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Paper Reference:	**SECP_63_1412_14**
Action:	**For Decision**

New Modification Proposal SECMP0068

1. Purpose

New Modification Proposal SECMP0068 'Alt HAN Company third party rights to enable external financing arrangements' has been raised by E.ON. This paper sets out our proposed approach for progressing this modification for the Panel's approval. We are recommending that this modification be progressed as an Urgent Modification and that it proceeds directly to Change Board vote. We are also requesting the Panel approves the Modification Report and the implementation approach, and agrees that SECMP0068 is an Authority Determined Modification.

This paper provides a high-level summary of the key points. A copy of the Proposal Form submitted by the Proposer can be found in Appendix A. Full details can be found in the draft Modification Report in Appendix B.

2. Summary of the proposal

What is the issue?

As preparations for, and as the Alt HAN Technology Solutions roll-out commences, high costs of technology solutions contracted via AltHANCo will be incurred over a short period. The pass-through of these costs in-year to Energy Suppliers will not be the most appropriate funding mechanism. This is because Suppliers will be burdened with high upfront costs for Alt HAN, which will not necessarily reflect the level of benefit that current and future Suppliers will receive from Alt HAN solutions as market share changes over time.

Following direction from the Alt HAN Forum (a Forum established under SEC Section Z and consisting of all Relevant Supplier Parties), AltHANCo is investigating possible financing routes to spread and reduce in-year costs for Energy Suppliers. Currently, the preferred financing model is an assignment of receivables model where AltHANCo would assign its right to receive income for the financed costs from the DCC directly to a funder. The need for AltHANCo to be given enforceable rights to receive payments from the DCC under the SEC would be required for all financing options.

The key issue for this financing arrangement is the ability to assign rights to receive income to the funder, to provide the necessary comfort that their revenue stream is secure. As AltHANCo is not a party to the SEC, technically it does not currently have an enforceable contractual right to receive payment of the AltHANCo costs from the DCC, and therefore by extension it cannot assign these rights. However, DCC are obligated to pay AltHANCo under its licence, as per SEC Section Z4.7, or for Relevant Suppliers to pay as per SEC Section Z4.11. It is not clear how AltHANCo would enforce its purported rights, since it is not a Party to the SEC and there is no reference to AltHANCo in the

Third Party Rights clause (Section M11.5(b)), through which other Third Parties (such as Communication Hub Lenders and SECCo) are permitted to enforce their rights.

As a result, it is not currently possible for funders to take an assignment of the right to the income received from the DCC, as they would have no ability to enforce that right. AltHANCo would be unable to pursue its preferred financing model as funders will not lend without a SEC Modification to give AltHANCo enforceable rights under the SEC and the ability to assign these rights. BEIS has confirmed that the policy intent was for AltHANCo to be able to finance, but the current SEC drafting does not support this intent.

What has the Proposer proposed as a solution?

The proposed solution is to give AltHANCo Third Party Rights to enable it to enforce and assign its rights to receive payments from the DCC. It has been agreed in principle by the Forum that AltHANCo should be given Third Party Rights to enable it to enforce its rights under Section Z4 and shall be entitled to assign the benefit of these rights.

This is the preferred solution, as it is less complex than other options considered, creates assignable and enforceable rights for AltHANCo against the DCC and (with Ofgem consent) licensed suppliers, limits AltHANCo exposure to other SEC obligations and will not bind AltHANCo to the prohibition on assignment of rights (Section M11.8). It also represents a similar approach to that used elsewhere in the Smart Meter programme as the DCC has previously used this structure for its financing activities.

3. Proposed progression

Request for progression as an Urgent Modification

The Proposer has requested that SECMP0068 be progressed as an Urgent modification, as they believe it meets Ofgem's Urgency Criteria (a)[1].

AltHANCo is looking to initially finance development and mobilisation costs over the next financial year, which would be spread over a number of years rather than being incurred in-year by Suppliers. From the 2020/21 financial year, AltHANCo will be looking to finance larger roll-out activities over a number of years. Financing will reduce in-year costs significantly for small and large Suppliers which AltHANCo considers has an advantage for competition as Suppliers will face fewer cashflow issues.

The DCC has also given AltHANCo a deadline of 31 January 2019 to provide an updated view on the AltHANCo budget for the 2019/20 financial year. This approach has been approved as part of the budget consultation. A view as to whether financing is going ahead before this date is needed to prevent the DCC from over-recovering in the 2019/20 financial year from Suppliers.

Without Urgent status, the Proposer believes the Modification will not be implemented in time to allow AltHANCo to finance costs next year.

We agree with the Proposer's view that this should be progressed as an Urgent Modification. We therefore believe that the Panel should recommend to the Authority that Urgency **should** be granted for SECMP0068.

[1] Be linked to an imminent issue or a current issue that if not urgently addressed may cause a significant commercial impact on parties, consumers or other stakeholder(s).

Progression timetable if Urgency is granted

We propose the following progression timetable if this modification is granted Urgency:

Activity	Date
Modification Report presented to Panel	14 Dec 18
Change Board vote	19 Dec 18
Authority decision	TBC

We do not believe there would be a need to consult the industry on this change, as it has already been consulted upon under Alt HAN governance; this modification has been raised to give effect to the decisions made by the Alt HAN Forum. We therefore believe this modification could be submitted directly to the Change Board for vote.

Progression timetable if Urgency is not granted

If this modification is not progressed as Urgent, we propose the following timetable is followed:

Activity	Date
Modification Report presented to Panel	14 Dec 18
Modification Report Consultation	17 Dec 18 – 10 Jan 19
Change Board vote	23 Jan 19
Authority decision	TBC

We believe that, if Urgency is not granted, this modification should proceed directly to Modification Report Consultation. As this solution has already been discussed and developed under the Alt HAN arrangements, we do not believe there is anything further a Working Group needs to assess. The Proposer notes that this timetable would mean AltHANCo will not be able to finance in time to meet the DCC's deadline of 31 January 2019.

Self-Governance

The Proposer believes that SECMP0068 should be progressed as an Authority Determined Modification, as it would have a material impact on Commercial Activities connected with the Supply of Energy (SEC Section D2.6(b)). We agree with this assessment.

Implementation approach

We recommend an implementation approach of:

- **2 January 2019** if a decision to approve is received by 31 December 2018; or
- **One Working Day following approval** if a decision to approve is received after 31 December 2018.

4. Recommendations

The Panel is requested to:

- **RECOMMEND** to the Authority that SECMP0068 **should** be progressed as an Urgent Modification;
- **RECOMMEND** to the Authority the progression timetable to be followed if Urgency is granted;
- **AGREE** that if the Authority does not grant Urgency SECMP0068 should be progressed directly to the Report Phase;
- **APPROVE** the Modification Report;
- **APPROVE** the implementation approach; and
- **AGREE** that SECMP0068 should be progressed as an Authority Determined Modification.

Joe Hehir

SECAS Team

7 December 2018

Attachments:

- **Appendix A:** SECMP0068 Proposal Form
- **Appendix B:** SECMP0068 Modification Report
    - **Annex A:** SECMP0068 Legal Text