

Price Cap - Working paper on 2022 annual review of SMNCC allowances

Executive summary

1. This working paper is about the non-pass-through Smart Metering Net Cost Change (SMNCC) allowances in the default tariff ('cap') for prepayment and credit meters. Specifically, it is the first step in our next annual review of these allowances, which will conclude in August 2022. This annual review will set the final allowances for cap period nine (October 2022 to March 2023) and cap period ten (April to September 2023).
2. For the next annual review, we propose to use Smart Meters Annual Information Request (SMAIR) data from the Department for Business, Energy and Industrial Strategy (BEIS) to update certain costs and benefits in the SMNCC model.
3. We propose not to use SMAIR data to update smart meter installation costs, as we intend to gather our own data, in early 2022, on sunk installation costs and the cost per installation in 2021. We intend to update our estimate of sunk installation costs in 2021 with this data in our next annual review. Any revisions to sunk installation costs or the cost per installation for 2021 will affect our calculation of advanced payments.
4. We do not currently intend to make other changes to our SMNCC modelling approach as part of our next annual review. This reflects the fact that we currently consider that the approach developed through previous consultations remains appropriate. However, we welcome any comments from stakeholders about whether there are other areas we should review.
5. We are seeking views by **9 November 2021**. Please respond to: retailpriceregulation@ofgem.gov.uk.

Introduction

Subject of this working paper

6. The default tariff cap ('cap') protects approximately 15 million domestic customers on standard variable and default tariffs (which we refer to collectively as 'default tariffs'), ensuring that they pay a fair price for their energy, reflecting its underlying costs. The cap is one of the key activities which fall within the outcome "consumers pay a fair price for energy and benefit from rights and protections" within our Forward Work Programme for 2021-22.¹ We set the cap by considering the different costs suppliers face. The cap is made up of a number of allowances which reflect these different costs.

7. One cost to suppliers is the net cost of installing and operating smart meters. We reflect this in the cap through two allowances. The operating cost allowance includes the cost of smart metering in the 2017 baseline year (alongside other operating costs).² The Smart Metering Net Cost Change (SMNCC) allowance reflects the change in smart metering costs since 2017.

8. The SMNCC allowance comprises a 'pass-through' element covering industry charges relating to smart metering and a 'non-pass-through' element covering suppliers' smart metering costs.

- We update the pass-through element as part of the six-monthly cap updates. This element is not the focus of this working paper.
- We use a forward-looking modelled approach to set the non-pass-through element for future cap periods. This working paper focuses on the non-pass-through SMNCC allowances (which we refer to as 'the SMNCC' for the remainder of this document).

¹ Ofgem (2021), Forward work programme 2021/22
<https://www.ofgem.gov.uk/publications-and-updates/forward-work-programme-202122>

² We index this allowance with inflation as part of the six-monthly cap update.

Smart Metering Net Cost Change update process

9. We set the SMNCC allowances in the cap for the duration of the cap.
10. We review the SMNCC annually and update all future values of the cap when we conclude an annual review.³ These are the final SMNCC allowances for the next year. The SMNCC allowances for the remaining cap periods beyond this are subject to revision through subsequent annual reviews.⁴

Role of this working paper

11. This working paper is the first step in the annual review which we expect to conclude in August 2022 ('2022 Annual Review').⁵ The 2022 Annual Review will determine the final SMNCC allowances for cap periods nine (October 2022 to March 2023) and ten (April to September 2023). These values will replace those set previously. It will also set the SMNCC allowance for the remaining cap period (cap period eleven, which runs from October to December 2023), although we then intend to update this SMNCC allowance as part of the annual review which we expect to conclude in August 2023.
12. This working paper covers the SMNCC allowances for both credit meters and prepayment meters (PPM). We have produced a single working paper given the similarities between our proposals for these areas. We indicate where a proposal only applies to one meter type.

³ When we are unable to conclude our annual review and have to set a contingency allowance, we only update the SMNCC for the next cap period.

⁴ For further information on the annual review process, see Chapter 1 of the final consultation for our 2021 Annual Review (published on the same day as this working paper).

⁵ The 'Next steps' section explains our intended process beyond this working paper.

Parallel consultation

13. Separately, we have published the final consultation for the current annual review ('October 2021 consultation').⁶ The deadline for responding to that consultation is the same as for this working paper.

14. As part of the October 2021 consultation, we are carrying out a similar disclosure process as for our previous final consultations. Please see that consultation for details on the disclosure process and how to participate.

15. Given that we are seeking views at the same time on the October 2021 consultation and this working paper, we confirm that stakeholders may use the information disclosed to respond to this working paper (as well as to the October 2021 consultation). For the avoidance of doubt, this does not mean that we will conduct a disclosure process alongside working papers (as opposed to final consultations) for future annual reviews.

Intended scope of the 2022 Annual Review

16. This section sets out what we intend to be the scope of the 2022 Annual Review of the SMNCC allowances.

17. At a high level, we intend to update the model with new data in certain specific areas and to calculate revised SMNCC values using the updated model. We do not presently intend to gather additional data or to make wider changes to the modelling approach.

Smart Meters Annual Information Request data

18. Suppliers submit Smart Meters Annual Information Request (SMAIR) data to BEIS each year. This data provides information on costs related to smart and traditional metering that they have incurred in the previous year.

⁶ Published on the same day as this working paper and available on our website.

19. We intend to take the same approach to the SMAIR data as set out in our August 2021 decisions.⁷ We intend to update the areas listed below.

20. The areas that we intend to provide updates for using SMAIR data are:

- costs: the costs of smart meters, communications hubs and In-Home Displays (IHDs).
- benefits: the number and cost of avoided site visits - this applies to both the credit and PPM SMNCCs. The following benefits apply to credit only: change of supplier, inbound enquiries, debt, and remote change of tariff.

21. We do not consider that the other areas included in the SMAIR are as significant, or likely to have changed materially. We therefore do not intend to update these other areas. As we stated in our May 2020 credit MNCC consultation, we only intend to update significant parameters based on SMAIR data. This would allow us to take into account new data, and therefore improve the accuracy of the cap.⁸

22. For smart meter installation costs and costs per installation in 2021, we intend to gather our own data rather than using SMAIR data. This is because, as explained in our first credit SMNCC working paper from November 2020 (previously referred to as 'SMNCC WP1'), we could not update installation costs using our normal approach based on SMAIR data (ie without sunk installation costs) given the impact of COVID-19.⁹

⁷ Ofgem (2021), Price Cap – Decision on credit SMNCC allowance, Appendix 10, paragraph 1.5.

<https://www.ofgem.gov.uk/publications/price-cap-decision-credit-smncc-allowance>

Ofgem (2021), Price Cap – Decision on PPM SMNCC allowance, paragraph 2.161.

<https://www.ofgem.gov.uk/publications/price-cap-decision-ppm-smncc-allowance>

⁸ Ofgem (2020), Reviewing smart metering costs in the default tariff cap: May 2020 statutory consultation, paragraph 3.33. <https://www.ofgem.gov.uk/publications/reviewing-smart-metering-costs-default-tariff-cap-may-2020-statutory-consultation>

⁹ Ofgem (2020), Updating allowance for smart metering costs in the default tariff cap: working paper, paragraph 3.6 - 3.10. <https://www.ofgem.gov.uk/publications/updating-allowance-smart-metering-costs-default-tariff-cap-working-paper>

Updating sunk installation costs for 2021 with actual data

23. In our August 2021 decisions, we set out our approach to considering the impact of COVID-19 on installation costs in 2020 and 2021.¹⁰

24. For 2021, we decided to estimate sunk installation costs using a bottom-up approach.¹¹

25. As set out in our August 2021 decisions, we intend to update our estimates of sunk installation costs and the cost per installation in 2021 with actual data in our next annual review. We intend to gather data on these areas using a similar RFI to the one we issued in early 2021. If stakeholders have any comments on the approach to gathering data in these areas, they should include them in response to this working paper. We then intend to gather data in early 2022.

26. Any revisions to sunk installation costs or the cost per installation for 2021 will affect our calculation of advanced payments.

Other areas

27. We maintain the position from our August 2020 decisions that we do not expect to carry out future annual reviews (including this one) with the same level of detail as our May 2020 credit consultation, as we consider this would be disproportionate.¹²

28. We intend to maintain our August 2021 decision not to gather other data to update the SMNCC model. We do not consider that further data gathering is likely to increase the

¹⁰ Ofgem (2021), Price Cap – Decision on credit SMNCC allowance, chapter 3.
<https://www.ofgem.gov.uk/publications/price-cap-decision-credit-smncc-allowance>
Ofgem (2021), Price Cap – Decision on PPM SMNCC allowance, paragraph 2.83 – 2.125.

¹¹ Ofgem (2021), Price Cap – Decision on credit SMNCC allowance, paragraph 3.39.
<https://www.ofgem.gov.uk/publications/price-cap-decision-credit-smncc-allowance>
Ofgem (2021), Price Cap – Decision on PPM SMNCC allowance, paragraph 2.95.
<https://www.ofgem.gov.uk/publications/price-cap-decision-ppm-smncc-allowance>

¹² Ofgem (2020), Reviewing smart metering costs in the default tariff cap: August 2020 decision, paragraph 5.39. <https://www.ofgem.gov.uk/publications/decision-reviewing-smart-metering-costs-default-tariff-cap>

accuracy of the SMNCC model significantly, or that this would be a proportionate use of resources.¹³

29. If there are other areas that stakeholders consider we should gather data for, in addition to what we have referred to above, they should raise this in response to this working paper. Stakeholders should explain – in as much detail as possible – what data they consider we should gather, and the reasons for this. When explaining the reasons for further data gathering, stakeholders should explain why this would be proportionate and likely significantly to increase the accuracy of the SMNCC model.

30. We do not presently intend to make other changes to our SMNCC modelling approach as part of our 2022 Annual Review. This reflects the fact that we consider that the existing approach, which we have developed through significant previous engagement with stakeholders, remains appropriate.

31. However, if stakeholders consider that there are other areas we should consider as part of our 2022 Annual Review, they should raise this in response to this working paper. Stakeholders should justify any such comments in as much detail as possible, in particular highlighting any relevant new evidence and/or developments.

32. There have been a number of supplier exits following the recent rise in wholesale gas prices. Where a supplier has taken on additional customers (eg as a Supplier of Last Resort), this will have an impact on the number of smart meters it will be required to roll out in future years.

33. In the event that suppliers consider that there would be any impacts on the revenue required through the SMNCC allowance, which would not be addressed by our current methodology, then we encourage them to submit comments in response to this working paper. Suppliers should explain, in as much detail as possible, the nature of any issues and

¹³ Ofgem (2021), Price Cap - Decision on credit SMNCC allowance, Appendix 10, paragraph 1.23.
<https://www.ofgem.gov.uk/publications/price-cap-decision-credit-smncc-allowance>
Ofgem (2021), Price Cap – Decision on PPM SMNCC allowance, paragraph 2.167.
<https://www.ofgem.gov.uk/publications/price-cap-decision-ppm-smncc-allowance>

how they consider these could be addressed. When commenting, suppliers should bear in mind that we are required to set a single cap level across suppliers.

Outputs from 2022 Annual Review

34. We expect to use our revised SMNCC model to set the SMNCC allowances, taking into account the updates we intend to carry out. However, if we require a contingency allowance, we intend to use this revised SMNCC model as a starting point for setting this contingency allowance. This would make use of the most recent data available.

Next steps

35. We welcome responses to this working paper by **9 November 2021**. Please respond to: retailpriceregulation@ofgem.gov.uk.

36. We do not ask specific questions in this document. Rather, we welcome views on any of the matters discussed in this consultation.

37. We will publish non-confidential responses on our website at www.ofgem.gov.uk/consultations. Please see Appendix 1 for further detail on confidentiality.

38. As the next step in our 2022 Annual Review, we intend to publish a final consultation in spring 2022. We then intend to publish a decision in early August 2022. Any changes from this annual review would take effect from 1 October 2022.

Appendix 1 – Confidentiality and privacy notice

Confidentiality

1. You can ask us to keep your response, or parts of your response, confidential. We'll respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.
2. If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you *do* wish to be kept confidential and those that you *do not* wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published. We might ask for reasons why.
3. If the information you give in your response contains personal data under the General Data Protection Regulation (Regulation (EU) 2016/679) as retained in domestic law following the UK's withdrawal from the European Union ("UK GDPR"), the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice in the next section.
4. If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

Privacy notice

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

1. The identity of the controller and contact details of our Data Protection Officer

The Gas and Electricity Markets Authority is the controller, (for ease of reference, "Ofgem"). The Data Protection Officer can be contacted at dpo@ofgem.gov.uk

2. Why we are collecting your personal data

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

3. With whom we will be sharing your personal data

We may share consultation responses with BEIS.

Please note that responses not marked as confidential will be published on our website. Please be mindful of this when including personal details.

4. For how long we will keep your personal data, or criteria used to determine the retention period.

Your personal data will be held for six months after the project, including subsequent projects or legal proceedings regarding a decision based on this consultation, is closed.

5. Your rights

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data
- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it
- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3rd parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

6. Your personal data will not be sent overseas

7. Your personal data will not be used for any automated decision making.

8. Your personal data will be stored in a secure government IT system.

9. More information

For more information on how Ofgem processes your data, click on the link to our "[Ofgem privacy promise](#)".