

Duncan Mills
Regulatory Economist
Ofgem
9 Millbank
London
SW1P 3GE
duncan.mills@ofgem.gov.uk

20 March 2007

Your Ref: Ofgem doc 29/07

Dear Duncan

Early replacement of electricity PPMs and removal of electricity metering obligations: Proposed licence amendments

energywatch welcomes the opportunity to respond to the issues raised in the consultation. This response is non-confidential and we are happy for it to be published on the Ofgem website.

We remain strongly opposed to the removal of the electricity metering price controls from 1 April 2007. Responses to previous consultations have highlighted that removal of the controls will not promote any more innovation in metering provision and services than already occurs. There is also scant evidence that competition will increase significantly, given the intention of some suppliers to develop more in-house provision. In fact, this creates the real risk that small suppliers may be forced to take metering services from providers associated with rival suppliers. Furthermore, the proposed changes allow DNOs to pass through a proportion of the costs of retaining legacy (stranded) PPMs to all PPM consumers, who are amongst the most vulnerable consumers, at a time when high retail energy prices do not reflect significantly lower wholesale prices.

In these circumstances, Ofgem ought to have undertaken a thorough review of the extent of metering competition **prior** to deciding on the removal of price controls. This approach would have been far more informative about the development of competition, the extent of any stranded asset problem and the impact in cost terms on consumers, and whether, and how, stranded asset cost recovery would be implemented if this was desirable. Ofgem's proposed intention to review the arrangements within 18 months of removal should also be thorough, and should not preclude the use of effective regulatory action if metering competition does not develop sufficiently in the interim. There must be clarity on the specific measures to be used to determine effectiveness of the removal of the price controls, e.g. whether innovation has increased and by which measure.

From the DNOs' information on the recoverable cost of stranded PPM assets, consumers will be expected to pay around 30p on average (up to £1.20 per customer in some regions). This is a further burden on hard-pressed consumers at a

time of high energy prices and there is a lack of certainty about the recoverable amount, even if Ofgem proposes longer recovery periods. DNOs and suppliers are more than capable of absorbing the full impact of these costs without further recovery from end consumers.

Ofgem also suggests that there may be limited activity in PPM replacement as a result of these proposals. We need clarity about whether proposed PPM replacement programmes are being influenced by an issue such as debt, which has always been a concern for consumers but which has become more prominent with recent energy price rises. If it is the case that PPM replacement is not unduly impacted, there appears to be even less reason for removing price controls if part of the reason for doing so is to stimulate increased metering competition.

We would reject any use of retrospection in the calculation of stranded asset cost recovery. DNOs should only be able to apply forward-looking asset life in the calculation as otherwise there is an uncertain liability for consumers if they are expected to cover a proportion of the cost recovery. It would create an unfortunate precedent if end consumers are also expected to bear such costs in other areas. We continue to reject any recovery of any of these costs from consumers who have no control over the timing and speed of PPM replacement, regardless of the assurances provided to DNOs about stranded protection during the last distribution price control. These costs can be better absorbed elsewhere.

We are concerned that stranded asset cost recovery will be provided when the replacement PPMs use existing (token, key or smartcard) technology. There can be no benefit to affected PPM consumers of long-term replacement with older technology which fails to assist them in understanding their energy usage and costs, particularly when energy efficiency should be promoted by suppliers amongst households. There is a further risk that smarter metering, which may assist domestic consumers to more effectively understand their energy requirements, may be rolled out more slowly because there is no cost recovery proposed and, therefore, little incentive to use it for replacement PPMs.

We believe that robust guidelines are needed on stranded asset cost recovery, which allow DNOs to apply for only clearly permissible costs after early PPM replacement. DNOs should provide as much evidence as possible in support of an application. The guidelines must not introduce uncertainty into the process of calculating cost recovery given that Ofgem proposes that 30% of the recoverable costs are shared by consumers.

While DNOs retain the ability to offer metering services, there should be effective regulation through the licence to ensure that anti-competitive practices are prevented. Separation of metering services would increase their transparency but we accept that it is not desirable to implement separation in the short term.

We note the proposed licence changes which appear to reflect Ofgem's intention as set out in the consultation. We have no specific comments on the changes.

Going forward, we will continue to keep these issues under review as and when they are raised, always considering the possible impact on consumers.

If you do wish to discuss our response further please do not hesitate to contact me on 0191 2212072.

Yours sincerely

Carole Pitkeathley
Head of Regulatory Affairs