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Ofgem
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15 June 2021

Dear Karen,

PRICE CAP: FINAL CONSULTATION ON UPDATING THE CREDIT SMNCC ALLOWANCE

Thank you for the opportunity to comment on Ofgem's consultation on its proposals to update the credit SMNCC allowance for cap period 7 (October 2021 to March 2022) and cap period 8 (April 2022 to September 2022).

Our comments take into consideration Ofgem's addendum¹ of 1 June where it set out its intention to adopt a contingency allowance for cap period 7. We summarise below our views on the proposals in this consultation and the questions in the addendum. These points are covered in more detail in Annex 1.

- (a) **Contingency arrangement** – We agree with Ofgem's intention to adopt a contingency allowance for cap period 7 but disagree with the proposal to amend the rollout profile in the SMNCC model by using Q2 2021 forecasts to estimate Q3 and Q4 2021. We think Ofgem should analyse the rising trend in actual rollout volumes over Q2 and extrapolate that over Q3 and Q4 instead of flat-lining the rollout profile in Q2 to Q3 and Q4.
- (b) **Marketing costs** – Ofgem's view that suppliers will not, under a framework of mandated targets, incur higher marketing costs than historically does not reflect operational reality. We believe Ofgem has an opportunity, while contingency arrangements are in place, to explore with suppliers what the anticipated trends marketing costs will be.
- (c) **Covid-related installation costs** – Ofgem infers that, "suppliers would pay more each year for the annual rental of the smart meters which were installed in 2020". We encourage Ofgem to explain what evidence it has for assuming that increased installation costs related to COVID would be reflected in rental charges rather than being borne by suppliers.

¹ Price cap – addendum to consultations on reviewing the credit and PPM SMNCC allowances
<https://www.ofgem.gov.uk/publications-and-updates/price-cap-addendum-consultations-reviewing-credit-and-ppm-smncc-allowances>

- (d) **Next steps for cap period 8 (April-October 2022)** – We think it is premature for Ofgem to assume by default that it would only require a short consultation in early Autumn 2021 to finalise its approach to cap period 8. Ofgem should be prepared to consult in more detail on arrangements for cap period 8, should this be necessary.
- (e) **Content of policy document versus model** – It would be helpful for Ofgem to include more detail in its policy document on important non-confidential information and how it has undertaken calculations in significant areas (such as advance payment adjustments). We also think the user guide and/or the model could be updated to make the process of testing alternative rollout profiles simpler.

Please do not hesitate to contact me if you have any questions arising from this response.

Yours sincerely,



Richard Sweet
Head of Regulatory Policy

**PRICE CAP: FINAL CONSULTATION ON UPDATING THE CREDIT SMNCC
ALLOWANCE – SCOTTISHPOWER RESPONSE**

1. Introduction

We comment below on the following points in Ofgem's consultation:

- Contingency arrangements
- Marketing costs
- Covid-related sunk installation costs
- Next steps for cap period 8
- Balance of information in policy document versus model

2. Contingency arrangements

The addendum Ofgem issued in response to BEIS's decision to extend the 'all reasonable steps' framework to the end of 2021 seeks views on whether Ofgem should use a 'contingency' allowance to set the SMNCC for cap period 7 and what type of contingency allowance Ofgem should use.

We agree with Ofgem's intention to adopt a contingency allowance for cap period 7 but disagree with the proposal to amend the rollout profile in the SMNCC model by using Q2 2021 forecasts to estimate Q3 and Q4 2021. With an easing of lockdown restrictions in the final quarters of 2021 we anticipate a higher rollout over this period when compared with Q2. We think Ofgem should analyse the rising trend in actual rollout volumes over Q2 and extrapolate that over Q3 and Q4 instead of flat-lining the rollout profile in Q2 to Q3 and Q4.

We believe Ofgem should use the same SMNCC values for period 7 as in cap periods 5 and 6 to give it time to request actual rollout data for Q2 2021 from suppliers for the purpose of estimating the rollout in Q3 and Q4.

3. Marketing, asset and installation costs

Ofgem's view that suppliers will not, under a framework of mandated targets, incur higher total marketing costs than historically does not reflect operational reality. It is unclear what, if any, central policy incentives will be introduced to support consumer engagement. In addition, a greater emphasis will need to be placed on marketing as suppliers engage the subset of harder-to-reach customers.

The planning assumption for suppliers is that the onus rests on us to promote greater uptake of smart meters to meet mandated targets and that this would entail more marketing. Ofgem should approach suppliers for information that will enable it to establish a more realistic view of future marketing costs.

4. Covid-related sunk installation costs

Ofgem's February 2021 RFI asked suppliers to report on installation costs incurred during 2020 distinguishing between 'sunk' and 'productive' costs. It proposes to estimate COVID-

related sunk costs in 2020 (for the purpose of the sunk cost allowance) using the sunk installation cost data provided by suppliers and to assume that the COVID-related increase in 'productive' installation costs will simply be reflected in higher rental costs for meters installed in that year. An alternative approach, which Ofgem proposes to reject, would be to assume that all the COVID-related excess costs in 2020 need to be recovered by suppliers in year, rather than feeding their way through to rental charges. As Ofgem notes in its discussion, the two options result in very different values for the sunk cost allowance, and it is important that Ofgem bases its decision between these options (or on a hybrid of them) on robust evidence as to what is actually happening in the market, rather than a stylised hypothetical view of the market. We would encourage Ofgem to obtain further evidence if necessary to justify its decision.

5. Next steps for cap period 8

Suppliers are in the process of reacting to BEIS's decision (published 1 June) and we have not had much time to reassess Ofgem's proposals for cap period 8 in the context of this decision. We think it is premature for Ofgem to assume by default that it would only require a short consultation in early autumn 2021 to finalise its approach to cap period 8. Ofgem should be as comprehensive as possible in the autumn when consulting on arrangements for cap period 8.

6. Balance of information in policy document versus model

Ofgem's consultation document provides limited information on key pieces of information relating to its assumptions (such as rollout profile percentages) with an expectation that stakeholders are able to navigate Ofgem's SMNCC model to easily extract data. It would be helpful for Ofgem to include more detail in its policy document on important non-confidential information and how it has undertaken calculations in significant areas (such as advance payment adjustments). This would help ensure that there is an external paper in future to understand how Ofgem came to its conclusions – which would not be the case where information is subject to the the Confidentiality Ring obligation to delete all restricted material.

Also, Ofgem appears to concede that some of these parameters will be important to suppliers in planning their businesses but fails to appreciate that suppliers are not allowed to use the information for anything other than responding to the consultation.²

We have not found the process of testing alternative rollout profiles by updating values in the 'Scenarios input' sheet of the model to be as straightforward as the user guide suggests. For example, we have attempted to change inputs to the rollout profile in line with the guidance document but do not observe an immediate change to allowances. It would be helpful if the user guide and/or the model could be updated to make this process simpler.

ScottishPower

June 2021

² Ofgem's April 2021 PPM consultation says (paragraph 7.17) "We are also running a disclosure process, and relevant data, such as the modelling for the PPM SMNCC, will be disclosed after publication of the April 2021 consultation. This should allow suppliers to plan and budget with more certainty." However, planning and budgeting are not permitted uses under the Authorised Attendee Undertakings.