the risk of underperformance under an *ex-ante* regime (eg provisions to allow clawback in case of delivery failing to meet specifications)?**	No. We agree that appropriate incentives to deliver the right quality of output could be designed and implemented under an ex-ante regime. DNOs operate under an ex-ante price control. The DCC total reported allowed revenue costs for the RY 21/22 were £502m which is ~18 % more than the allowed revenue of £424m for the whole of ENWL (for the same period and which was subject to an ex ante model) owning, developing and operating the electricity distribution network that distributes around 10% of Great Britain's electricity.
19	**What are your views on how best to assess costs under an *ex-ante* approach? For example: What level of detail on costs and benefits would be appropriate? How early should DCC share details of costs with customers? How should this information be shared and evaluated?**	A consulted upon and published DCC business plan will provide stakeholders with cost allowances and justification before the cost are incurred. However, a step change is needed from the DCC regarding its poor track record in stakeholder engagement and acting upon customer feedback regarding its planning. We consider a Totex incentive mechanism and other incentives, taking the RIIO principled approach applied to network regulation is a good starting point. See our response to Q3.
20	**Do you agree with our initial view that an *ex-ante* model has the potential to reduce the resource burden both for Ofgem and DCC? Please state why.**	We are unable to answer this question as we do not have sight of all the commercial sensitive data the DCC sends Ofgem and BEIS or redacts from their published price control documents. However, we can understand how a hybrid regime (under which certain aspects of the DCCs allowed revenue are subject to ex-ante price control whereas others remain within the ex-post framework) could be resource intensive all parties. A such we recommend clear thresholds for justifying why any aspects should remain within the ex-post framework. In general, greater transparency would help increase scrutiny and data transparency is a direction the whole industry is moving in. How far the transparency goes should be guided by protecting consumer interests and balancing the costs and benefits of providing greater transparency. See our response to 14.