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Price Cap: Consultation on reflecting potential changes to BSUoS charges in the price cap

EDF is the UK's largest producer of low carbon electricity. EDF operates low carbon nuclear power stations and is building the first of a new generation of nuclear plants. EDF also has a large and growing portfolio of renewable generation, including onshore, offshore wind and solar generation, and energy storage. We have around six million electricity and gas customer accounts, including residential and business users. EDF aims to help Britain achieve net zero by building a smarter energy future that will support delivery of net zero carbon emissions, including through digital innovations and new customer offerings that encourage the transition to low carbon electric transport and heating.

Suppliers continue to operate in a financially challenging environment and face increasing risks as a result of the continued period of market volatility, high prices, and operating under the default tariff cap. EDF remains committed to working constructively with both BEIS and Ofgem to develop and introduce measures that promote a healthy, well-functioning market that allows efficient and sustainable businesses to attain a fair margin and enable continued innovation and investment to benefit the interests of consumers.

The way BSUoS charges are currently recovered under the price cap introduces significant risks to suppliers around cost recovery, particularly in a market which continues to see high and volatile wholesale energy costs and where BSUoS costs are expected to increase in the future. The current lagged nature of cost recovery impacts on suppliers' ability to ever recover their actual costs given the risk of customers switching from default tariffs to fixed tariffs and at the time exiting the current price cap.

CMP 361

Following the publication of this consultation Ofgem has approved a CMP361 alternative modification that introduces an ex-ante fixed volumetric BSUoS tariff to replace the existing variable charge. Consequently, we are supportive of Ofgem's proposal to reflect this change in the price cap methodology by replacing the lagged variable charge with an ex-ante fixed charge.

Transition

EDF supports Ofgem's proposal to adopt a transitional adjustment when moving from an ex-post to an ex-ante BSUoS recovery mechanism. Such an approach should ensure that suppliers recover their BSUoS charges incurred between January 2022 and March 2023. Although we don't have any significant concerns with the proposed adjustment calculation, including the proposal to not offset any adjustment against a portion of the headroom, we do remain concerned with the proposed duration over which an adjustment will be applied.

The duration over which each adjustment should apply should seek to recover any shortfall/surplus in a timely manner. On that basis we would support it being applied over two quarterly cap periods. This approach would allow for accurate adjustments to be calculated and for actual costs to be recovered by suppliers in a timely manner, reducing any cashflow and cost of capital impacts. We are concerned that the proposed approach will result in a recovery period that extends to June 2024. This would increase the likelihood that the market has opened up again before suppliers are able to fully recover their costs and so would result in an under recovery of BSUoS charges if significant numbers of default tariff customers moved to fixed products. We ask Ofgem to provide clarity on how suppliers would be compensated for their losses in the event that significant switching to fixed products occurred before June 2024. As set out above, the best way to mitigate this risk would be to reduce the duration of the recovery period.

BSUoS Rate Re-opener

We are pleased to see that Ofgem has acknowledged our concerns around the potential for the Electricity System Operator (ESO) to re-open the 'fixed' BSUoS rate within a cap period and how any potential increase in supplier costs would be captured under the price cap. Ofgem's proposal to review the BSUoS allowance on a quarterly basis and include any additional adjustment resulting from the difference between the initial and revised tariff in a future cap period is a sensible and proportionate approach to addressing the risks faced by suppliers in this respect.

Price cap model

In Appendix 1 Ofgem comment that "*Given that the Energy Prices Act 2022 extends the cap beyond 2023, we intend to reflect this change by extending the cap models to include cap periods beyond December 2023. We plan to carry this out in the next year.*" We welcome clarity on this fact but would also call for Ofgem to undertake this activity before or during the publication of the Q2-23 cap level. Ofgem's quarterly Financial Stress Test requires a price cap view up to and including 2025 and as such a timely extension of the model would be beneficial to this process for suppliers, including making the stress testing efficient, more transparent, and more comparable between suppliers.

Finally, we note that Ofgem state in Paragraph 3.6 of the consultation that the BSUoS component is currently set ex-post as the charges are particularly volatile and the forecast at the time of the 2018 decision were not sufficiently accurate. We consider this argument is equally applicable for the CfD allowance under the price cap where CfD costs have the potential to be more volatile than

BSUoS costs were in 2018. Consequently, we strongly urge Ofgem to consider adopting an alternative approach to amending the CfD allowance that better reflects the risks of LCCC forecasts being materially different to outturn rates and the ability of suppliers to recover/payback their CfD costs/benefits under the cap.

Should you wish to discuss any of the issues raised in our response or have any queries, please contact Steven Eyre or myself. I can confirm that this letter may be published on Ofgem's website.

Yours sincerely

A handwritten signature in black ink, appearing to read "J. Mason", enclosed within a thin black rectangular border.

John Mason
Senior Manager (Price Regulation and Market Dynamics)