

Forward Work Programme Team
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Dear Team,

OFGEM FORWARD WORK PROGRAMME 2022/23

Thank you for the opportunity to comment on Ofgem's draft Forward Work Programme (FWP) for the 2022/23 regulatory year. We recognise the challenging circumstances that confront the industry and Ofgem as we enter the 2022/23 regulatory year; in particular rising and volatile wholesale energy prices, significant numbers of suppliers exiting the market, and sustained losses for those suppliers remaining in the market.

In this context, we are keen to work with Ofgem to deliver effective and practicable short and medium term solutions to mitigate the impacts of wholesale prices on suppliers and consumers without displacing key Ofgem workstreams and activities from its forthcoming work programme, and also to work with Ofgem to deliver the changes required to move to a more sustainable regulatory framework and market in the longer term which is more robust to volatility and ensures a pathway to net zero.

We set out the following comments on selected aspects of Ofgem's draft FWP.

Point 1: Enduring Priorities

Default Tariff Cap – We welcome the actions by Ofgem to address issues with the price cap methodology in the short and medium term, but consider more needs to be done as we have set out in our responses to various consultations and through bilateral engagement. In its role for setting the price cap level, as Ofgem implements changes to the cap methodology, it must consistent the impacts of transition between different methodologies and implement measures to mitigate impact to consumers and suppliers.

Energy Company Obligation (ECO) – We welcome Ofgem's commitment to strengthen its systems to improve delivery and efficiency of the next phase of ECO due to commence in the 2022/23 regulatory year. We are also pleased to see Ofgem's stated intent to engage with key stakeholders to establish clarity regarding scheme requirements from the outset of ECO 4. In this context we are keen to meet with Ofgem at the earliest opportunity to discuss the administration of ECO 4 in particular to understand how Ofgem's administration will adapt to the changes from ECO 3 and identify where Ofgem's requirements can be streamlined to avoid duplication with other schemes.

Capacity Market – We note that the Forward Work Plan makes no mention of the Capacity Market and we would ask that Ofgem consider this as a priority workstream to ensure that changes to Capacity Market (CM) Rules can be progressed to ensure the effectiveness of the scheme. We are concerned that previous CM rule reviews have been subject to delay and therefore we would welcome explicit commitment from Ofgem to implement timely rule changes in 2022/23. In particular we would urge Ofgem to progress work around evergreen prequalification, the establishment of the Capacity Market Advisory Group and Secondary Trading.

Point 3: Future of Retail

Ofgem/BEIS Energy Retail Strategy – It is not clear from the draft FWP whether Ofgem will resume its joint review with BEIS on the future of retail strategy. We believe this is an important workstream that should commence as early as possible providing incumbent businesses and prospective new entrants greater clarity and certainty regarding the vision for a future market and the transition to achieving it. We believe the future market should be a financially resilient one that delivers sustainable and fair prices to consumers, protects their interests particularly vulnerable consumers and facilitates the transition to Net Zero by engaged consumers. We believe an important of the vision will be the process to transition to removal of the market wide default tariff price cap.

Price Cap Policy and Level Setting – As we have shared with Ofgem in various engagement over recent times, while it remains in place, structural change to the default tariff cap is essential given the dire financial position that all surviving suppliers have been left in as a result of the flawed price cap design. Beyond the timescales that Ofgem is currently consulting on, Ofgem and Government must go back to first principles to design a mechanism that will resolve the problems that exist and be fit for purpose in a future flexible net zero world. It is crucial that, in balancing the needs of consumers, Ofgem must also take into account consumers' interest in having a dynamic, competitive and sustainable supply market, which depends critically on supplier financeability.

Financial Resilience and Controls – We welcome Ofgem's activity to increase supplier resilience, and consider this workstream a critical part of Ofgem's 2022/23 actions. In developing and implementing its work however Ofgem must ensure that it does so in a proportionate manner and in alignment with the required regulatory process to avoid any unintended consequences of a decision that has not had full stakeholder scrutiny or placing disproportionate burden on suppliers.

We are pleased to see Ofgem is including explicit recognition of measures to provide greater protection against the risk of cost mutualisation for customer credit balances and Renewable Obligation (RO) payments in the draft FWP. Events over the last months and years have given added urgency for these arrangements to prevent additional costs being imposed on consumers following supplier financial insolvency. We believe Ofgem should be able to implement reforms quickly given previously consulted on proposals for protecting consumer credit balances. Although amendments to secondary legislation may be sufficient to implement RO reforms set out in the August 2021 consultation¹, Ofgem and BEIS should consider whether the forthcoming energy bill could be used to

¹ <https://www.gov.uk/government/consultations/renewables-obligation-ro-addressing-electricity-supplier-payment-default-under-the-ro-scheme>

make any changes requiring primary legislation. We believe these reforms will mitigate a substantial part of the consumer detriment arising from supplier insolvency and therefore reduce the residual risk to be addressed by other measures to strengthen supplier financial resilience.

More generally, we would strongly support Ofgem giving further consideration to requiring suppliers to hold minimum levels of risk capital in their businesses. This can potentially have a twin benefit. First, the holding of risk capital will be set off against and reduce any costs that are mutualised on failure. So, for example, if the risk capital is sufficient to cover customer credit balances, there will be less need for prescriptive rules around ring fencing. Second, whoever is providing the risk capital, be it the parent company or capital markets, will have a strong incentive to monitor the supplier risk management practices – and may be able to do so more effectively than Ofgem.

Point 4: Low Carbon Infrastructure

Ensuring timely renewable generation connections – The recent ScotWind auction concluding with 25GW of prospective offshore wind generation in addition to 12GW of existing onshore wind generation pipeline for Scotland will provide a major step to meet net-zero targets. Generation developers need assurance that connection dates are not going to be delayed by slow or insufficient network investment identified and progressed by the electricity system operator (ESO), TOs and Ofgem. We would encourage Ofgem to work with the ESO, network operators and Government to proactively investigate ways network investment can be brought forward to facilitate timely connection of the present offshore and onshore generation pipeline. Ofgem's Low carbon Infrastructure strategic change programme must therefore be driven by a need to deliver the necessary network investment on time and in sufficient capacity. In this context we would recommend timely connection of renewable generation is included as an explicit priority alongside the FWP's stated focus on offshore transmission co-ordination, efficiency, and low costs. This will also be true of any enduring offshore transmission regulatory regime delivered by the Offshore Transmission Network Review (OTNR). In this respect it is also essential that Ofgem makes sufficient progress with its anticipated reviews of TNUOS and DUOS charges in 2022/23.

Electricity Transmission Network Planning Review – We support the development of a strategic network plan as an output of the review. We believe there is no single party best placed to develop and deliver this plan; rather it should involve all parties with the relevant expertise and experience, including but not limited to the TOs, ESO, Government, Ofgem and devolved governments and authorities. We would expect this to be reflected in the governance arrangements put in place regarding delivery of the strategic network plan.

RIIO-3 Development – We would encourage Ofgem to engage with companies early to consider any change to the price control process. In this context, we believe thought should be given to how the RIIO-T3 framework has the flexibility required to allow Net Zero critical infrastructure to be planned and built on a timely basis.

RIIO-2 Electricity Distribution Price Control Development – We urge Ofgem to take a balanced approach when determining the ED2 settlement in the context of the “cost of living crisis”. Although affordability is a key consideration, the price control framework in itself has limited scope to address rising energy costs which are primarily driven by wholesale energy prices and other factors exogenous to networks. Investment within the

ED2 framework is imperative to achieving timely progress to reaching Net Zero and will unlock wider economic benefits.

RIO-2 Needs Cases – Ofgem should confirm infrastructure delivery models as soon as possible for key LOTI projects so as not to unduly delay delivery of these key projects, for example by delaying the associated consenting process and preparations and engagement with the supply chain. We support the use of competition only when it can demonstrably deliver value for money for consumers. We encourage Ofgem to supplement their activities in this area with sufficient cost benefit analysis and impact assessments to ensure that delivery from outside the regulated framework remains in consumers' interests.

Point 5: Full Chain Flexibility

Large-scale and long duration electricity storage (LLES) - we welcome Ofgem's commitment to Work with government to address barriers to LLES and the development of required de-risking mechanisms AS a renewable generation developer we are deploying battery storage and hydrogen technologies to develop and transform existing generation into hybrid sites with storage capabilities. It would be helpful for Ofgem and Government to establish a proper definition enabling focussed and effective policy and regulation can be developed to support this asset class. Specifically, defined LLES technologies require appropriate incentives facilitating their transition from nascent development stage to commercially viable technologies. More generally, Ofgem must ensure regulatory policy and regulation keep pace with the rate of change in technology and investment by the industry.

Please do not hesitate to contact me or my colleague Haren Thillainathan (hthillainathan@scottishpower.com) if you have any questions arising from this response.

Yours sincerely,



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