

# Protecting Energy Consumers with Prepayment Meters: May 2020 statutory consultation

26 June 2020

## Introduction

Energy UK is the trade association for the energy industry with over 100 members spanning every aspect of the energy sector – from established FTSE 100 companies right through to new, growing suppliers and generators, which now make up over half of our membership.

We represent the diverse nature of the UK's energy industry with our members delivering almost all (90%) of both the UK's power generation and energy supply for over 27 million UK homes as well as businesses. The energy industry invests over £13.1bn annually, delivers around £85.6bn in economic activity through its supply chain and interaction with other sectors, and supports over 764,000 jobs in every corner of the country.

This is a high-level industry response to Ofgem's protections for energy consumers with prepayment meters in the default tariff cap. We would be happy to discuss any of the points made in further detail with Ofgem or any other interested party if this is considered to be beneficial.

## Executive Summary

Energy UK agrees with the underlying principle of using the default tariff cap to cover relevant PPM customers in place of the CMA's standalone PPM cap, as well as the timing proposed by Ofgem.

However, we believe that it would be more appropriate for Ofgem to utilise its contingency arrangements from 1 October 2020 for the PPM-specific cap level. In line with our response to the separate SMNCC review consultation, we have serious concerns with the proposed use of the average rollout profile and the costs and benefit assumptions used by Ofgem.

In addition, we believe that Ofgem should look to disaggregate credit and PPM rollouts in any single profile to ensure that cap levels are more reflective, as there are significant differences between credit and PPM.

## Protection for PPM Customers

Energy UK agrees with Ofgem's proposals in principle to use the default tariff cap (DTC) to cover relevant customers in place of the PPM cap, with suitable adjustments to account for costs-to-serve.

## Additional Efficient Operating Costs for PPM Customers with Traditional Meters

Energy UK welcomes Ofgem's acknowledgement that there is cross-subsidisation of PPM customers within the cap, and its intention for it to be unwound. However, we do not believe that Ofgem has provided sufficient rationale for not unwinding the full amount at the onset of its new PPM-specific cap, and through an increase to the PPM uplift rather than adjustments to the SMNCC.

## **Impact of the Smart Meter Rollout**

Individual suppliers will be best placed to provide detailed comments on the cost assumptions Ofgem has made, and their suitability and impact on the ability to efficiently fund the smart meter rollout for PPM customers. However, at a high-level, we do not believe that Ofgem has fully accounted for the costs associated with rolling out smart meters to PPM customers. This may be a result of its data, and we note that Ofgem's February 2020 SMNCC RFI only addressed credit customers. Ofgem should ensure that it does not rush to impose a new PPM-specific non-pass-through SMNCC if there is insufficient data to be confident of its robustness.

Ofgem has assumed that it believes suppliers are no longer installing traditional prepayment meters, and that there will be a decrease in costs via a reduced volume of customer communications. We do not believe either of these assumptions to be accurate and would welcome clarification as to the data Ofgem has based them on. Ofgem has also not accounted for the impacts that enrolment and adoption of SMETS 1 meters will have on suppliers' costs and has overstated the benefits of the rollout in some instances. Individual suppliers will be best placed to provide detailed responses to Ofgem outlining these concerns.

## **Setting a Single Rollout Profile**

In addition to the concerns raised in Energy UK's response to the SMNCC consultation regarding Ofgem's use of an average rollout profile and impact of BEIS' 18 June decision on the future smart meter rollout framework,<sup>1</sup> we have a further concern with its use in the PPM-specific cap level. We do not believe that it would necessarily be reasonable to assume the same rollout profile for credit and PPM given there are significant differences and Ofgem has not sufficiently shown that this assumption is robust. In disaggregating the credit and PPM rollouts, Ofgem should also consider the impact that specialist PPM-only suppliers would have on the average, and to take account of any disproportionate effect that is imposed on the overall average to ensure that the profile is reflective of the market as a whole.

## **Future Reviews of the SMNCC**

Energy UK has responded to Ofgem's proposals for annual reviews of the SMNCC in its response to the SMNCC May 2020 consultation, which also reflects our position for this response. Energy UK agrees that a future review of SMNCC will be necessary in order to properly account for the exceptional impacts of COVID-19 and to ensure that the future policy framework of the smart meter rollout is sufficiently reflected within the methodology following any BEIS decisions. Exceptional impacts of COVID-19 on other areas of the cap (such as bad debt) must also be reviewed.

However, while we support a one-off review to ensure the cap addresses the exceptional and unforeseeable circumstances of the Covid-19 pandemic, we continue to oppose the introduction of a general claw-back mechanism into the SMNCC as highlighted in our previous consultation responses. We are, therefore, concerned that the proposal to hold ongoing annual reviews will fundamentally change the nature of the default tariff cap from a prospective cap, to a wholly reactive cap. In that scenario, there will be a severe risk of undermining suppliers' ability to effectively forecast and reducing reliability and certainty when budgeting. Suppliers will only have some certainty for two cap periods at a time, and even that certainty will be at risk of retrospective changes at the next review. This would introduce intolerable uncertainty whereby allowances would change retrospectively, but operational decisions cannot be rolled back. Uncertainty is also created by Ofgem identifying more smart meter rollout costs within the Opex than previously signalled, but with no compensating Opex uplift.

We also note Ofgem's intention to rely on suppliers' ASR data to inform the yearly reviews. We do not believe ASR data is currently best formatted to achieve this aim and Ofgem should transparently outline and seek feedback, via consultation, on its proposed evidence base should it seek to proceed with the proposals.

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<sup>1</sup> <https://www.energy-uk.org.uk/publication.html?task=file.download&id=7573>

## **Contingency Arrangements**

Energy UK believes that it would be reasonable and appropriate for Ofgem to utilise its contingency arrangements for the PPM-specific cap level from 1 October 2020. It will be vitally important to ensure that the PPM-specific cap is robustly developed and set at an appropriate level that protects customers, and allows suppliers to recover the efficiently incurred costs of serving PPM customers and continuing the Government's smart meter rollout. We have raised a number of concerns with the assumptions being relied upon by Ofgem, as well as the proposed rollout profile, and we anticipate that suppliers will be providing more detailed submissions based on their own data to scrutinise Ofgem's workings.

We believe that Ofgem should endeavour to utilise its contingency arrangements if its assumptions prove incorrect, to allow for adjustments to be made. As the industry overcomes the immediate impacts of the COVID-19 emergency, and enters a phase of recovery, Ofgem must ensure that the cap is not set at a level that risk under-recovery of efficient costs, particularly with regards to the smart meter rollout which could undermine the speed at which PPM customers receive the benefits of the programme.

## **Timing**

Energy UK agrees with the proposal and rationale to introduce changes to the default cap with effect from 1 October 2020 and request the CMA issue the relevant direction to allow Ofgem to introduce a PPM-specific cap level for those customers on default tariffs.

**If you would like to discuss the above or any other related matters, please contact me directly on 020 7747 2931 or at [steve.kirkwood@energy-uk.org.uk](mailto:steve.kirkwood@energy-uk.org.uk).**