

Decision

Financing arrangements for DCC1 and DCC2 during Business Handover

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This document outlines our¹ decision on proposed modifications to the Smart Meter Communication Licence (SMCL) to enable the holder of the Successor Licence (“DCC2”) to recover costs necessary for Business Handover activities prior to Transfer Date and our conclusions on further changes to the Successor Licence in relation to a mechanism that would best enable the current Licensee (“DCC1”) to recover costs necessary for mandated activities following the Transfer Date.

We are extending the consultation period on our second proposal in relation to provisions necessary to ensure that liabilities arising during Handover Period can be met to 16th January 2026.

¹ The terms ‘we’, ‘us’, ‘our’ refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

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Executive summary

Through our combined policy and statutory consultation, we proposed and sought views on two separate issues:

1. Funding of DCC2 and DCC1 mandatory activities pre- and post-Transfer Date
2. Ensuring any liabilities which may arise during Handover Period can be met

1. Funding of DCC2 and DCC1 during Handover Period

Firstly, we sought views on a mechanism to enable the Successor Licensee to recover legitimate Business Handover costs incurred prior to the Transfer Date via DCC1's Allowed Revenue. We also sought views on the criteria for allowable costs and exclusions. We proposed to expand the definition of the Pass-Through Costs term in the Allowed Revenue formula by modifying **LC 36 of the Smart Meter Communication Licence**. Respondents to the consultation supported our proposal (rationale and modification) and have decided to proceed with the licence modification. We will work with applicants for the Successor Licence to obtain estimates of Business Handover costs which will be included in DCC1's Charging Statement for RY26/27.

Secondly, we sought views on a reciprocal approach to enable the current Licensee to recover its efficient costs for mandatory activities after the Transfer Date. We also sought views on classifying the scope of any agreed assistance provided by DCC2 to DCC1 as part of DCC2's Mandatory Business under the Successor Licence. We found general support for the proposed approach. We will implement these via **changes to the draft conditions of the Successor Licence (SL)** (expected March 2026), subject to consideration of other representations to our consultation on the conditions of the SL. We will assess and consult on the costs of DCC1's post-TD activities as part of our scrutiny of the *ex-ante* Price Control submission for the First *ex-ante* Price Control Period (from TD to March 2028).

These decisions honour a principle that only one charging statement should exist at a time (DCC1's prior to Transfer Date and DCC2's thereafter). We expect the details of the process for payments between DCC1 and DCC2 to be set out in a legally enforceable agreement entered into by both parties.

2. Ensuring any liabilities which may arise during Handover Period can be met

Having considered initial representations, we are extending the consultation period on this proposal for additional 28 days until 16th January 2026.

1. Introduction

The Smart Meter Communication Licence (SMCL), under which Smart DCC Ltd (“DCC1”) operates, is due to expire in September 2027. Two key milestones must occur before then:

- **Successor Licence award:** Planned for March 2026, whereafter DCC1 and the Successor Licensee (“DCC2”) will co-exist to enable an orderly handover and closure of the current SMCL.
- **Business transfer:** Responsibility for delivering the Authorised Business, along with all resources, will pass from DCC1 to DCC2 on the Transfer Date (TD), currently set for 1 November 2026.

Both entities will require funding for mandatory activities during the transition. The pre-TD and post-TD requirements for funding can be characterised as the following two distinct yet interlinked time periods:

- From March 2026, DCC2 will begin mobilisation, which will include activities such as setting up of its Board and governance arrangements, contract novation or preparation for the transfer of staff from DCC1 and providing onboarding support. DCC2 will require access to funding during this period until November 2026, when DCC2 will take on the Authorised Business and begins to levy charges on service users.
- From November 2026 until the DCC1 Licence expires in September 2027, DCC1 will no longer deliver the Authorised Business and will no longer be able to levy charges on users. It will, however, have residual duties until its Licence expires, such as the duty to submit to Ofgem the Price Control information in respect of the Final Regulatory Year (from 1 April 2026 to Transfer Date).

In October 2025 we consulted on:

- A modification to the SMCL to enable DCC2 to recover necessary Business Handover costs pre-TD via DCC1’s Pass-Through Costs
- Changes to the draft conditions of the Successor Licence to ensure DCC1 can recover its own costs post-TD for residual mandatory activities via DCC2’s *ex-ante* revenue

We also consulted on proposals to ensure that liabilities which may arise during Handover Period can be met by:

- Directing and increase in the value of the Parent Company Guarantee (PCG) (and the associated on-demand bond) under LC26
- Ringfencing profit elements of DCC1 in the last two Regulatory Years (RYs) pending Ofgem’s Price Control decisions in respect of the Allowed Revenue in those RYs by introducing a requirement on DCC1 to transfer to DCC2 Margin and Gainshare amounts on Transfer Date and establishing refund rules in the SL

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This decision responds only to the proposals related to cost recovery by DCC1/2 pre- and post-TD. As some stakeholders have asked for additional time to make representations, **we are extending the consultation period on the proposals dealing with potential liabilities by additional 28 days until 16th January 2026.**

We received 5 responses during the first consultation period. We publish non-confidential responses alongside this decision.

Context and related publications

Document	Published	Link
Decision on the detailed design and implementation of the <i>ex-ante</i> cost control arrangements	May 2025	www.ofgem.gov.uk/publications/dcc-review-phase-2-determination-allowed-revenue-conclusions
Statutory decision on interim changes to the DCC Licence	July 2025	www.ofgem.gov.uk/decision/modifications-smart-meter-communication-licence-transition-ex-ante-cost-control-and-other-changes-required-licence-closure-decision
Draft new Smart Meter Communication Licence	September 2025	www.ofgem.gov.uk/consultation/draft-new-smart-meter-communication-licence
Consultation on financing arrangements for DCC1 and DCC2 during Business Handover	October 2025	www.ofgem.gov.uk/consultation/financing-arrangements-dcc1-and-dcc2-during-business-handover
The DCC Licence		www.ofgem.gov.uk/energy-regulation/how-we-regulate/energy-licences-and-guidance/licences-and-licence-conditions

Decision-making stages

Stage	Activity	Date
1	Consultation opened	24 October 2025
2	Consultation closed (awaiting decision); deadline for responses	25 November 2025
3	Responses reviewed and published	19 December 2025
4	Consultation outcome – decision 1 published	19 December 2025
5	Second consultation period on liability proposals commenced	19 December 2025
6	Second consultation period on liability proposals closes	16 January 2026
7	Further responses expected to be reviewed and published	Q1 2026
8	Consultation outcome – decision 2 expected to be published	Q1 2026

2. Current SMCL Pre-TD recovery pathway

Section summary

We have decided to proceed with our proposal and modify the definition of Pass-Through Costs in Condition 36.8 of the SMCL to include payments made by the Licensee to the Successor Licensee for purposes associated with Business Handover, as the Authority may direct. Respondents supported our proposals and agreed that the proposed mechanism would allow DCC2 to recover eligible cost of business handover prior to the Transfer Date and enable a smooth transition. Reflecting respondents' feedback, we have decided to amend the eligibility criteria. We expect to issue a direction in time for DCC1's final Charging Statement for RY26/27, commencing on 1st April 2026.

Questions posed at consultation

- Q1. What are your views on the proposed mechanism to enable DCC2 to recover necessary Business Handover costs prior to Transfer Date?
- Q2. Do you agree that the proposed modification to the definition of Pass-Through Costs accurately and sufficiently captures the policy intent? Do you have any views on the wording of the proposed modification?
- Q3. What are your views on the criteria for allowable DCC2 handover costs?

Background

2.1 Our aim has been to ensure that DCC2 has access to funding and can recover the costs associated with legitimate Business Handover activities taking place ahead of the Transfer Date. We said that we considered it appropriate for customers to fund DCC2's set-up and handover activities as:

- They will be necessary to facilitate a compliant handover of Authorised Business from one licensee to the next to ensure business continuity
- DCC2 will operate on a not-for-profit basis and therefore its shareholder would not be able to offset initial set-up costs by future profits in a manner that is transparent to service users

2.2 To deliver this objective, we proposed a targeted amendment to Licence Condition 36 (LC 36) of the current SMCL. Specifically, the amendment would allow legitimate DCC2 Business Handover costs to be recovered via DCC1's Charging Statement as Pass-Through Costs (PTC).

Current framework and proposed amendment

2.3 Under LC 36, DCC1's Allowed Revenue (AR_t) includes a Pass-Through Costs (PTC_t) term alongside other cost categories. The established formula for the calculation of the Allowed Revenue is as follows:

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$$AR_t = EC_t + IC_t + CRSR_t + PTC_t + BM_t + BMPA_t + ECGS_t - VASC_t + K_t$$

2.4 Currently, LC 36 defines Pass-Through Costs as the sum of:

- The total annual fee paid by the Licensee to the Authority;
- Payments made by the Licensee to SECCo Ltd for SEC governance and administration; and
- Payments made by the Licensee to AlthANCo Ltd for Alt HAN arrangements.

2.5 We proposed to amend this definition by inserting into LC 36, Part C, Paragraph 8, the following wording as an additional component of PTC:

- **“the amount that is equal to the payments made by the Licensee to the Successor Licensee for purposes associated with Business Handover as the Authority may direct.”**

2.6 We also sought views on the criteria for eligible handover activities and explicit exclusions.

Overview of responses

Rationale and modification

2.7 All five respondents supported our rationale and the proposed modification to LC36.

2.8 There was support for the principle that there should only be one charging statement in place at a time (DCC1's pre-TD and DCC2's post-TD) and the rationale for allowing DCC2 to recover necessary costs via DCC1's revenue.

2.9 Some respondents suggested a need for controls over pre-approved expenditure to verify the economy and efficiency of allowable costs.

2.10 One respondent highlighted that if the current licence holder was re-awarded the rights to manage DCC2, the set-up costs should not qualify as eligible handover costs.

Cost eligibility

2.11 Respondents suggested the costs of the following activities or requirements should be considered when setting the eligibility criteria for DCC2 set-up funding:

- DCC2 shareholder personnel seconded into DCC2 prior to the Transfer Date for handover activities
- Business insurance costs
- Regulatory registrations, eg HMRC, The Pensions Regulator, Information Commissioner's Office

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- Dedicated short-term office space until the Transfer Date
- Broader contract law advice during the Business Handover period
- Security clearance and background vetting of DCC2 staff to comply with security obligations
- Audit and assurance support on topics other than “handover deliverables”

Implementation

- 2.12 DCC1 agreed with our proposal to include an initial estimate into the indicative charging statement in January 2026 with a final forecast provided by end-February 2026 for the final charging statement issued ahead of the commencement of a new RY. DCC1 noted that there should be no ‘price shock’ event for customers and asked that estimates from DCC2 applicants should be gained sufficiently in advance to inform setting of charges for RY26/27.
- 2.13 DCC1 noted that the other Pass-Through Costs, in particular SECCo and AltHAN Co charges, are more certain as code bodies are established undertakings with known budgets, whereas DCC2 costs will relate to inherently uncertain set-up activities. DCC1 therefore highlighted the risk of DCC2’s outturn costs diverging from the initial estimates. To mitigate that risk, DCC1 suggested that payments to DCC2 should be made on the basis of invoices levied by DCC2 which would be subject to a regulatory approval by Ofgem. Similarly, another respondent noted that where actual costs incurred are lower than the estimates included in 2026 Changing Statements, then refunds should be promptly issued to customers.
- 2.14 DCC1 agreed that DCC1 and DCC2 should enter into a binding financial agreement to set out the details of the process for payments being made between the parties.

Our decision

- 2.15 **Having reflected all representations, we have decided to proceed with the proposed modification to LC 36.8 of the SMCL.**
- 2.16 We consider this modification appropriate to facilitate the recovery of necessary handover costs by the Successor Licensee prior to Transfer Date in a way which maintains transparency and stability of charges and minimises burden on both the current and successor licensees as well as service users. We maintain our rationale set out in the consultation, noting respondents’ support of the overall proposal. Below, we address respondents’ specific comments and set out further details on cost eligibility and implementation.

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Cost eligibility

2.17 We welcome respondents' additional suggestions on which costs should be considered eligible for recovery by the Successor Licensee. Accordingly, we have decided to revise the eligibility criteria as follows (changes highlighted):

Eligible costs include economic costs relating solely to activities necessary for a compliant and efficient execution of Business Handover in accordance with Business Handover Plan approved by the Authority under LC 43 of the Smart Meter Communication Licence. The costs of the following activities will be deemed eligible:

- *Setting up of internal governance, including the constitution of the Board and onboarding of a senior executive team*
- *Setting up of internal systems required for mobilisation*
- *Procurement of legal and commercial expertise to support contract novation, regulatory compliance and the transfers of assets*
- *Security accreditation, **including necessary security clearance and background vetting for new staff***
- *Essential dual-running of systems where unavoidable to protect service continuity*
- *Structured knowledge transfer and TUPE-related onboarding support and recruitment where necessary*
- *Audit and assurance linked to handover deliverables*
- ***Provision of office space (if required on premises separate from the shareholder)***
- ***Business insurance and mandatory registrations***

2.18 We do not consider necessary to include an explicit provision for DCC2 shareholder employee costs; insofar as any shareholder staff may be seconded to DCC2, if operated at an arm's length, the resulting costs should be directly linked to business handover activities and do not in themselves form a separate category. Similarly, we consider the existing provision for audit and assurance and legal expertise linked to handover deliverables to be sufficiently broad. For example, although it may be appropriate for the Successor Licensee to procure contract law advisory services as suggested by one respondent, they should always relate to handover activities. We will work directly with the bidders and clarify specific requirements as part of the tender process, as necessary.

2.19 We maintain our view in respect of cost exclusions.

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Implementation

- 2.20 As set out in our consultation, we expect the implementation via DCC1's Charging Statement from 1st April 2026. Based on the draft eligibility criteria, we have already sought from the qualified bidders their best estimates of the necessary set-up costs, which will be communicated to DCC1 for inclusion in the indicative charging statement to be published in January 2026. This estimate may be revised further, once the successful applicant has been selected, ahead of the final Charging Statement issued in March 2026. Subject to this modification being made, we expect to issue a formal direction under the new provision in LC 36.8 to include those costs into the calculation of DCC1's Allowed Revenue as Pass-Through Costs from 1st April 2026.
- 2.21 We note some respondents' concerns about the risk of outturn costs differing from the Successor Licensee's estimate and the need for appropriate controls in place. We also note DCC1's suggestion to follow a Purchase Order process and pay on receipt of a verified invoice from the Successor Licensee. We will consider further the process for the Pass-Through Cost payments in collaboration with both DCC1 and DCC2. We agree that the details of the arrangements should be documented within a written, legally enforceable financial agreement entered into by both parties.
- 2.22 We will also consider what necessary controls and monitoring will be in place, which may include:
- Placing limitations on the expenditure in a direction
 - Verifications of expenditure against invoices
- 2.23 We would expect the final payments for eligible set-up cost to be made by DCC1 to DCC2 on or before the Transfer Date. This is because DCC1 will cease to collect charges from service users on Transfer Date and DCC2 will commence operations with own budget agreed through the first *ex-ante* cost control.

Other matters

- 2.24 We agree that if the current licence holder was awarded the Successor Licence, this provision would not apply as business handover would not be taking place.

3. Successor SMCL post-TD recovery pathways

Section summary

Having considered all representations, we have concluded that it will be appropriate to make amendments to the draft Successor Licence to: designate pre-agreed activities carried out by the Successor Licensee to support DCC1 in discharging its licence obligations post-TD as Mandatory Business under the SL; and clarify that service charges can be levied to discharge Mandatory Business provided under the Successor Licence itself.

Subject to full consideration of the representations made in response to the SL consultation, we intend to give effect to these conclusions in our upcoming decision on the conditions of the Successor Licence.

We will assess and consult on DCC1's proposal for the costs of post-TD activities as part of the first *ex-ante* cost control.

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| <p>Q4. What are your views on the proposed mechanism to enable DCC1 to recover necessary costs for mandatory activities after Transfer Date and for pre-agreed assistance by DCC2 to be considered Mandatory Business under the Successor Licence?</p> <p>Q5. Do you have any comments on how best to reflect the proposed mechanism for DCC1 cost recovery post-Transfer Date in the Successor Licence?</p> |
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Background

3.1 DCC1 will continue to be bound by Price Control and other reporting obligations post-Transfer Date. This may have two cost implications:

- DCC1 may be entitled to be reimbursed for its own efficient costs of complying with its licence obligations – for this purpose, we proposed to use a mirror provision and pass these costs through via the Pass-Through Cost element of DCC2's revenue. Any payments made would be subject to a written agreement entered into between both parties
- DCC1 may require assistance from DCC2 (to access people, systems and data which will have transferred on Transfer Date – for example to deliver the final Price Control submission) which would generate Internal Costs for DCC2

DCC2 Pass-Through Costs

3.2 Under the draft SL, "Allowed Revenue" is replaced by a newly introduced term "Required Revenue", which remains functionally equivalent. The draft principal formula is:

$$\text{Required Revenue} = EC + IC + \textbf{PTC} - VASC$$

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- 3.3 Subject to our decision on the conditions of the SL, the definition of PTC in the SL will allow for an inclusion of such costs on direction by the Authority. We therefore did not propose further changes to this definition but sought views on the practicalities of using this method.

DCC2 Internal Costs and Mandatory Business

- 3.4 We sought views on whether DCC2's assistance to DCC1 for Price Control reporting and related obligations post-TD should be designated as part of DCC2's Mandatory Business.
- 3.5 To achieve this objective, we proposed using draft LC 6.2(b) which defines "Prescribed Business Services" as set out in LC 6.8. Specifically, Prescribed Business Services are those needed to discharge the Licensee's duties listed in Schedule 4 of the Successor Licence. We sought views on including the following wording into Schedule 4 to designate as Prescribed Business:
- **"Activities carried out by the Licensee pursuant to a written Agreement entered into by the Licensee with the Previous Licensee for the purposes of enabling the Previous Licensee to discharge its licence obligations"**
- 3.6 We further proposed a minor amendment to draft LC26.5(a) to clarify that service charges can be paid for Mandatory Business Services delivered under the SEC, REC, or the Licence itself.

Overview of responses

- 3.7 All respondents supported our policy rationale and the proposed amendments to the draft conditions of the Successor Licence. The proposal was considered fair and proportionate.
- 3.8 Mirroring its proposed approach for DCC2 pre-TD, DCC1 suggested that its access to payments for the reimbursement of economic costs of necessary post-TD activities should also be contingent on presenting invoices raised under a legally enforceable agreement between DCC1 and DCC. Equally, DCC1 suggested that any DCC1 invoice should be accompanied by a specific direction from Ofgem approving the expenditure as DCC2 will not be able to validate the activities.
- 3.9 DCC1 welcomed our proposed approach to including necessary costs in DCC2's Required Revenue via the first *ex-ante* cost control process and confirmed that it will update its Business Plan Report and Price Control submission (due to be submitted to Ofgem by 31st December 2025) to include cost estimates for residual post-TD activities. DCC provided an initial view of the expected duties to arise post-TD.
- 3.10 One respondent stated that DCC1 should be penalised if its resourcing model is skewed too heavily towards senior roles or contractors and consultants with

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unjustified day rates, or where these resources are retained for an excessive time-period; equally, they suggested that DCC1 should not make unjustified demands on DCC2-employed staff.

- 3.11 One respondent noted that costs of post-TD DCC1 support should be considered if DCC2 is unable to properly manage the Authorised Business alone.

Our decision

- 3.12 Having considered all responses and noting the support, **we have decided to proceed with our proposal** to make amendments to the draft Successor Licence to:

- Designate “activities carried out by the Licensee pursuant to a written Agreement entered into by the Licensee with the Previous Licensee for the purposes of enabling the Previous Licensee to discharge its licence obligations” as Prescribed Business (and therefore as Mandatory Business) under Schedule 4
- Amend draft LC 26.5(a) to clarify that service charges can be levied to discharge Mandatory Business provided under the Successor Licence itself

- 3.13 Subject to full consideration of the representations made in response to the SL consultation, **we intend to give effect to these conclusions in our upcoming decision on the conditions of the Successor Licence** (expected in March 2026).

Implementation

- 3.14 As set out in our consultation (paragraphs 4.9-4.10), we will assess DCC1’s forecasts for post-TD activities under the *ex-ante* submission (which DCC1 must make on or before 31st December 2025). We will consult on the allowable costs as part of the overall DCC2 Required Revenue (consultation expected in May/June 2026). Once the Successor Licence has been awarded, subject to our final decision on its conditions, we will issue a direction to designate the costs of DCC1 post-TD activities as Pass-Through Costs under DCC2’s Required Revenue and direct the inclusion of approved economic and efficient costs into the calculation of the Required Revenue from the Transfer Date.

- 3.15 We will work with DCC1 and the Successor Licensee, once appointed, to formalise:

- The process for payments to be made by DCC2 to DCC1 for agreed activities falling under Pass-Through Costs
- The extent of any support that DCC2 may provide to DCC1

- 3.16 We expect these matters to be set out in detail in the legally enforceable financial and cooperation agreement governing the exchange of funds entered into by both DCC1 and DCC2. The written cooperation agreement would mitigate the risk of

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unreasonable demands being placed on DCC2 staff post-TD. We will further consider what additional controls may be required so that only economic and efficient costs are passed through; as in the case of DCC1 set-up costs, this may include the use of direction under the SL and/or verification of invoices.

Other matters

- 3.17 We note the concern about the ability of DCC2 to manage the Authorised Business post-TD and whether further DCC1 support costs should be considered. DCC2 will be fully responsible for the operation of the Authorised Business under the Successor Licence from the Transfer Date. It will have at its disposal all staff, resources and systems transferred to it by DCC1. The extent to which DCC1 may provide any further limited support would be subject to the written cooperation agreement and any resulting costs would have to be included in DCC2's *ex-ante* Required Revenue (either as DCC2 Internal Costs or approved Pass-Through Costs).

Send us your feedback

We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this decision. We would also like to get your answers to these questions:

- Do you have any comments about the quality of this document?
- Do you have any comments about its tone and content?
- Was it easy to read and understand? Or could it have been better written?
- Are its conclusions balanced?
- Did it make reasoned recommendations?
- Do you have any further comments?

Please send your feedback to stakeholders@ofgem.gov.uk.