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OVO response to Ofgem's Forward Work Programme - 2023/24

Thank you for the opportunity to provide comments on Ofgem's draft Forward Work Programme for 2023/24, we give our general thoughts followed by comments on some specific areas below. We are broadly supportive of the strategic priorities set out and are keen to work with Ofgem, Government and the rest of the industry to meet the ongoing challenges of the energy crisis whilst ensuring the future of the sector is resilient, delivers for customers and enables a successful transition to net zero.

General comments

This is an ambitious programme of work and it would be helpful if there was additional clarity around the timing of these projects to enable suppliers, and others in the sector, to plan internal resourcing for the year ahead and beyond. It would also be beneficial to have assurance that Ofgem are appropriately resourced to manage these projects. Additionally the programme should recognise where projects may need to be reconsidered if there is a need to respond to external circumstances (as has been the case in recent years); we would suggest that given the urgency of the climate crisis and the increasing number of households struggling with the cost of living that Ofgem's primary focus should be on these areas, any programme of work that does not facilitate the net zero transition, or that does not reduce the financial burden on those least able to pay should be a second-order priority.

We note that there are programmes from Ofgem's forward work programme for 2022/23 that have not been carried forward, such as full-chain flexibility - an enabler for net zero and allowing consumers to play a more active role in demand

side response. We are keen to understand whether this has been subsumed into other programmes and, if not, how the objectives set out in last years' forward work programme will be met.

We would like to see how a joined up approach will be ensured across the projects within the forward work programme, recognising the interactions and interdependencies between programmes. For example, we cannot isolate net zero enablers from market reform, and both need to ensure outcomes that deliver fair prices for all consumers and protections for vulnerable groups. As far as possible projects should work in tandem to ensure the right outcomes that place customer benefits at the centre and deliver for the sector overall, this particularly holds true for programmes that are being delivered across multiple organisations where impacts and dependencies may be overlooked.

Ensuring prices are fair

We believe that the most pressing short-term priority for Ofgem, and the industry, at this time of increased energy costs and the ongoing cost of living crisis, is to ensure protections for customers in vulnerable circumstances. There are two key issues that need to be addressed to provide sustainable, long term solutions that support the most vulnerable while protecting other bill payers and allowing for future investment - prepayment meter switching and the introduction of a social tariff. We therefore offer the below suggestions for inclusion in Ofgem's programme of activities to ensure prices are fair.

We have proposed that a new meter switching industry standard should be introduced, establishing what customers should expect when moving from a credit meter to a prepayment meter. This should include clearly agreed, transparent and published processes which customers understand and against which suppliers can be held to account. We also propose that as switching is only used as a last resort, and that these customers should only be moved to smart prepayment meters wherever possible so that suppliers can better understand customers' circumstances and proactively offer additional support to manage usage and debt - traditional prepayment meters should only be used in exceptional and defined circumstances.

We have publicly expressed our support for a social tariff to mitigate fuel poverty and affordability issues, and are keen to work with Ofgem and BEIS to explore options that would allow a social tariff to be implemented with effect from April 2024 when customers will no longer benefit from the Energy Price Guarantee.

As legislation may be required to implement a social tariff, consideration must be given to the Parliamentary timetable, therefore all parties must proceed at pace to develop a robust, workable, and fair solution. We have recently submitted a paper to Ofgem - 'Implementing an Energy Social Tariff' - setting out in more detail our position on the requisite considerations for a social tariff; the key questions that must be answered and policy principles that must drive the process. Any measures to deliver meaningful support must:

1. Aim to reduce the level of fuel-poverty across the UK by being targeted at those that need it most (the most financially vulnerable households), and calculated based on affordability for those eligible, not on the cost of supplying energy to them
2. Minimise cliff edge scenarios where the 'squeezed middle' are overlooked
3. Work alongside other policies and regulations which support households with other vulnerabilities e.g. access or health vulnerabilities, and not impact other industry initiatives or take funding away from other social schemes such as the WHD Industry Initiative and ECO obligation
4. Have a centrally-run eligibility assessment mechanism to ensure consistent support across the industry, and to avoid any consumers who should benefit from missing out
5. Be simple to understand for consumers to avoid confusion and mistrust
6. Protect other non-eligible bill payers both now and in the future
7. Be appropriately funded in a way that incentivizes suppliers to deliver best outcomes for eligible customers
8. Be truly fair, long term and sustainable - it should be politically robust and adaptable to changing economic circumstances
9. Be considered and implementable alongside other proposed retail and wholesale market reforms (e.g. review of the Price Cap, REMA and the Energy Retail Market Review), given the transition that we're on to a fully decarbonised energy sector
10. Be operationally and commercially viable for those involved in scheme delivery and administration, including for energy suppliers and consumer groups

We recognise that a social tariff is not a panacea for supporting customers in vulnerable circumstances, and that broader protections are needed alongside improvements in the accessibility of available support. This is why we are calling for a National Consumer Hub to consolidate the data on vulnerability that is held by various bodies across multiple sectors into a national database. Such a Hub would provide a central point for customer data, protected on a secure Government system, facilitating a "one-stop shop" for vulnerable consumers to access, and apply for, financial and non-financial support. The National Consumer Hub would allow approved/regulated bodies and organisations across sectors to more easily identify households in need of support whether through social tariffs, hardship funds, debt advice, or priority services. We urge Ofgem to progress this solution in partnership with other regulators, Government and relevant stakeholders.

Creating resilience across the energy sector

The provision of financial support to vulnerable customers is only one element in ensuring that bills are fair for all consumers. The structure and operation of the retail and wholesale energy markets have in recent years resulted in increased costs for customers through a combination of supplier failures, increased volatility, and uncertainty created through the significant number of policy and regulatory interventions that have ensued. We believe that regulatory efforts should be targeted in the right areas to maximise benefits for consumers and ensure they do not bear the costs of unnecessary interventions.

We have, in the past, welcomed Ofgem's approach to improve financial resilience in the sector and would commend the success of measures introduced to date which have seen a significant improvement in the ability of the sector to withstand market shocks. Financial stress testing and increased monitoring and oversight have enabled Ofgem to take a proportionate and risk-based approach to target their compliance and enforcement powers allowing for recognition of the difference between how incumbent and challenger suppliers structure their operations, and is consistent with the principles of good regulation. We believe that this approach has been proven successful by the marked decline in the number of supplier failures - there have been no major failures this winter despite difficult market conditions.

However, we remain concerned that the additional steps proposed by Ofgem and included within the FWP, such as ring-fencing Renewables Obligations, will increase costs for customers and are disproportionate given the improvements already made to the financial resilience of the retail market - we have provided further information within our responses to Ofgem's consultations on strengthening financial resilience and the review of the EBIT allowance under the Price Cap. We believe that it would be more appropriate for Ofgem to continue the current approach whilst working with BEIS to reduce volatility and improve market liquidity, making it easier for suppliers to effectively manage risks and thereby reduce overall costs for customers.

Last year we shared a paper with Ofgem titled 'A Plan to Lower Volatility and Lower Costs in the Energy Retail Market'. The paper identified and set out our views on systematic risks that carry significant potential impacts on suppliers and customers. We believe addressing and mitigating these risks, as summarised below, will improve financial resilience of the retail energy market, we are therefore pleased to see that Ofgem's Forward Work Programme also includes an exploration of wholesale power market liquidity issues and we are keen to work with BEIS and Ofgem to develop solutions to mitigate liquidity risks.

| Risk | Mitigation |
|--|---|
| Elevated balancing costs | Establish a new contracts-for-difference type scheme for extreme balancing costs , recovered through a levy charged on all suppliers. |
| Elevated bad debt | Better reflect expected bad debt levels in the Price Cap and implement targeted measures to reduce non-payment across the industry. |
| Sudden falls in wholesale prices leave suppliers 'out of the money' | Strengthen the Market Stabilisation Charge so that, in addition to it enabling the recovery of trading losses on commodity hedges held for customers that switch, it accounts for the under-recovery of costs incurred by the losing supplier that have arisen due to delayed cost recovery mechanisms under the price cap (i.e. backwardation costs). |

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| Electricity shaping costs increase due to poor market liquidity | Improve liquidity and the availability of peak electricity products in the wholesale electricity market by placing an obligation to facilitate the market in such products on an existing body or an independently appointed provider funded through an industry wide levy. |
| Increase supplier exposure to CfD levy payment differentials | Structure all future CfD contracts to minimise the transfer of risks associated with intermittent generation onto suppliers, and align the price cap setting process with actual levies on suppliers. |

Developing and delivering market reforms

Wholesale market and network charging reforms must deliver the right outcomes for flexibility markets. Projects under the banner of this strategic priority must be delivered in tandem to avoid the risk of piecemeal change stifling flexibility markets and innovation and leading to disengagement from customers.

Flexibility markets are vital to a successful net zero transition. Market-wide half hourly settlement and smart metering are key to ensuring consumers can actively participate in providing the flexibility that will be required to meet a zero carbon future led by renewable generation, and while these have been placed within Ofgem's longer term priorities we hope that this does not indicate a lack of urgency for these projects.

The take up of smart metering improves when there are services and products in place that demonstrate the consequential benefits to customers. Market-wide HH settlement will support suppliers in developing these services and products that maximise flexibility and will drive take up of smart metering. We are already undertaking innovative pilots and trials such as our successful 'Vehicle-to-Grid' trial which enabled customers to earn around £420 a year, and our recently announced 'Vehicle-to-Everything' trial, INFLEXION. We know that through the provision of new products and offerings we can support customers in their net zero journeys and in minimising their bills. Ofgem's market reform projects must have customers' interests at the heart of change and ensure that schemes such as INFLEXION can help consumers become active participants in flexibility markets.

We hope you have found our comments helpful, and should you wish to discuss any aspect of our response please do not hesitate to get in touch.

Kind regards,

Nicola Roberts
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