SEC
Smart Energy Code

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Consultation on the Successor Licensee's Regulatory Instructions and Guidance (RIGs)

Dear Jakub,

The SEC Panel welcomes the opportunity to respond to Ofgem's consultation on the Successor Licensee's Regulatory Instructions and Guidance (RIGs).

We welcome the opportunity to engage with Ofgem on this important development and are broadly supportive of the proposals to enhance cost transparency, introduce ringfenced Service Family budgets, and transition to an ex-ante cost control regime. Our response includes specific recommendations to strengthen cost predictability, improve the alignment between cost assumptions and actual rollout behaviour, and consider the potential for future volumetric charging approaches.

We look forward to continued dialogue as these reforms are implemented, and to ensuring that the new RIGs deliver robust oversight, fair cost allocation, and long-term value for SEC Parties and consumers.

If you would like to discuss any aspect of our response in further detail, please don't hesitate to contact Oli Meggitt, Senior Strategy Manager (oli.meggitt@seccoltd.com) or consultations@seccoltd.com.

Yours sincerely,

Angela Love

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SEC Panel Chair

Q1: What are your views on our proposed changes to reflect the shift from ex-post to ex-ante reporting? How many RYs of historic costs in the current Licence should be reported in the SL RIGs?

We support the principle of moving to an ex-ante cost control regime as it can provide greater cost certainty and predictability for the Successor Licensee and, ultimately, for SEC parties (and by extension of this, consumers). This proactive approach to cost control aligns with good regulatory practice by establishing clear allowances upfront.

However, we would welcome further clarity on how the ex-ante regime will handle cases where actual rollout behaviour deviates significantly from the assumptions used to set the allowances. For instance, the retirement and replacement of meter cohorts may not follow projected trajectories, and without a mechanism to adjust for this, cost predictability could be undermined. We therefore recommend that the cost control framework includes a means to reconcile actual supplier rollout behaviour with allowed cost recovery, to avoid significant mismatches or unintended under/over-recovery.

Regarding the reporting of historic costs, while understanding the value of historical data for trend analysis and assessment, the number of Regulatory Years of historic costs required should be carefully balanced against the practicalities of data collection and the relevance of older data in an evolving environment. A focused period of perhaps the last 3 RYs would be sufficient to establish trends and provide meaningful context without imposing an excessive reporting burden, particularly given the shift to a new control regime and potential changes in the DCC's operations and services. Any costs going back many years will have less relevance as time passes.

Q2: What are your views on our proposals to introduce Service Families and ringfenced budgets at the Service Family-level? Do you agree with the structure of the Service Families?

We generally support the introduction of Service Families and ringfenced budgets as a mechanism to enhance transparency and accountability for External Costs. This approach has the potential to provide clearer insights into the allocation and management of significant cost drivers within the DCC's operations. The concept of grouping contracts that deliver a common functionality or service appears sound.

Regarding the proposed structure of the Service Families (SMETS1, SMETS2, 4G and Connectivity, Centralised Registration Service (Switching), Meter Data Management, Privacy and Security, Service Management, and Testing Services), we believe that, at a high level, these categories seem logical and reflective of the core services provided by the DCC. However, we would emphasize the need for clear and consistent definitions of what falls into each SF to prevent ambiguity and ensure accurate reporting. We also highlight the importance of clearly defining how inter-Service Family dependencies and cost reallocations (e.g., Change Requests impacting multiple SFs) will be managed and reported to ensure full transparency and avoid double counting.

We also encourage Ofgem and the DCC to consider the role of volumetric charging as a potential future mechanism to improve fairness and transparency in cost allocation. By linking charges more directly to usage (for example, by cohort or service consumption), volumetric charging could help align cost recovery with actual service utilisation, and better reflect the benefits derived by each party.

Q3: What are your views on the proposed replacement of Cost Centres by Internal Functions and changes in Ledger Code reporting? Do you agree with the proposed Internal Functions? Do you agree with the split of External Services into separate resource and non-resource GL codes?

We acknowledge the intent behind replacing Cost Centres with Internal Functions and refining Ledger Code reporting to better reflect the DCC's organisational structure and provide greater clarity on internal resource allocation. The proposed Internal Functions (e.g., Chief Technology Officer, Service Delivery, Operations, Chief Financial Officer, Commercial, etc.) appear to represent key operational and corporate functions within the DCC. We believe that this shift has the potential to offer more insightful reporting on internal costs, provided that the definitions of each function are robust and consistently applied over time to maintain traceability.

We support splitting External Services into 'External Services (Resource)' (ESR) and 'External Services (Non-Resource)' (ESNR). This helps distinguish resource-based costs, which can be reallocated across projects, from non-resource costs, which are tied to specific Service Families. This clearer reporting improves transparency and cost efficiency assessment.

Q4: What are your views on the ways in which application of Uncertainty Mechanisms would be captured in the SL RIGs? Do you agree with the separate reporting of costs subject to Automatic Adjustments?

We recognise the necessity to introduce clearly defined Uncertainty Mechanisms as these are required for managing unforeseen cost fluctuations and ensuring the DCC's ability to adapt to changing circumstances while maintaining financial stability. However, we emphasise that the primary goal should be to minimize their use, thereby providing greater cost certainty and predictability for SEC parties and the wider market.

We agree with the separate reporting of costs subject to Automatic Adjustments. This segregation is vital for transparency, ensuring that volume-driven costs, contractual indexation, and pre-agreed adjustments are clearly distinguished from other cost elements. This allows for a more focused assessment of DCC's cost management.

Q5: Do you agree that Supplementary Schedules should become part of the RIGs templates? What are your views on the proposed list of required information? Do you agree that the Licensee should have the flexibility to report the information in format of its choosing, so long as the information is accurate and complete?

We agree that Supplementary Schedules should become a formal and integral part of the Successor Licensee RIGs. These schedules provide essential detailed information that complements the aggregated data in the Main RIGs, allowing for a more comprehensive understanding of DCC’s costs and operations. We support the proposed list of required information, finding it crucial for effective regulatory oversight. While allowing the Licensee flexibility in reporting format is acceptable to reduce burden and leverage internal systems, the information must always be accurate, complete, and readily usable for analysis.

Q6: Do you agree with the proposed bridging of accruals vs cash-based reporting? Are there other factors which may need to be accounted for?

We agree with the proposal to require Successor Licensee RIGs to be reported on an accruals-basis with an additional report showing the cash view used for charging purposes, along with a bridge between the two. This dual reporting approach is essential for providing a comprehensive financial picture. Accruals-based reporting offers a more accurate representation of the economic performance and cost incurrence over a period, which is vital for regulatory assessment of efficiency and allowed revenue. Conversely, the cash view is critical for understanding the actual cash flow and its implications for charges to SEC parties. The 'bridge' functionality on tab 3, with the proposed additions and removals, is a positive step towards ensuring transparency between these two perspectives.

Regarding other factors that may need to be accounted for, we suggest the following should be considered:

- Working Capital Movements: Reconciliation of working capital changes between the accruals and cash views should be provided, as these can significantly impact cash flow but might not be immediately apparent from accruals alone.
- Impact of Capex vs. Opex Treatment: Ensure clarity on how different classifications of expenditure are reflected in both accruals and cash reporting.

Q7: Do you have any other comments or suggested areas for changes or improvements?

Stakeholder Engagement and Review Process: We encourage Ofgem to maintain an open and transparent engagement process with SEC parties and other stakeholders following the implementation of the new RIGs, particularly after the first cost control period. This would allow for lessons learned to be incorporated and for necessary revisions to be made to ensure the RIGs remain fit for purpose.

Integration with Other Regulatory Documents: Emphasis should be placed on ensuring seamless integration and consistency between the Successor Licensee RIGs and other relevant regulatory documents, such as the Smart Meter Communication Licence and the SEC itself.

Digitalisation and Data Usability: As the industry evolves, consideration should be given to how the RIGs can support greater digitalisation of reported data in the future and integrate with any other data repositories.

Cost Recovery Mechanisms: We note the need for further discussion on the differences between charging and pricing, and the associated cost recovery mechanisms. While the consultation implies pass-through structures may largely remain the same, further clarity would be helpful. In particular, the balance between mechanisms that allow for re-opening (adjusting future allowances based on actuals) versus those that rely on over- and under-recovery (with reconciliation at the end of a control period) should be carefully considered to ensure both fairness and stability in the regime.