

Karen Mayor
Deputy Director
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

15 June 2021

Dear Karen,

PRICE CAP: FINAL CONSULTATION ON UPDATING THE PREPAYMENT SMNCC ALLOWANCE

Thank you for the opportunity to comment on proposals to update the prepayment (PPM) SMNCC allowance for cap period 7 (October 2021 to March 2022) and cap period 8 (April 2022 to September 2022).

The points we raise in this response are mainly focussed on areas where Ofgem has taken a different approach in its PPM methodology to credit. Most of our comments that relate to common approaches for PPM and credit are captured in our response to the credit SMNCC consultation.

These include our views on contingency arrangements, marketing, asset and installation costs, COVID-related sunk installation costs, arrangements for cap period 8 and the balance of information in the policy document and model. Therefore, this response should be read in conjunction with our response to the credit SMNCC consultation. The main points we wish to raise in relation to PPM proposals are as follows (some covered in more detail in Annex 1):

- (a) **Offsetting under-recovery of PPM costs** – We disagree with Ofgem’s proposal that any remaining under-recovered PPM costs that cannot be offset by the current SMNCC allowance will not be carried over to the next cap period. Ofgem should allow under-recovery of PPM costs to be carried over.
- (b) **Rollout profile** – It is inappropriate for Ofgem to exclude the rollout profile of a supplier where enforcement action *is ongoing*.

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

Yours sincerely,

A handwritten signature in blue ink that reads "Richard Sweet". The signature is written in a cursive, flowing style.

Richard Sweet
Head of Regulatory Policy

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

1. Introduction

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

- offsetting the possible under-recovery of efficient PPM costs
- exclusion of suppliers from calculation of rollout profile

2. Offsetting the possible under-recovery of efficient PPM costs

Ofgem says it proposes to use a PPM cost offset that works on a cap period basis rather than cumulatively. This means that for a given cap period, any remaining under-recovered PPM costs that cannot be offset by the current SMNCC allowance will not be carried over to the next cap period.¹

We disagree with Ofgem's proposal. The purpose of the offset is to compensate suppliers for an estimated £17 shortfall in the PPM cost to serve differential originally allowed by the CMA. Ofgem proposes to adjust for the shortfall by means of an 'offset' to any negative NPT SMNCC, which has the effect of ensuring that the cap can never increase above the level that would have resulted from the previous methodology. If the NPT SMNCC is not sufficiently negative in any given period, there will be no adjustment for the shortfall, and under Ofgem's proposals, there will be no carry forward to future periods.

We consider this approach is inconsistent with the approach Ofgem is adopting elsewhere and is wrong in principle. Ofgem justifies its proposal on the basis that the £17 uplift is merely a *possible* under-recovery (representing an upper-bound) rather than a definite one, so even if Ofgem does not manage to offset £17 in every cap period, this would not necessarily underfund suppliers; and, conversely, adopting a carry-forward approach could be too generous to suppliers.² Although there may be uncertainty around the value of the uplift, this should not prevent Ofgem coming up with a reasonable central estimate of the value, and then applying a carry forward approach based on that figure. Not to do so would be inconsistent with the cumulative approach that Ofgem has adopted in the case of advance payment clawbacks, and could be viewed as introducing an unfair bias towards downward adjustments over upward adjustments, undermining credibility in the process.

3. Rollout profile

Ofgem says that it proposes to 'exclude the rollout profile of any supplier where enforcement action has been taken, or is ongoing, in respect of their smart meter rollout as a single rollout profile option', on the grounds that such [enforcement] action may cast sufficient doubt as to whether the supplier has been rolling out at an efficient level.³

¹ Price cap - Final consultation on updating the PPM SMNCC allowance <https://www.ofgem.gov.uk/publications-and-updates/price-cap-final-consultation-updating-ppm-smncc-allowance> (para 4.73)

² As above (para 4.79)

³ As above (para 6.47, footnote 121)

Ofgem has identified two options for the PPM rollout profile, the rollout profile of the supplier with the highest net cost and the market average rollout profile (which it prefers). It is unclear to us whether Ofgem's proposed exclusion relates only to the calculation of the highest net cost profile or whether it will also exclude such suppliers from the calculation of the market average. We would welcome clarification on this point.

However, whichever rollout profiles Ofgem's proposal applies to, we believe it is inappropriate for Ofgem to exclude the rollout profile of a supplier where enforcement action *is ongoing*, and where Ofgem has not yet decided on whether the supplier failed to meet its obligations. As a matter of principle, Ofgem should not presuppose guilt before concluding its investigation and taking into account all the relevant circumstances.

ScottishPower
June 2021