Data Communications Company

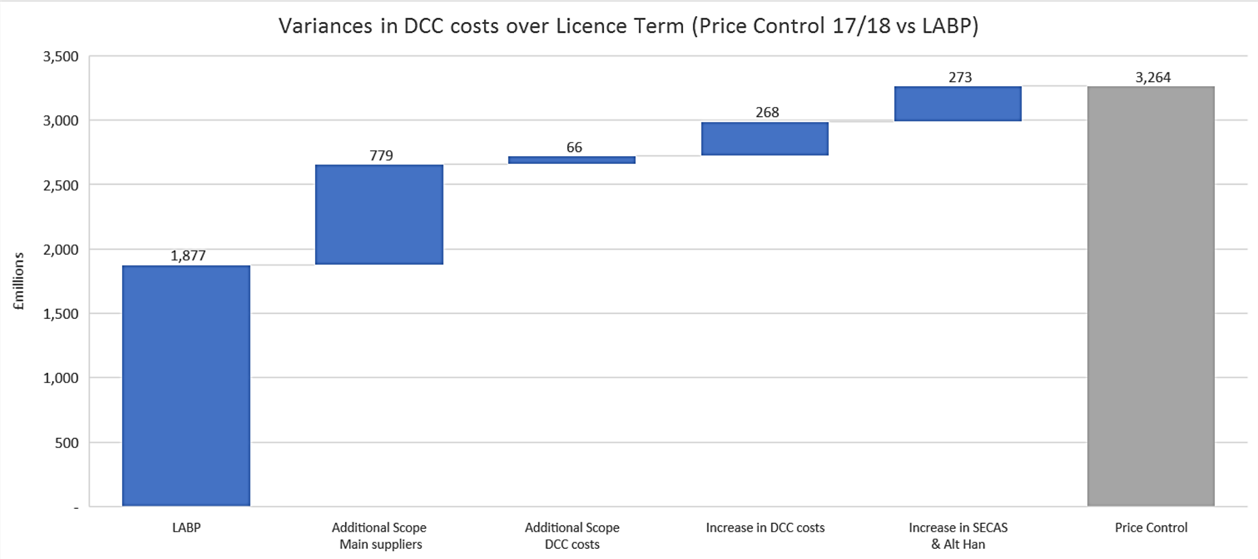
DCC Price Control

RY2017/18 – Responses to Stakeholder Event

Table of Contents

1 Details of projects and break up under ‘additional scope of costs’ and ‘SECAS and Alt Han’ shown in slide 14.

Stakeholders requested a more detailed breakdown of both “Additional Scope of Main Suppliers” and “SECAS and Alt Han” variance shown in a graph provided during the session. The graph is show below for convenience.



The following two sections will provide the breakdown and an explanation of what is driving the variance.

1.1 Additional Scope of Main Suppliers

The incurred costs for this item stems solely from new scope for our Fundamental Service Provider (FSP) contracts. This includes CSP North (Arqiva), CSP South and Central (Telefonica), and the DSP (CGI).

Firstly, it is important to understand that the values are total costs to the end of the licence or the end of the contract. Second, its critical to understand that the value of £779m represents a *variance*. The original baseline value already in our forecasts from the original contracts was £193m. The additional change requests totalled £972m, resulting in a difference of £779m.

Table 1-1: High level summary of the £779m variance from “Additional Scope Main Suppliers”

	LABP	CRRY	VARIANCE (CCRY - LABP)
	£'m	£'m	£'m
EXTERNAL COSTS VARIANCE	**1,668.506**	**2,447.335**	**778.829**
Baseline	*1,668.506*	*1,475.398*	*(193.108)*
New Scope	-	*971.937*	*971.937*

In the spirit of transparency, we have therefore provided a breakdown of the primary drivers of new scope.

DCC adds new scope to our FSPs through “change requests” or CRs. Therefore, itemised breakdowns may have a CR number associated with them. In general, CRs map to the different releases or programmes as shown in the table below. It is important to note that the costs don’t map perfectly, so please do not use these values as official figures. For example, CR091 had costs that were negotiated before the multi-release strategy that resulted in R1.2, R1.3, and R1.4.

Table 1-2: New Scope Driver to Programme / Release projects

Release / Programme	Primary Driver of New Scope
Releases 1.2, 1.3, and 1.4	• CR091 - Uplift of Service Provider solutions to align with IRPs issued post GBCS v0.8 • CR035 GBCS Re-baselining • CR160 Implementation of Releases 1.2 and 1.3 • CR255 - R1.4 Release as Individual Iterations
Release 2.0 – DBCH	• CR253 - Release 2.0 SIT – DIT • CR208 Environment for Enduring Operations, Tactical Element • PR023 Develop DBCH Detailed Specification • CR184 - Provision of DBCH Han Variants • CR194 - Updated SEC Technical Specifications
SMETS1	• SMETS1 Projects

The contract change requests CR160 and CR091 are the bulk of the new scope cost variance. R2.0/ DBCH is the next largest cost change, followed by SMETS1.

For reasons of commercial confidentiality, we are not able to split these by Fundamental Service Provider.

1.2 SECAS and Alt Han

The breakup of SECAS and Alt Han is relatively straightforward. The breakdown is shown below.

Table 1-3: Breakdown of SECAS and Alt Han including current forecast costs.

Pass through Baseline:	**Baseline**	**CRRY**	**Variance**
SECCO	56.871	66.976	10.105
Alt HAN		263.322	263.322
	56.871	330.298	273.427

2 Details on savings made in the SMETS1 project.

DCC presented a breakdown of the cost savings for SMETS1 on a confidential basis in the Q4 DCC Finance Update for Customers event, which took place on 10 December 2018.

As outlined in the session with Ofgem and our customers, the forecast costs of the SMETS1 implementation is expected to be at a lower level than the ‘do nothing’ business case which is owned by BEIS. DCC estimates that as a result of the good potential outcomes from the commercial negotiations, even after the DCC costs of building the integration solution, there is **a cost saving of almost £400m to industry over a 12-year period**.

It would not be appropriate for DCC to share this breakdown with customers given that it is owned by BEIS and forms the business case for the SMETS1 programme.

3 How will customer input be sought and used to inform decisions on future one-off projects

Stakeholders at the DCC-Ofgem event were clear and consistent in conveying their desire to be engaged earlier on projects that will incur additional costs for them.

DCC is consulting currently on Improving Engagement with Customers and Stakeholders.[1] We are seeking views on how we can improve the quality and breadth of engagement, and in particular where this influences expenditure decisions. We would be very interested in your opinions on our questions and proposals and would welcome any further views in addition to these. The close of this consultation is 31 January 2019.

Having acknowledged this, we expect to create multiple opportunities for customers to be involved during the life of projects, both current and in the future. The key area where DCC is learning, and where we hope to get feedback on through the consultation is when we should engage customers and when we should not. There is a balance between sharing all information for all projects and the current level of engagement. Extensive engagement creates a burden for our customers, especially small suppliers, as well as an increase in DCC staff time. This is an extreme example but demonstrates that interaction will be appropriate to the decisions that need to be taken. We will discover in the future where that balance lies.

When presenting information, we will endeavor to also strike a balance on the depth and detail of the information. For example, where it is possible to present options, we will do so to customers. We can also present tradeoffs between projects and other activity. In addition, we will provide project documentation which is geared to enabling customers to make properly informed decisions.

DCC's overarching goal is to ensure that customers are engaged at the right time, and before decisions are taken.

[1] https://www.smartdcc.co.uk/customer-hub/consultations/improving-smart-dcc-engagement-with-customers-and-stakeholders/

4 Improve transparency around shared services

DCC was awarded the Smart Meter Communication Licence by the Department of Energy and Climate Change (DECC) in September 2013 to establish and manage the data and communications infrastructure for smart meters in Great Britain (GB). DCC is regulated under an ex-post price control regulatory framework by Ofgem with costs being assessed after they have been incurred.

The Licence awarded to DCC was the outcome of a competitive tendering process. Capita PLC (Capita), DCC's parent company, bid for the licence and was successful. At the bid stage, in the Licence Application Business Plan (LABP), Capita included an overhead charge of 9.5% on DCC's internal costs that were included at the time of the bid.1 This overhead charge was to be paid to Capita and was accepted by DECC as part of the successful bid. Although the nature of the overhead charge is to provide a contribution to centrally incurred costs, DCC receives a range of services and benefits from Capita which are not separately charged for or contracted. In any business, overhead costs need to be recovered for the business to be financially viable. As central functions do not generate their own revenues, businesses such as Capita, with a range of operating business units, will generally include an overhead charge to cover both the cost of services provided to business units and the residual central costs.

At Ofgem's request, in September 2015, DCC committed to providing additional information to Ofgem on why they considered the overhead charge of 9.5% to represent value for money. Ofgem accepted that analysis in their RY2015/16 Decision, agreeing 9.5% would be applied to all base scope activity. To date, only the Switching Programme is New Scope activity, as it was not mentioned or included in the original Operational Service Requirements from DECC (now BEIS), nor within the final Invitation to Submit Best and Final Offer (ISBAFO) document.

Therefore, for RY2017/18, DCC requested a separate rate of 7.22% based on whether services included in the original study would be applied to the Switching Programme. The list of services DCC receives from Capita under the shared service charge is listed below.

Table 4-1: List of benefits / services DCC receives from Capita included within the Shared Service charge

Category	Benefit / Service Received
Training Courses	Access to Capita's online training courses which would be mandatory for DCC's employees. This includes: 1) Data Protection; 2) Information Security; 3) Social Media; 4) Financial Crime; 5) Safety, Health and Environment; and 6) Diversity and Inclusion.
	Subsidised access to Capita's skills training courses. Although DCC is charged for these courses, the cost of these courses is cheaper than the cost of taking these courses from alternative providers in the market.
Property Function	Provision of alternative office space for business continuity and disaster recovery
	Access to advice on office move, which has been utilised previously and may be required in the future.
Accounts Payable and Accounts Receivable cashier function	Provision of Accounts Payable cashier function. This involves processing of related transactions. This also entails use of relevant IT systems, and related policies and procedures.
	Provision of Accounts Receivable cashier function. Although not a full function, this would include applying receipts to debtors and sales ledger reconciliations. This also entails use of relevant IT systems; and related policies and procedures.
Payroll and HR function	Processing payroll transactions, including salary, pension, car scheme, healthcare scheme, expenses and other benefits. This also entails use of relevant IT systems (including time sheeting), and related policies and procedures.

Category	Benefit / Service Received
	Having expertise and knowledge on existing HR policy and regulation, monitoring changes to policy and ensuring compliance with legal requirements
	Access to support for employee issues (e.g. grievance)
IT function	Development and use of IT systems for AR, AP, Payroll and HR processing
	Advice on existing and future IT requirements taking account of internal and external changes to the operating environment
Public relations	Provision of public relations capability to respond to any issues
Senior Management Input	Non-Executive Director, (Capita) time spent on providing oversight and guidance on DCC's operations
	Senior Divisional Finance Director, (Capita) time spent on provision of independent financial expertise for DCC's Audit Committee
	Review and advice on DCC's Governance, Risk and Compliance (GRC) arrangements by Capita's GRC team
	Oversight and guidance by Capita's Divisional Board. This Board reviews DCC's operations and provides issue resolution and guidance as required.
	Time spent by Capita's CEO on DCC
Policy development and monitoring	Development, updating and monitoring of policies and processes applicable to DCC. This includes: anti-bribery and corruption processes; sanctions' monitoring and advice; Capita's register of legislation and related updates; and health and safety policy development, monitoring and reporting.
Legal services	Access to Capita's legal services group for ad hoc queries
Insurance	Provision of insurance, including professional indemnity, employers' liability and others.
	Advice on insurance claims. This also entails use of related policies and procedures.
Travel portal	Access to Capita's dedicated business travel portal, with negotiated rates and governance over booking procedures. Able to take advantage of IT updates or upgrades.
Internal audit services	Review of DCC's internal audit arrangements by Capita's internal audit team
Other advisory services	Advice on tax and treasury issues by Capita's Tax and Treasury teams
Total standalone IT system costs and other IT set-up costs	In addition to IT system costs, if DCC was a standalone entity, it would need to set up a wide range of policies, procedures and functions to enable the company to operate effectively on a standalone basis. This may include the following elements: • HR set up costs: this may include the development of HR strategy, policies and procedures, performance management process, initial design of salary and incentive schemes (e.g. healthcare scheme, car scheme and pension benefits) and other elements; • Finance set up costs: this may include the development of AP, AR, GL and payroll processes and governance; • Legal set-up costs: this may include a register of relevant legislation, policy and regulation to ensure that DCC is fully aware of its operating environment; and • Set up of other policies and updates: this may include anti-bribery and corruption processes, sanctions monitoring, and health and safety policies Note this is amortised over the duration of the Licence
Higher interest of Keep Well	DCC has a licence requirement with regards to financial security. To meet this requirement, DCC uses a combination of a Keep Well Bond and a Parent Company Guarantee from Capita, which it pays a fee for. If DCC were to be a

Category	Benefit / Service Received
Bond vs. Company Guarantee	standalone entity, it would no longer be able to use a Parent Company Guarantee to meet its licence requirement. Therefore, the standalone business would incur an additional interest expense of having another bond of £10m. The difference in interest between and Bond and a Parent Company Guarantee is estimated to be 250 basis points. Therefore, the standalone entity is likely to incur an £250,000 of costs per annum relative to the current arrangements. Note this is amortised over the duration of the Licence