



Department for
Business, Energy
& Industrial Strategy

**Department for Business,
Energy & Industrial Strategy**

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Electricity and gas licensees, National Grid, Smart
DCC Ltd, the Authority (Ofgem), the SEC Panel, SEC
Parties and other interested parties

Dear Consultees,

**SMART METERING IMPLEMENTATION PROGRAMME: CONSULTATION ON
ESTABLISHING A MECHANISM FOR RECOUPING SMART METER COMMUNICATION
LICENSEE ADMINISTRATION COSTS**

The Smart Meters Act 2018 introduced a special administration regime ('SAR') for the Smart Meter Communication Licensee ("SMCL") in order to ensure the continuity of the smart meter communication service to consumers in the highly unlikely event that the licensee was ever to become insolvent. This will bring the position for the SMCL in line with that already in place for equivalent organisations such as network companies and energy suppliers. The current SMCL is Smart DCC Ltd ("DCC").

The consultation document attached at Annex A seeks views on proposed licence modifications to enable recovery of the costs of a special administration in the event that the regime put in place by the Smart Meters Act 2018 were ever required. These modifications are needed in order to set up a mechanism for recovering the costs of a SMCL administration, including any Government support provided to the SMCL whilst it is in administration. This will help ensure that the SAR works effectively and as envisaged in the Smart Meters Act 2018.

Without a SAR in place, if the SMCL becomes insolvent, the impacts could be significant for consumers and the energy industry. For instance, disruption to billing and settlement could lead to inaccurate billing for consumers and cash flow issues for energy suppliers. Energy suppliers may also incur costs by having to put in place new procedures to replace the services provided by the DCC.

The proposed mechanism would allow the costs of administration to be recovered via a Shortfall Direction issued by the Secretary of State to National Grid, in its role as the national system operator for the gas and electricity transmission systems in Great Britain, to raise charges should there be a shortfall. The changes also clarify that the financial security put in

place under the SMCL's licence is available where necessary in the event of a SMCL administration.

The envisaged licence modifications to gas shipper, electricity supplier and electricity transmission licences and to National Grid's gas transportation licence are narrowly focussed on a mechanism for recouping administration costs from industry and work by modifying existing licence conditions that already operate and allow for the costs of other energy SARs to be recouped. In the highly unlikely event that a special administration were required, the special administrator would be under a duty to manage the company in a way that ensures that functions of the licensee under its licences continue to be performed efficiently and economically and to secure that it becomes unnecessary for the administration order to remain in force, either by rescue of the company or transfer of its business.

The proposed licence amendments are attached at Annexes C-G. Subject to consideration of consultation responses, the proposed amendments will be incorporated into the regulatory framework using the Secretary of State's powers set out in Sections 6 and 7 of the Smart Meters Act 2018.

As detailed in the consultation document at Annex A, any responses to the consultation should be submitted by 9 August 2019.

Yours faithfully,



Duncan Stone

Head of Delivery,

Smart Metering Implementation Programme

List of Annexes to this letter

Annex A	Consultation Document
Annex B	Cost Recovery Mechanism
Annex C	Legal text of proposed amendments to the Standard Conditions of Electricity Transmission Licences
Annex D	Legal text of proposed amendments to the National Grid Gas Transporter (NTS) Licence
Annex E	Legal text of proposed amendments to the Gas Shipper Licence
Annex F	Legal text of proposed amendments to the Electricity Supply Licence
Annex G	Legal text of proposed amendments to the DCC Licence
Annex H	Assessment of the cost for implementing a Special Administration Regime for the SMCL

Annex A – Consultation Document

1. The Government is committed to ensuring that every home and small business in Great Britain is offered a smart meter by the end of 2020. The Smart Metering Implementation Programme aims to roll out over 50 million smart gas and electricity meters to all domestic properties, and smart or advanced meters to smaller non-domestic sites - impacting approximately 30 million premises. Over 14.3 million smart and advanced meters had been installed and were operating across homes and businesses in Great Britain by the end of March 2019. The smart meter rollout is expected to deliver £5.7 billion in net benefits¹.
2. The Government is facilitating and overseeing the smart meter rollout by developing a regulatory framework establishing the key rights and obligations for all aspects of smart metering design, development, installation, operation, monitoring and reporting. As part of this, the Government has overseen the establishment of a national smart meter communication and data service provider - the Smart Metering Communication Licensee or “SMCL” (currently Smart DCC Limited or ‘DCC’) – which is a licensed entity regulated by Ofgem.
3. The SMCL provides a national communications infrastructure for smart metering and began offering live services in November 2016. DCC’s continued operation is fundamental to providing uninterrupted services, protecting consumers and securing benefits for both consumers and industry.
4. Through DCC, energy supply companies, network companies and other users can, subject to the provisions of the smart metering Data Access and Privacy Framework, access metering data remotely and securely. This enables them to deliver the benefits of smart metering, including accurate billing. Meters operated through DCC are fully interoperable, enabling consumers to switch energy supplier and keep their smart services. The services provided by DCC also facilitate faster switching between energy suppliers and the development of smart time of use tariffs.

SPECIAL ADMINISTRATION REGIME

5. Whilst DCC is subject to the provisions of the Insolvency Act 1986, until last summer there had been no special statutory provisions to deal with the threatened or actual insolvency of the SMCL. This is in contrast with the position for the water industry, the railways, the transportation or supply of gas, and the transmission, distribution or supply of electricity.
6. The Government considers that the risk of DCC’s insolvency is low, not least because of its financial arrangements under which, for example, users of its services are required to put up credit cover and DCC has the ability to reopen the charging statement and to recover any bad debt from other customers. However, the impact of DCC becoming insolvent for consumers could be high, potentially resulting in a loss of energy billing services (including prepayment services) which would particularly affect vulnerable consumers. The Smart Meters Act 2018 therefore introduced a Special Administration Regime (SAR) for the SMCL.
7. The objective of the SAR is to ensure the continuity of the smart meter communication service. Applying standard insolvency procedures could lead to the SMCL being wound up

¹ The Government is intending to publish an updated cost benefit analysis for smart metering later this Summer.

in the interests of its creditors, jeopardising the provision of the data and communications service and, as a result, the effective and efficient operation of the energy market and system.

8. By contrast, the SAR allows the Secretary of State (or Ofgem with the Secretary of State's agreement) to apply to the court for a special administration order to be made in relation to the SMCL. Such an order would direct that, while it is in force, the affairs, business and property of the SMCL are to be managed by an administrator appointed by the court.
9. The aim of the administrator would be to ensure that the functions of the SMCL under its relevant licences are performed efficiently and economically pending the SMCL being rescued, or its business being transferred as a going concern to another company (or other companies), as quickly and as efficiently as is reasonably practicable. This protects consumers and the continued provision of the smart meter communication service.

COST RECOVERY

10. The Secretary of State may make grants and loans, or provide guarantees, to the SMCL whilst it is in administration. The Secretary of State may also agree to indemnify persons in respect of liabilities incurred for loss or damage sustained in connection with the exercise of the administrator's powers and duties.
11. Any SMCL subject to a SAR may not be in a position to repay some or all of the funding it receives from the Government in the event of its insolvency, and so the Smart Meters Act 2018 provides for any such funding, and other SMCL administration costs, to be recovered from industry via a licence mechanism.
12. In the event of a shortfall in the assets available to repay costs occurring during or at the end of a SMCL administration, the Secretary of State can choose to trigger a cost recovery mechanism. Sections 6 and 7 of the Smart Meters Act 2018 enable the Secretary of State to modify gas and electricity licences to allow for the recovery of the amount of any shortfall through raising charges that industry participants are already required to pay as a condition of their licences. For these purposes the Secretary of State will act in accordance with the principal objective to protect the interests of existing and future consumers and general duties as set out in the Gas Act 1986 and Electricity Act 1989. An assessment of the cost for implementing a Special Administration Regime for the SMCL can be found in Annex H.
13. If there is any shortfall in the assets available to a SMCL under the SAR to repay funding provided by the Secretary of State and other relevant debts (such as the payment and expenses of the administrator and debts arising out of contracts entered into by the company while it is in administration) during or at the end of SAR, then the modified licence conditions will apply. This will allow the costs of the administration to be recouped, via a licence mechanism insofar as these cannot be met through the proceeds of sale or restructuring. We set out in Annex B illustrative scenarios on what these costs could be as well as how the cost recovery mechanism would work including a summary of proposed licence changes.
14. This cost recovery mechanism is in line with that which is already in place for the energy networks and energy supplier SARs. It follows the well-established principle in energy market trading arrangements that if a market participant, as a result of insolvency, defaults on any charges it is required to pay under industry codes, the cost is socialised across market participants (and may ultimately be passed through to energy consumers).

15. Without this procedure, expenses arising out of an SMCL administration might not be recovered, undermining the whole SAR operation. Therefore, there is a need for a mechanism for raising charges for the specific purpose of paying for the expenses of a SMCL administration.

DCC FINANCIAL SECURITY ARRANGEMENTS

16. Part B of Condition 26 of the DCC Licence requires the DCC to have in place an arrangement in respect of financial security that has been approved by the Authority and that contains (or is otherwise supported by) express provision for the Authority to direct that funds are to be released from the arrangement for one of the following purposes:
 - a. ensuring that any financial liabilities of the Licensee that remain or fall due to be met during a Handover Period may be discharged, so far as is possible, before the expiry or any revocation of the Licence; and
 - b. securing the Licensee's compliance with any requirement with respect to the application of funds imposed on it by virtue of a direction given by the Authority under Condition 42 (Management Orders for the Licensee) of the Licence.
17. Following entry into force of the Smart Meters Act 2018, Condition 42 of the DCC Licence has ceased to have legal effect.² As a consequence, we consider that the ability of the Authority to direct that funds are to be released from the arrangement in respect of financial security that the DCC is required to have in place under Part B of Condition 26 for the purposes of securing the Licensee's compliance with a direction made by the Authority under Condition 42 is no longer required. We therefore propose to remove this drafting.
18. In addition, following the introduction of the SMCL SAR, we consider that a scenario could arise under which it would be appropriate for the Authority to direct that funds are to be released from the arrangement in respect of financial security required by Part B of Condition 26 of the DCC Licence in connection with an ongoing special administration of the SMCL.
19. We therefore propose to amend Condition 26.8 of the DCC Licence to enable the Authority to direct that funds are to be released from the arrangement in respect of financial security for any purpose specified by a Smart Meter Communication Administrator as being necessary for the purposes of enabling the Smart Meter Communication Administrator to manage the affairs, business and property of the Licensee and exercise and perform all of the powers and duties of a Smart Meter Communication Administrator. We additionally propose a consequential amendment to Condition 26.17 of the DCC Licence to define Smart Meter Communication Administrator with reference to the meaning given to that term in the Smart Meters Act 2018.
20. We consider that this proposed amendment aligns with the original intent of Condition 26 of the DCC Licence, which was set out in our April 2012 consultation on the draft DCC Licence as ensuring "that the DCC has sufficient capital vested in the company to ensure

² Condition 42.17 of the DCC Licence provides that Condition 42 ceases to have effect from the date on which either or both of the Secretary of State and the Authority is able by virtue of an enactment to apply to the High Court for an order appointing a person to manage the business, affairs, and property of the Licensee for purposes and in circumstances substantially equivalent to those that apply under Chapter 3 of Part 3 of the Energy Act 2004 with respect to the making of an energy administration order in relation to a protected energy company.

that shareholders have a clear interest in the ongoing financial viability of the business as opposed to walking away in challenging circumstances”.³

Consultation Questions	
1.	Do you agree with the proposed licence modifications set out in Annexes C - F to recover the costs of the Special Administration Regime? Please provide reasons with your response.
2.	Do you agree with the proposed modifications to Condition 26 of the DCC Licence set out in Annex G relating to the release of funds from the arrangement in respect of financial security that the DCC is required to have in place under Part B of that Condition? Please provide reasons with your response.

Responding to this consultation

Responses to this consultation should be submitted by **17:00 on 9 August 2019** to: smartmetering@beis.gov.uk; or addressed to: Smart Metering Implementation Programme – Regulation, Department for Business, Energy & Industrial Strategy, 1 Victoria Street, London SW1H 0ET.

Information provided in response to this consultation, including personal data, may be subject to publication or release to other parties, or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000, the Data Protection Act 2018, and the Environmental Information Regulations 2004).

The individual responses to this consultation may be published and you should therefore let us know if you are not content for your response or any part of it to be published. If you indicate that you do not want your response published, we will not publish it automatically, but it could still be subject to information requests as detailed above. If you do not want your individual response to be published, or want it to otherwise be treated as confidential, please say so clearly in writing when you send your response to the consultation. For the purposes of considering access to information requests, it would also be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

³ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/43058/4937-cons-draft-dcc-licence-smart-meters.pdf

Annex B –Cost Recovery Mechanism

1. In the event of a shortfall in the assets available to repay costs occurring during or at the end of a SMCL administration, the Secretary of State can choose to trigger a cost recovery mechanism. Under these circumstances it is proposed that the Secretary of State would issue a direction to National Grid, in its role as the national system operator for the gas and electricity transmission systems in Great Britain to raise, through the charges it levies on gas shippers and electricity suppliers, a specified amount to make good the shortfall.
2. As is the case for other energy SARs⁴ the shortfall direction would include:
 - the details of the amount of the shortfall;
 - the details of the amount to be raised and applied in making good the shortfall;
 - to whom it will be paid (this will usually include the Secretary of State) and, where there is more than one recipient, the priority in which it is to be applied;
 - which charges will be modified;
 - when the amount will be raised and when it will be paid to the specified recipients;
 - any interest to be charged on a late payment; and
 - the details of the amount that can be raised and retained for administering this cost recovery mechanism and the manner in which it is to be raised.
3. As soon as reasonably practicable after receiving the shortfall direction, and taking into account the timeframe in which gas shippers and electricity suppliers are able to pass through the additional charges, National Grid will modify its charges and notify those to whom the modified charges apply of:
 - the modified charges;
 - any changes to the date or time period within which the charges are to be paid;
 - the reason for the modified charges; and
 - any interest rate applicable to late payment of the modified charges.
4. The Secretary of State will decide which charges to modify when issuing the shortfall direction. As the cost recovery mechanism works by modifying an existing charge, the starting point for allocation of the costs will depend on the way in which the underlying charge is calculated (see further below).
5. The Government recognises that there will be cashflow implications for gas shippers and electricity suppliers and will consider the timescale for recovering costs when issuing a shortfall direction and ensure that it gives adequate notice of payments.
6. National Grid will be able to recover its administrative costs for operating the cost recovery mechanism and the Secretary of State will specify a permitted administration fee in the shortfall direction, which National Grid will be able to recover in the same way as it

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https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/200469/cost_recovery_mechanism_cons_gov_response.pdf

recovers the rest of the money required to be raised by the shortfall direction. This is in line with the existing SARs for energy network and supply companies.

7. In order to put in place the cost recovery mechanism it will be necessary to modify National Grid's electricity transmission and gas transporter licences, electricity supply licences and gas shipper licences.

COMPETITION

8. It is the Government's intention to recover any shortfall through charges that distribute the cost equitably and do not lead to any market distortions. We are aware that choosing one particular charge over another may impact disproportionately on certain market participants. Full consideration will be given to the impacts any shortfall direction is likely to have, including the effect on competition, before it is made.
9. Given the current structure of National Grid charges, in order to avoid any distributional impacts it is probable that the Secretary of State would direct National Grid to recover any shortfall through the System Operator Commodity Charge⁵ in relation to gas customers and potentially through the Assistance for Areas with High Distribution Costs Charge in relation to electricity customers.
10. It is important that the Government has the flexibility to determine the notice period and the timeframe over which the increased charges would apply depending on the circumstances at the time. When making any shortfall direction, the Government's priority will be to keep the impact on energy consumers' bills to a minimum. This will require giving electricity suppliers and gas shippers adequate notice of any charge increases and a reasonable timeframe for implementation of the charge increases. As the structure of charges may change over time, it is the Government's intention to keep the flexibility to be able to direct National Grid to raise any of the charges it levies on gas shippers and electricity suppliers.

MODIFICATION OF NATIONAL GRID'S LICENCES

11. Annex C sets out proposed modifications to standard condition C24 of electricity transmission licences, and Annex D sets out proposed modifications to special condition 11D of National Grid's gas transporter licence. These proposed modifications would require National Grid to modify the charges it levies on electricity suppliers and gas shippers, respectively, to raise the amounts determined in the shortfall direction.

MODIFICATION OF GAS SHIPPER LICENCES

12. The Uniform Network Code (UNC) forms the contractual framework between National Grid as the national gas transporter and the shippers whose gas is transported. Under the UNC gas shippers are liable for a number of payments and charges to National Grid Gas plc in its capacity as transmission owner (TO) and system operator (SO) of the national transmission system (NTS).
13. Briefly, shippers that put gas onto the system must pay the following charges:
 - TO Entry Capacity Charge;
 - TO Entry Commodity Charge;

⁵ <https://www.nationalgridgas.com/charging/transmission-system-charges>

- SO Entry Commodity Charge.
14. Shippers that take gas off the system must pay the following charges:
- TO Exit Capacity Charge;
 - TO Exit Commodity Charge;
 - SO Exit Commodity Charge
15. Standard condition 19 of the gas shipper licence requires shippers to pay charges that are modified to raise sums used in making good an energy administration shortfall. The Government proposes to modify standard condition 19, which has previously been modified to cover the energy supplier and energy network SARs, to allow National Grid to raise the charges it levies on shippers to comply with a shortfall direction in relation to a SMCL administration. The proposed modifications to the licence condition are set out at Annex E.

MODIFICATION OF ELECTRICITY SUPPLY LICENCES

16. Electricity suppliers are required to sign up to the requirements of the Connection and Use of System Code and the Balancing and Settlement Code. These codes require them to pay National Grid's Transmission Network Use of System Charge and the Balancing Services Use of System Charge. These charges are considered sufficiently broad in scope to allow National Grid to increase them for the purpose of complying with a shortfall direction from the Secretary of State without modifying the electricity supply licence.
17. However, in order to allow the Secretary of State maximum flexibility in deciding which charges should be modified if he issues a shortfall direction, it is proposed that standard condition 15 be modified. The charge specified in this licence condition is narrower in scope and was originally intended to raise money from electricity suppliers to provide assistance with the high costs of distributing electricity in certain areas.
18. This condition was amended in 2006 by adding a new requirement for electricity suppliers to pay such additional sums as result from the modified charges for the purpose of raising any sums specified in a shortfall direction in relation to an energy administration (the special administration regime for energy network companies). This condition was further amended in 2013 to cover a shortfall direction in relation to energy supply company administration.
19. The Government is proposing a further modification so that electricity suppliers are required to pay additional sums resulting from modified charges for the purpose of raising any sums specified in a shortfall direction in relation to a SMCL administration. The proposed modifications to the licence condition are set out at Annex F.

COST RECOVERY MECHANISM ILLUSTRATIVE SCENARIOS

20. Overall it is considered highly unlikely a SMCL SAR (and so also any cost recovery mechanism), would ever be required given the various financial safeguards the SMCL has in place to support its cash flow. For example:
- Where a customer fails to pay its charges, the SMCL can make in-year adjustments to recover that bad debt from other SEC parties (see K9.4 of the SEC)
 - There is an independent board with decision rights for all expenditure over £1m, as well as being subject to a range of additional cost control mechanisms and audits

- There is a parent company deed of guarantee and indemnity which is a financial security arrangement that can be released as required (see condition 26 of the Licence)
 - The SMCL can increase charges at any time in the year to recover costs where necessary (see condition 19 of the Licence)
 - The SMCL recovers a prudent estimate of its allowed revenue to ensure it can meet payments in-year without the need to raise charges (see condition 36.4 of the Licence).
21. During the passage of the Smart Meters Bill, BEIS committed to consider and illustrate through this consultation the potential costs and scenarios which could arise from the implementation of an SMCL cost recovery mechanism in support of a SAR, should the SMCL enter insolvency.
22. Given the protections in place, there are no scenarios which are considered likely. However, as an illustration, scenarios leading to the insolvency of the SMCL could be:
- significant cost disallowances made by Ofgem;
 - the failure of large energy suppliers or a number of smaller energy suppliers to pay charges; or
 - significant failures or malpractice in the SMCL's management.
23. If the Government was not able to provide financial support to a SAR, then consumer interests could be adversely affected on two counts if the SMCL had to cease operations as a consequence:
- a. first, there could be a period when no data communications functions are available, impacting consumer services. Smart prepayment consumers could lose an easy mechanism for topping up their accounts, for instance;
 - b. second, energy suppliers might be unable to access data in order to bill their customers or send through new tariff information. So, at a minimum there could be delays in billing and possibly the need to re-introduce estimated billing and manual meter reading.
24. Without smart meter services, we therefore know that there could be additional costs and inconvenience for energy consumers. We also expect that these would significantly outweigh any cost of administration. We do not consider below a counterfactual for administration costs against the absence of a SAR, but rather only consider the impact of the SAR itself. Additional costs from the SAR compared to the SMCL carrying on its business under normal circumstances are the amount required to fund the administrator and any other disallowed costs. All other costs incurred would simply form part of the SMCL's standard operating costs and would be incurred regardless of whether the SMCL were operating under administration or not. If, however, the SMCL became insolvent and the necessary provisions for a SAR had not been made, as stated, this would come at great cost to the consumer. The costs of implementing a SAR for the SMCL are set out in more detail in Annex H.
25. In summary, the administrative costs which could need to be recovered would ultimately depend on the amount of funding provided by the Government to the SMCL in the event of insolvency and the extent to which the Government was able to recover the funding from the SMCL when it is rescued or sold as a going concern. We assume below a worst case scenario that no capital has been recovered through the sale or rescue of the

SMCL. Other key assumptions determining overall amounts which may need to be recovered include:

- a. the period of time the SMCL is in administration, as this has direct cost implications for the funding of the administrator; and
 - b. the point in time at which the administrator requests financial support from the Government.
26. We have modelled a number of scenarios to evaluate the extent to which financial support from the Government and the implementation of the cost recovery mechanism to recoup these funds from energy suppliers would impact on consumer bills: these scenarios suggest that any impact on bills would be very low.
27. To provide an illustration of these impacts on consumer bills, we set out two examples below – although as stated previously, we believe the risk of these scenarios materialising is extremely low.
28. Scenario 1 – SMCL becomes insolvent as a consequence of £10m of internal/external, costs being disallowed by Ofgem. For this scenario we are assuming:
- DCC is not permitted to access its Prudent Estimate sum;
 - DCC’s management is unable to access the £10m on-demand bond or the Parent Company Deed of Guarantee and Indemnity;
 - Assumed that insolvency period is 12 months
 - We assume that the costs of employing technical specialists and the administrator for this period would be ~£850,000 (see Annex H for detail).
 - The cost of working capital applying to the sum of all costs above is 6%, consistent with estimates in the Smart Meter 2016 Cost Benefit Analysis.
29. Under this assumption, you would need to recover a sum of around £11.5 million.
30. Scenario 2 - SMCL enters insolvency due to a large energy supplier, or a group of smaller energy suppliers that contribute significant sums to the SMCL revenue, being unable to pay charges. For this scenario we assume the following:
- The only costs incurred under the above counterfactual are those of the administrator and the technical expertise necessary throughout the insolvency period;
 - SMCL has used its Prudent Estimate sum;
 - Assumed that insolvency lasts between 3 and 6 months (until the SMCL can agree with Ofgem to vary charges on other energy suppliers);
 - We assume that the costs of employing technical specialists and the administrator for this period would be £265,000-£460,000 (see Annex H for detail);
 - SMCL’s management are able to access the £10m on-demand bond or the Parent Company Deed of Guarantee and Indemnity.
31. Under this assumption, you would need to recover a sum of under £1 million.
32. Under scenario 1, this could increase the average dual fuel energy bill in the range of £0 - £1 for one year. This also assumes that this pass-through cost will be received as a one-off charge to consumers, whereas in practice the costs will be passed on in smaller increments over time. In scenario 2, the additional costs would have a negligible impact on the average dual fuel domestic consumer bill even where passed on in full to only domestic consumers and as a one-off charge.

33. It would not be accurate to extrapolate from the estimates shown above the impact on consumer bills as a result of any higher amount of cost recovery required. These illustrative scenarios use published cost data from DCC in order to demonstrate the potential sum of money that might be drawn from the HMT Consolidated Fund⁶ in order for the SMCL to continue operating as normal, as well as the impact on consumer bills.
34. The SAR and cost recovery mechanism work to protect other market participants from large unpredictable increases in charges, which may then be passed through to consumers. Therefore, using the cost recovery mechanism, the costs can be managed to minimise any impact that is passed on to consumers. Industry participants will be given adequate notice of any increased charges to allow any unmet costs of the SAR to be repaid over a longer timeframe and so be passed through to consumers in a manner designed to reduce the impact on bills.

⁶ <https://www.parliament.uk/site-information/glossary/consolidated-fund/>

ANNEX C: STANDARD CONDITIONS OF ELECTRICITY TRANSMISSION LICENCES

Condition C24: Energy Administration, ~~and~~ Energy Supply Company Administration ~~and~~ Smart Meter Communication Licensee Administration: National Electricity Transmission System Operator Shortfall Contribution Obligations

1. The purpose of this condition is to require the licensee, in specified circumstances, to modify the charges imposed by it in carrying on its licensed activities (“charges”) to raise such amounts as are specified by the Secretary of State in a shortfall direction:
 - (i) from the persons; and
 - (ii) in the manner,specified in such shortfall direction, and to pay such amounts to the persons specified in the shortfall direction.

2. Where there is a shortfall during or at the completion of an energy administration, ~~or~~ energy supply company administration or smart meter communication licensee administration, the Secretary of State, after consultation with the Authority and the licensee, may issue one or more shortfall directions (including one or more shortfall directions to modify or replace any previously issued shortfall direction or directions) to the licensee specifying:
 - (a) the amount of the shortfall (including the amount of any interest accruing on the shortfall calculated to the date specified in sub-paragraph (f));
 - (b) the amount to be raised by the licensee and applied in making good the shortfall;
 - (c) the persons to whom the amount referred to in sub-paragraph (b) above is to be paid (“shortfall payment recipients”);
 - (d) the rate or rates of interest applicable to any part or parts of the amount referred to in sub-paragraph (b) above, and any other relevant information to enable the licensee to calculate liability (if any) for payment of any interest in respect of any late payment of such amount to or by the licensee;
 - (e) the method or methods by which the licensee may raise the amount referred to in sub-paragraph (b) above (including, without limitation, the manner in which and persons from whom it is to be raised and whether such amount is to be raised within or outside the licensee’s normal billing cycle);

- (f) the date by which the licensee is required to pay the shortfall payment recipients the amount referred to in sub-paragraph (b) above (or, where payment of the amount is required in instalments, the dates on which the licensee is required to make payment of each instalment);
- (g) where the shortfall includes relevant debts owed to more than one shortfall payment recipient, the priority in which the amount referred to in sub-paragraph (b) above is to be applied in discharging those debts;
- (h) the extent to which a subsequent shortfall direction modifies or replaces a previously issued shortfall direction;
- (i) where a shortfall direction is to modify or replace any previously issued shortfall direction, where appropriate, a requirement not to modify charges further pursuant to paragraph 5 below; and
- (j) the amount the licensee is permitted to raise and retain for administering the mechanism contained in this condition (“permitted administration fee”) and the manner in which the permitted administration fee is to be raised,

and the licensee shall comply with any such shortfall direction.

3. As soon as reasonably practicable after receiving a shortfall direction, the licensee shall:

- (a) modify its charges (in accordance with any method or methods specified in the shortfall direction) so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue resulting from the modification will equal the amount to be raised by it as specified in the shortfall direction (including, at the licensee’s discretion, any permitted administration fee); and
- (b) notify the persons who are subject to the charges so modified of:
 - (i) the modifications made to the charges;
 - (ii) any modification to the date or time period within which such charges shall be paid;
 - (iii) the reason for those modifications; and
 - (iv) the interest rate applicable to late payment of such modified charges.

4. The licensee shall on or before the date (or dates) specified in the shortfall direction pay the amount raised under sub-paragraph 3(a), (excluding any permitted administration fee), to the shortfall payment recipients, in accordance (where applicable) with any priority set out in the shortfall direction. For the avoidance of doubt the licensee shall not at any time be under any liability:
 - (i) to make any payments to any shortfall payment recipient, to the extent that those payments exceed the amount of additional revenue which the licensee has already received pursuant to the modification of its charges in accordance with this condition (excluding any permitted administration fee); or
 - (ii) to pay interest to any shortfall payment recipient in respect of any period for which any payment is late (in whole or in part) where the delay to such payment arises from the late payment of monies to the licensee.

5. Save where the Secretary of State specifies otherwise in a shortfall direction modifying or replacing a previously issued shortfall direction, if the amount raised by the licensee under sub-paragraph 3(a) (excluding any permitted administration fee):
 - (a) is less than the amount the licensee is obliged to raise by the shortfall direction to be applied in making good the shortfall (other than as a result of late, partial or non-payment of the modified charges by one or more party subject to those charges), the licensee shall:
 - (i) as soon as reasonably practicable, modify its charges (in accordance with any method or methods specified in the shortfall direction) so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue effected by such modification will equal the amount of that deficit together with any interest as specified in the shortfall direction; and
 - (ii) pay that amount to the shortfall payment recipients as soon as reasonably practicable but otherwise in accordance with the shortfall direction; or
 - (b) is more than the amount the licensee is obliged to raise by the shortfall direction to be applied in making good the shortfall, the licensee shall, as soon as reasonably practicable, further modify its charges so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue effected by such modification will equal the amount of the excess together with any accrued interest thereon.

6. For the purposes of sub-paragraph 3(a) and paragraph 5:
 - (a) the licensee may modify its charges notwithstanding that it has not given prior notice of such a variation required by any other condition of this licence and/or the CUSC and any charges levied by the licensee after modification pursuant to sub-paragraph 3(a) or paragraph 5 of this condition shall be deemed to be compliant with the licensee's obligations under Condition C4 (Charges for use of system), Condition C5 (Use of system charging methodology) and Condition C13 (Adjustments to use of system charges (small generators)) as from time to time amended;
 - (b) the licensee shall not enter into any agreement with another party which does not permit it to vary its charges in pursuance of this condition and shall take all steps within its power to amend, where necessary, any existing agreement to permit such variation; and
 - (c) in modifying its charges for the purposes of this condition the licensee shall not discriminate between any person or class or classes of person, except in so far as any differences in charges reasonably reflect objective differences between such persons or classes of persons or such differences in charges are required to give effect to the shortfall direction.
7. The licensee shall, immediately after making any payment under paragraphs 4 or 5 above, send a notice to the Authority and to the Secretary of State specifying the amount of that payment, the shortfall payment recipients to whom it was paid, the date on which it was paid and whether any of the payment was made up of interest resulting from late payment.
8. In calculating the licensee's revenue during any period for the purposes of any charge restriction condition, any change in the licensee's revenue attributable to the licensee's compliance with this condition shall be treated as if it had not occurred.
9. The licensee shall prepare, in respect of each period of 12 months ending on 31 March in which its charges are modified in pursuance of sub-paragraph 3(a) or paragraph 5, a statement showing:
 - (a) the aggregate amount of its revenue derived from any modification to charges in pursuance of sub-paragraph 3(a);
 - (b) the aggregate amount of its revenue derived from any modification to charges in pursuance of sub-paragraph 5(a);
 - (c) the aggregate amount of the change in its revenue resulting from any modification to charges in pursuance of sub-paragraph 5(b); and

(d) the aggregate payments made by the licensee during that period of 12 months ending on 31 March in accordance with paragraph 4 and, where applicable, subparagraph 5(a), and shall give the statement to the Authority within four months of the expiration of the period to which it relates.

10. On giving the statement mentioned in paragraph 9 to the Authority, the licensee shall also publish it on its website.

11. In this condition:

(a) any words or expressions used in Chapter 3 of Part 3 of the Energy Act 2004 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;

(b) any words or expressions used in Chapter 5 of Part 2 of the Energy Act 2011 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;

(c) any words or expressions used in the Smart Meters Act 2018 shall, unless the contrary intention appears, have the same meaning as they do in that Act when used in this condition;

(ed) “charge restriction condition” means any condition (including, without limitation, any revenue restriction condition) of this licence which places a monetary limitation on the revenue which may be recovered by the licensee during a given period; and

(de) “shortfall direction” ~~in relation to energy administration~~ means a direction issued by the Secretary of State for the purpose of meeting any “relevant debt”, within the meaning given to those words;

(i) in relation to energy administration, in section 169(4) of the Energy Act 2004; ~~or,~~

(ii) in relation to energy supply company administration, section 99 (4) of the Energy Act 2011;

(iii) in relation to smart meter communication licensee administration, in section 7(4) of the Smart Meters Act 2018,

~~-(including (iA) any modifications to such direction made by any subsequent shortfall direction, or (iiB) any shortfall direction replacing a previous shortfall direction).~~

ANNEX D: NATIONAL GRID GAS TRANSPORTER (NTS) LICENCE

Special Condition 11D. Energy Administration: NTS Shortfall Contribution Obligations

(1) The purpose of this condition is to require the licensee, in specified circumstances, to modify the charges imposed by it in carrying on its licensed activities (“charges”) to raise such amounts as are specified by the Secretary of State in a shortfall direction:

- (i) from the persons; and
- (ii) in the manner,

specified in such shortfall direction, and to pay such amounts to the persons specified in the shortfall direction.

(2) Where there is a shortfall during or at the completion of an energy administration, ~~or~~ energy supply company administration or smart meter communication licensee administration the Secretary of State, after consultation with the Authority and the licensee, may issue one or more shortfall directions (including one or more shortfall directions to modify or replace any previously issued shortfall direction or directions) to the licensee specifying:

- (a) the amount of the shortfall (including the amount of any interest accruing on the shortfall calculated to the date specified in sub-paragraph (f));
- (b) the amount to be raised by the licensee and applied in making good the shortfall;
- (c) the persons to whom the amount referred to in sub-paragraph (b) above is to be paid (“shortfall payment recipients”);
- (d) the rate or rates of interest applicable to any part or parts of the amount referred to in sub-paragraph (b) above, and any other relevant information to enable the licensee to calculate liability (if any) for payment of any interest in respect of any late payment of such amount to or by the licensee;
- (e) the method or methods by which the licensee may raise the amount referred to in sub-paragraph (b) above (including, without limitation, the manner in which and persons from whom it is to be raised and whether such amount is to be raised within or outside the licensee’s normal billing cycle);

- (f) the date by which the licensee is required to pay the shortfall payment recipients the amount referred to in sub-paragraph (b) above (or, where payment of the amount is required in instalments, the dates on which the licensee is required to make payment of each instalment);
- (g) where the shortfall includes relevant debts owed to more than one shortfall payment recipient, the priority in which the amount referred to in sub-paragraph (b) above is to be applied in discharging those debts;
- (h) the extent to which a subsequent shortfall direction modifies or replaces a previously issued shortfall direction;
- (i) where a shortfall direction is to modify or replace any previously issued shortfall direction, where appropriate, a requirement not to modify charges further pursuant to paragraph 5 below; and
- (j) the amount the licensee is permitted to raise and retain for administering the mechanism contained in this condition (“permitted administration fee”) and the manner in which the permitted administration fee is to be raised,

and the licensee shall comply with any such shortfall direction.

- (3) As soon as reasonably practicable after receiving a shortfall direction, the licensee shall:
 - (a) modify its charges (in accordance with any method or methods specified in the shortfall direction) so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue resulting from the modification will equal the amount to be raised by it as specified in the shortfall direction (including, at the licensee’s discretion, any permitted administration fee); and
 - (b) notify the persons who are subject to the charges so modified of:
 - (i) the modifications made to the charges;
 - (ii) any modification to the date or time period within which such charges shall be paid;
 - (iii) the reason for those modifications; and
 - (iv) the interest rate applicable to late payment of such modified charges.

- (4) The licensee shall on or before the date (or dates) specified in the shortfall direction pay the amount raised under sub-paragraph 3(a), (excluding any permitted administration fee), to the shortfall payment recipients, in accordance (where applicable) with any priority set out in the shortfall direction. For the avoidance of doubt the licensee shall not at any time be under any liability:
- (i) to make any payments to any shortfall payment recipient, to the extent that those payments exceed the amount of additional revenue which the licensee has already received pursuant to the modification of its charges in accordance with this condition (excluding any permitted administration fee); or
 - (ii) to pay interest to any shortfall payment recipient in respect of any period for which any payment is late (in whole or in part) where the delay to such payment arises from the late payment of monies to the licensee.
- (5) Save where the Secretary of State specifies otherwise in a shortfall direction modifying or replacing a previously issued shortfall direction, if the amount raised by the licensee under sub-paragraph 3(a) (excluding any permitted administration fee):
- (a) is less than the amount the licensee is obliged to raise by the shortfall direction to be applied in making good the shortfall (other than as a result of late, partial or non-payment of the modified charges by one or more party subject to those charges), the licensee shall:
 - (i) as soon as reasonably practicable, modify its charges (in accordance with any method or methods specified in the shortfall direction) so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue effected by such modification will equal the amount of that deficit together with any interest as specified in the shortfall direction; and
 - (ii) pay that amount to the shortfall payment recipients as soon as reasonably practicable but otherwise in accordance with the shortfall direction; or
 - (b) is more than the amount the licensee is obliged to raise by the shortfall direction to be applied in making good the shortfall, the licensee shall as soon as reasonably practicable, further modify its charges so as to secure that, in its reasonable estimation (such estimate to be agreed with the Authority), the change in its revenue effected by such modification will equal the amount of the excess together with any accrued interest thereon.

- (6) For the purposes of sub-paragraph 3(a) and paragraph 5:
- (a) the licensee may modify its charges notwithstanding that it has not given prior notice of such a variation required by any other condition of this licence and/or the uniform network code and any charges levied by the licensee after modification pursuant to sub-paragraph 3(a) or paragraph 5 of this condition shall be deemed to be compliant with the licensee's obligations under Standard Special Condition A4 (Charging - General) and Standard Special Condition A5 (Obligations as Regard Charging Methodology) as from time to time amended;
 - (b) the licensee shall not enter into any agreement with another party which does not permit it to vary its charges in pursuance of this condition and shall take all steps within its power to amend, where necessary, any existing agreement to permit such variation; and
 - (c) in modifying its charges for the purposes of this condition the licensee shall not discriminate between any person or class or classes of person, except in so far as any differences in charges reasonably reflect objective differences between such persons or classes of persons or such differences in charges are required to give effect to the shortfall direction.
- (7) The licensee shall, immediately after making any payment under paragraphs 4 or 5 above, send a notice to the Authority and to the Secretary of State specifying the amount of that payment, the shortfall payment recipients to whom it was paid, the date on which it was paid and whether any of the payment was made up of interest resulting from late payment.
- (8) In calculating the licensee's revenue during any period for the purposes of the charge restriction conditions, any change in the licensee's revenue attributable to the licensee's compliance with this condition shall be treated as if it had not occurred.
- (9) The licensee shall prepare, in respect of each period of 12 months ending on 31 March in which its charges are modified in pursuance of sub-paragraph 3(a) or paragraph 5, a statement showing:
- (a) the aggregate amount of its revenue derived from any modification to charges in pursuance of sub-paragraph 3(a);
 - (b) the aggregate amount of its revenue derived from any modification to charges in pursuance of sub-paragraph 5(a);
 - (c) the aggregate amount of the change in its revenue resulting from any modification to charges in pursuance of sub-paragraph 5(b); and

- (d) the aggregate payments made by the licensee during that period of 12 months ending on 31 March in accordance with paragraph 4 and, where applicable, subparagraph 5(a), and shall give the statement to the Authority within four months of the expiration of the period to which it relates.
- (10) On giving the statement mentioned in paragraph 9 to the Authority, the licensee shall also publish it on its website.
- (11) In this condition:
- (a) any words or expressions used in Chapter 3 of Part 3 of the Energy Act 2004 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;
- (b) any words or expressions used in Chapter 5 of Part 2 of the Energy Act 2011 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;
- (c) any words or expressions used in the Smart Meters Act 2018 shall, unless the contrary intention appears, have the same meaning as they do in that Act when used in this condition;
- (ed) “charge restriction condition” means any condition (including, without limitation, any revenue restriction condition) of this licence which places a monetary limitation on the revenue which may be recovered by the licensee during a given period; and
- (de) “shortfall direction” ~~in relation to energy administration~~ means a direction issued by the Secretary of State for the purpose of meeting any “relevant debt”, within the meaning given to those words:
- (i) in relation to energy administration, in section 169(4) of the Energy Act 2004; ~~or,~~
- (ii) in relation to energy supply company administration, section 99 (4) of the Energy Act 2011;
- (iii) in relation to smart meter communication licensee administration, in section 7(4) of the Smart Meters Act 2018,
- (including (iA) any modifications to such direction made by any subsequent shortfall direction, or (iiB) any shortfall direction replacing a previous shortfall direction).

ANNEX E: STANDARD CONDITIONS OF GAS SHIPPER LICENCES

Condition 19. Energy Administration, ~~and Energy Supply Company Administration~~ and Smart Meter Communication Licensee Administration: Shortfall Contribution Obligations

1. Pursuant to Chapter 3 of Part 3 of the Energy Act 2004, ~~and~~ Chapter 5 of Part 2 of the Energy Act 2011 and the Smart Meters Act 2018 and in accordance with this condition, the licensee shall, for the purpose of raising any sums specified in a shortfall direction, pay to the NTS operator such monies as result from any modification or modifications to the charges of the NTS operator made pursuant to Special Condition 11D (Energy Administration: NTS Shortfall Contribution Obligations) of the NTS operator's gas transporter licence.
2. For the avoidance of doubt, the modified charges to be paid by the licensee in accordance with paragraph 1 above shall be payable in accordance with the licensee's obligations governing the payment of those charges to the NTS operator, except insofar as required by the shortfall direction and so notified to the licensee by the NTS operator.
3. If it does not make the payment or payments required by this condition on or before the date required in accordance with paragraph 2 above, the licensee shall pay to the NTS operator an amount representing the rate or rates of interest applicable to any part or parts of the amount to be raised by the NTS operator, specified in the shortfall direction issued to the NTS operator pursuant to Special Condition 11D (Energy Administration ~~and Energy Supply Company Administration~~: NTS Shortfall Contribution Obligations) of the NTS operator's licence and set out in the notice given to the licensee by the NTS operator, which interest payment shall be made by the licensee as soon as possible after, and in any event within 28 days, of the date of the invoice from the NTS operator for such payment.
4. In this condition:
 - (a) any words or expressions used in Chapter 3 of Part 3 of the Energy Act 2004 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;
 - (b) any words or expressions used in Chapter 5 of Part 2 of the Energy Act 2011 shall, unless the contrary intention appears, have the same meaning as they do in that Chapter when used in this condition;

(c) any words or expressions used in the Smart Meters Act 2018 shall, unless the contrary intention appears, have the same meaning as they do in that Act when used in this condition;

(ed) “NTS operator” shall have the same meaning as in Standard Special Condition A3 of National Grid Gas plc’s gas transporter licence in respect of the NTS; and

(de) “shortfall direction” shall have the same meaning as in the Special Condition 11D (Energy Administration ~~and Energy Supply Company Administration~~: NTS Shortfall Contribution Obligations) of National Grid Gas plc’s gas transporter licence in respect of the NTS.

ANNEX F: STANDARD CONDITIONS OF ELECTRICITY SUPPLY LICENCES

Condition 15. Assistance for areas with high distribution costs scheme, Energy Administration Orders, ESC Administration Orders and SMCL Administration Orders: payments to System Operator

15.1 This condition sets out the obligations of the licensee in relation to payments to be made to the System Operator for the purpose of:

- (a) providing assistance with the high costs of distributing electricity incurred by a Relevant Distributor in a Specified Area; and
- (b) raising any sums specified in a Shortfall Direction in order to recover costs arising from the application of:

(i) an Energy Administration Order to a Protected Energy Company; ~~or~~

(ii) an ESC Administration Order to an Energy Supply Company; or

(iii) an SMCL Administration Order to a Smart Meter Communication Licensee.

15.2 The payments to which paragraph 15.1 refers are payments made pursuant to:

- (a) in the case of sub-paragraph 15.1(a), the Energy Act 2004 (Assistance for Areas with High Distribution Costs) Order 2005; and
- (b) in the case of sub-paragraph 15.1(b):

(i) in respect of sub-paragraph (i), the provisions of Chapter 3 of Part 3 of the Energy Act 2004; ~~or~~

(ii) in respect of sub-paragraph (ii), the provisions of Chapter 5 of Part 2 of the Energy Act 2011; or,

(iii) in respect of sub-paragraph (iii), the provisions of the Smart Meters Act 2018 ~~as the case may be.~~

Licensee's duty to pay

15.3 In accordance with paragraph 15.1, the licensee must pay to the System Operator:

- (a) the sums resulting from the pence per kWh tariff specified in accordance with the terms set out in standard condition C21 (Assistance for areas with high distribution costs

scheme: payments from authorised suppliers) (for this condition only, “standard condition C21”) of the Transmission Licence; and

- (b) where applicable, such additional sums as result from any modification of those charges made pursuant to standard condition C24 (Energy ~~administration~~ Administration, and Energy Supply Company Administration and Smart Meter Communication Licensee Administration: National Electricity Transmission System Operator: ~~GBSO shortfall~~ Shortfall contribution ~~Contribution obligations~~ Obligations) (for this condition only, “standard condition C24”) of the Transmission Licence.

15.4 Subject to paragraph 15.5, the sums to be paid by the licensee in accordance with paragraph 15.3 must be payable on a quarterly basis in each Financial Year (or such other basis as may be specified in standard condition C21 of the Transmission Licence) by:

- (a) the date indicated in each invoice received by the licensee from the System Operator requiring such payment; or
- (b) where no such date is indicated, no later than 28 days after the date of the invoice.

15.5 In the case of sums payable in accordance with sub-paragraph 15.3(b), the licensee must comply with any basis of payment different from that set out in paragraph 15.4 if this is required by the Shortfall Direction and has been notified to the licensee by the System Operator.

Late payment charges

15.6 In relation to sums required to be paid by sub-paragraph 15.3(a), the licensee must pay to the System Operator an amount representing 8% above the Base Interest Rate of any payment not made to the System Operator on the date specified pursuant to paragraph 15.4, calculated for each day after the date on which that payment should have been made, until the payment is made.

15.7 In relation to any sums required to be paid by sub-paragraph 15.3(b), if the licensee does not make that payment on or before the date required in accordance with paragraph 15.4 or 15.5, it must pay to the System Operator an amount representing the rate of interest applicable to any part of the amount to be raised by the System Operator that is specified in the Shortfall Direction and set out in the System Operator’s notice given to the licensee under standard condition C24 of the Transmission Licence, until the payment is made.

15.8 Any interest payment owed under paragraph 15.6 or 15.7 must be made by the licensee as soon as possible after, and in any event no later than 28 days after, the date of the System Operator’s invoice for such payment.

Definitions for condition

15.9 For the purposes of this condition:

Act means the Electricity Act 1989.

Base Interest Rate means, in respect of any day, the rate per annum which is equal to the base lending rate from time to time of Barclays Bank plc as at the close of business on the immediately preceding Business Day.

Business Day means any day of the week, other than a Saturday, on which banks are open for domestic business in the City of London.

Energy Administration Order has the same meaning as in section 154 of the Energy Act 2004.

ESC Administration Order has the same meaning as in section 94 of the Energy Act 2011.

Financial Year means a period of 12 months beginning on 1 April each year and ending on 31 March of the next calendar year.

Protected Energy Company has the same meaning as in section 154 of the Energy Act 2004.

Energy Supply Company has the same meaning as in section 94 of the Energy Act 2011.

Relevant Distributor has the same meaning as in section 184 of the Energy Act 2004.

Shortfall Direction has the same meaning as in standard condition C24 of the Transmission Licence.

Smart Meter Communication Licensee has the same meaning as the "smart meter communication licensee" in section 2(5) of the Smart Meters Act 2018.

SMCL Administration Order has the same meaning as a "smart meter communication licensee administration order" in section 2(1) of the Smart Meters Act 2018.

Specified Area means the area specified in the Energy Act 2004 (Assistance for Areas with High Distribution Costs) Order 2005.

System Operator means the holder, from time to time, of a Transmission Licence.

Transmission Licence means a licence granted, or treated as granted, under section 6(1)(b) of the Act and in which Section C of the standard conditions of that licence has effect.

Annex G – Smart Meter Communication Licences

Condition 26. Financial stability and financial security

Part B: Additional arrangements in respect of financial security

- 26.5 Within three months after Licence Commencement Date, the Licensee must propose to the Authority, and obtain its consent to, an arrangement in respect of financial security that is additional to such arrangements as the Licensee may have in place under Part A above in respect of financial stability.
- 26.6 Any proposal for which consent is sought under this Part B must include:
- (a) provision requiring the Licensee to notify the Authority forthwith should any element of the proposed arrangement for whatever reason cease to be legally effective; and
 - (b) sufficient information to enable the Authority to consider and decide whether in all the circumstances of the case it would be appropriate for it to consent to the proposal.
- 26.7 Any arrangement in place under this Part B must be in a form and substance that is approved by the Authority and that contains or is otherwise supported by express provision for the Authority at any time on reasonable Notice to direct:
- (a) that sums of such amount and on such terms as are specified in the direction are to be released from the arrangement; and
 - (b) that those sums are to be applied by the Licensee, to such an extent, in such manner, and at such times as may be so specified, for either or both of the purposes referred to in paragraph 26.8.
- 26.8 Those purposes are:
- (a) the purpose of ensuring that any financial liabilities of the Licensee that remain or fall due to be met during a Handover Period within the meaning of Condition 43 (Arrangements for the handover of business) may be discharged, so far as is possible, before the expiry or any revocation of this Licence; and
 - (b) the purpose of ensuring that any Smart Meter Communication Administrator who may be appointed in respect of the Licensee will have the financial resources necessary to manage the affairs, business and property of the Licensee and to exercise and perform the powers and duties of a Smart Meter Communication Administrator.
- 26.9 Arrangements arising under this Part B may include (for example only, and subject always to paragraphs 26.10 and 26.11) a Financial Security Instrument, such as:
- (a) a parent company guarantee procured in favour of the Licensee in respect of the Relevant Sum from a Holding Company of the Licensee that has an Investment Grade Issuer Credit Rating; or
 - (b) an unconditional and irrevocable letter of credit, or a performance bond, or an insurance policy, in each case issued in favour of the Licensee in respect of the Relevant Sum by a financial institution that has an Investment Grade Issuer Credit Rating; or

- (c) an escrow account containing the Relevant Sum that has been opened with a financial institution that has an Investment Grade Issuer Credit Rating.

- 26.10 References in paragraph 26.9 to an Investment Grade Issuer Credit Rating are to be read in accordance with the explanatory provisions of Appendix 1 (which has effect as part of this condition).
- 26.11 A Financial Security Instrument under paragraph 26.9, whether of a type mentioned in that paragraph or otherwise, must be expressed to be exercisable in Great Britain under English law.
- 26.12 The Authority's consent to a proposal under this Part B may be subject to such terms and conditions as it considers appropriate in all the circumstances of the case.
- 26.13 An arrangement that is in place in accordance with this Part B must, from the date on which it was put in place, be maintained by the Licensee for the full remaining duration of the Licence Term or (where applicable) of the Licence Term as extended by an Additional Licence Term.

Part C: Authority's powers with respect to Part B arrangements

- 26.14 This Part C applies where it appears to the Authority that there have been changes (or that changes are proposed):
 - (a) in the Authorised Business of the Licensee (whether by way of an enlargement of the activities of that business or otherwise); or
 - (b) in the external environment in which that business is or will be carried on,that are or are likely to be so significant as to materially affect the basis on which the Relevant Sum mentioned in Part B above was determined.
- 26.15 If this Part C applies, the Authority, where it considers that it is necessary to do so in all the circumstances of the case, may require the Licensee:
 - (a) to increase (or reduce, as the case may be) the Relevant Sum by such amount as the Authority thinks would be appropriate; or
 - (b) to propose a variation of any arrangement in respect of financial security to which the Authority has already consented under Part B above.
- 26.16 Before requiring the Licensee to do anything under paragraph 26.15, the Authority must consult the Licensee and SEC Parties and have regard to such views as may be expressed in relation to the matter.

Part D: Interpretation

- 26.17 For the purposes of this condition:

Financial Security Instrument has the meaning given to it in paragraph 26.9.

Relevant Sum means a monetary amount that:

- (a) was determined by the Secretary of State for the purposes of Part B above during or as a consequence of the Licence Application Process; and

(b) has been notified to the Licensee and the Authority in a direction issued by the Secretary of State for the purposes of that Part B with effect from the Licence Commencement Date,

and the determination may include an index or other means or method by reference to which the amount of the Relevant Sum may be adjusted (whether upwards or downwards) in such manner and at such intervals of time as may be specified in the determination.

Smart Meter Communication Administrator has the meaning given to that phrase in section 10(2) of the Smart Meters Act 2018.

26.18 Appendix 1 follows immediately below.

Annex H – Assessment of the cost for implementing a Special Administration Regime for the SMCL

BACKGROUND DATA ASSUMPTIONS FOR ILLUSTRATIVE SCENARIOS

1. Using evidence from the Government's Energy Supply Company Impact Assessment⁷, we have derived the incremental cost of running a Special Administration Regime, over and above that necessary to facilitate the normal operation of the DCC. These are as follows:
 - £70k to employ the relevant technical expertise and consult specialists, incurred by Government/Ofgem (as per the Energy Supply Company SAR Impact Assessment)⁸;
 - Daily rate of an Insolvency Practitioner will be used as a proxy for Special Administrator costs, this is between £2500-£3500. Assuming they are needed for:
 - 3 months, cost of a Special Administrator is ~£265,000 including legislative/specialist fees;
 - 6 months, cost of a Special Administrator is ~£460,000 including legislative/specialist fees;
 - 9 months, cost of a Special Administrator is ~£655,000 including legislative/specialist fees.
 - 12 months, costs of a Special Administrator is ~£850,000 including legislative and/specialist fees
2. The assumption is that these costs can be covered either by DCC or by Government. If it is the case that it is funded by Government, funds will be recouped at the direction of the Secretary of State by the proposed cost recovery mechanism.

FINANCIAL SAFEGUARDS TO SUPPORT DCC'S CASH FLOW

DCC Prudent Estimate

3. These are from DCC's Prudent Estimate projections taken from DCC's Q3 Indicative Budget published on 5th October 2018. These are taken from the Charging Statement for 18/19, the Indicative Charging Statement for 19/20⁹

⁷ See: <https://www.gov.uk/government/consultations/energy-supply-company-administration--2>

⁸ Energy Supply Company SAR Impact Assessment
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/66568/5574-energy-supply-company-administration-rules-impact-.pdf

⁹ https://www.smartdcc.co.uk/media/2841/ics_1920_-_issue_30_vfinal.pdf

Figure 1. DCC Prudent Estimate projections

Financial year	Charging statement	Indicative Charging Statement	Indicative Budget
2018/2019	£20.3m		
2019/2020		£22m	
2020/2021			£22m
2021/2022			£21.9m

Parent company deed of guarantee and indemnity

4. This is an agreement between Capita and DCC. Capita guarantees to pay on demand up to a maximum aggregate amount of £10m as if Capita were the principal debtor. The guarantee and indemnity amount is co-extensive with any amount claimed under the on-demand bond, an agreement between Capita, DCC and Euler Hermes, whereby Euler Hermes agrees to irrevocably pay any amount required to DCC so long as the combined total is a maximum £10m. Under Part B of Condition 26 of the DCC Licence, Ofgem can direct that funds are released from the bond for the purpose of ensuring that any financial liabilities of DCC that fall due during any Handover Period (when DCC hands over the business to another organisation) can be paid.
5. In the Deed the following is agreed:
 - The sums can be released under Condition 26.7 and used for the purposes stated in 26.8 of the DCC Licence;
 - Capita guarantees to pay on demand up to a maximum aggregate amount £10m as if Capita was the principal debtor;
 - The Guarantee Amount is co-extensive with any amount claimed under the On-Demand Bond – so in total under Part B of Condition 26 the Authority can direct that up to £10m in total is released from the Parent Company Guarantee and the On-Demand Bond.
6. We have proposed amendments to the DCC Licence to enable funds to be released from the financial security arrangement put in place under Part B of Condition 26 (see Annex G to this consultation).