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Gemserv, MRA Parties

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**Decision by the Authority to uphold the appeal by Utilita regarding Master Registration Agreement (MRA) CP 130 "Treatment of prepayment revenue which cannot be allocated"**

## Summary

On 28th June 2012 the MRA Forum met to consider appeals from EDF and Utilita against the decision of the MRA Development Board to implement CP130 (the Change Proposal). The Forum voted to reject the appeals. Utilita subsequently appealed that decision to the Authority in accordance with clause 7.26 of the MRA. The Authority issued a letter on 1 October 2012 setting out the process the Authority would follow in taking a decision and inviting written representations.

We have carefully considered the Change Proposal and the representations received. We have had regard to standard licence condition 23.3 of the Electricity Distribution Licence[1] and the Authority's wider statutory duties[2]. We have decided to uphold the appeal. The effect is that the Change Proposal cannot be made.

## Background

SSE raised a change to the MRA[3] on 1 March 2012. The modification is designed to deal with approximately £26m that is being held by Pre Payment Meter Infrastructure Providers (PPMIPs). This sum is classed as Unallocated[4] as the PPMIP does not have sufficient information to allocate payments to the correct supplier.

The modification is intended to introduce an algorithm for distributing unallocated money that has remained unallocated for more than two years amongst suppliers, based on their market share. Suppliers and PPIMPs would be informed by the MRA secretariat of the results of the calculation and PPIMPs would distribute the money they held in accordance with that calculation. Suppliers would have an obligation (through their contract with the PPMIP) to require the PPMIP to follow the MRA procedure. It is anticipated that this 'Allocation Run' would take place annually but the frequency and the decision to initiate an Allocation Run would be subject to the discretion of the MRA Executive Committee.

[1] The relevant provision is "23.3 (f) such other matters as are or may be appropriate for the development, maintenance, and operation of an efficient, co-ordinated, and economical system for the supply of electricity and for the purpose of facilitating competition in electricity supply."
[2] Ofgem's statutory duties are wider that the matter that the MRA Development Board must take into consideration and include a principle objective to protect the interests of consumers by promoting competition where possible.
[3] MRA Approved Procedure 14 (MAP14) sets out the arrangements for dealing with unallocated and misdirected payments. It requires supplier to ensure that their PPMIPs follow the requirements of the MAP.
[4] This is distinct from 'Misdirected' payments where the PPMIP will allocate payments based on a payment device that is not related to the consumer's current supplier.

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The 'Business Justification' for the modification set out on the MRA MAP Change Proposal form included the statement *"...it is hoped that this change will provide an incentive to allocate prepayment monies in a timely manner*."

The modification was considered at the 12 June meeting of the MRA Development Board and approved.

Two suppliers, EDF and Utilita, appealed (to the MRA Forum) the decision to approve the modification. The MRA Forum met on 28th June and rejected both appeals. Utilita subsequently appealed the decision of the MRA Forum to Ofgem. Ofgem issued a letter on 1 October 2012[5] setting out the arrangements for dealing with the appeal and inviting MRA parties to make a written representation. We invited respondents to consider the following questions:

a) Does the formula to re-distribute PPMs unallocated transactions better facilitate competition in electricity supply, in accordance with Standard Licence Condition 23 of the Electricity Distribution Licence?
b) Is there a more efficient and economical way to re-distribute these unallocated transactions, which would better facilitate competition in the supply of electricity?
c) Is the industry trying to find other ways of solving the issue of unallocated PPMs transactions?
d) Do you consider that this change aims to introduce an incentive on parties and, if so, do you think that the effect of this incentive would be retrospective?

**Representations**

Ofgem received five representations, four from suppliers (one of which was marked confidential) and one from Consumer Focus.[6]

Consumer Focus stated that they "...agree with and support the *intentions* of MAP CP 130" (italics added). They noted the inefficiencies of the current arrangements and that the issue would not arise with smart metering. They added that they had written to large suppliers proposing that the money that became available as a result of CP130 being adopted should be used for hardship funds operated by suppliers in respect of vulnerable consumers.

Two suppliers argued that the Change Proposal CP 130 should be made and two that it should not (and therefore that the appeal should be upheld).

*a) Does the formula to re-distribute PPMs unallocated transactions better facilitate competition in electricity supply, in accordance with Standard Licence Condition 23 of the Electricity Distribution Licence?*

Arguing for the Change Proposal, one supplier suggested that there are processes available to suppliers to recover money from the Unallocated Prepayment Revenue pot and that others have failed to take advantage of these processes. They noted that the Change Proposal would result in unallocated revenues being distributed on the basis of market share and therefore would better facilitate competition.

Those arguing against the Change Proposal thought that the use of a simple market share approach for distribution "could be seen as prejudicial to small suppliers". They cited that small suppliers will be more exposed to changes of supplier and meter exchanges that may cause transactions to be unallocated.

[5] Notice of Utilita Appeal Against MRA Forum Decision Regarding MAP CP130 http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=120&refer=Licensing/ElecCodes/MRA

[6] The non confidential responses have been published on our website: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=120&refer=Licensing/ElecCodes/MRA



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*b) Is there a more efficient and economical way to re-distribute these unallocated transactions, which would better facilitate competition in the supply of electricity?*

Suppliers arguing for the Change Proposal noted that, as the data needed to correctly allocate the transactions became older, it became increasing costly to investigate and the results less reliable. Therefore a cut-off after which an allocation would take place was efficient.

This was in part supported by those suppliers opposed to the Change Proposal. One stated that they would welcome further discussion on a better solution. They recognise that ultimately sums will have to be divided where the data does not exist but suggest 5 rather than 2 years for the historic cut-off. They noted that the underlying causes of unallocated transactions should be addressed. One supplier suggested that the allocation mechanism should only take account of supply points where a change of supplier had taken place.

*c) Is the industry trying to find other ways of solving the issue of unallocated PPMs transactions?*

The broad view was that considerable effort had been put into resolving this problem. However, one supplier thought that further work should be done to understand better the approach for resolving both unallocated and misdirected transactions.

*d) Do you consider that this change aims to introduce an incentive on parties and, if so, do you think that the effect of this incentive would be retrospective?*

There were mixed views from suppliers as to the incentive effect the Change Proposal would introduce. One supplier who supported the modification considered that it would introduce an incentive for a supplier to "reduce their exposure to any potential re-distribution of funds". Another disagreed and stated that it may lead suppliers to rely on the allocation mechanism rather than put effort into resolving the unallocated transactions if they thought they may benefit from the allocation.

**The Authority's decision**

We have decided to uphold the appeal raised by Utilita to the Change Proposal [with the effect that MAP CP 130 may not be made].

**Reasons for our decision**

We note that the current arrangements that support the operation of electricity prepayment meters give rise to both misdirected and unallocated payments. Efficient solutions that industry participants have confidence in are needed to resolve the problem. It is clearly not efficient to have significant sums of money being held by PPMIPs rather than being allocated to the correct supplier.

Where the data available to PPMIPs and suppliers is inaccurate or missing so as to prevent the correct allocation of payments, we accept that it would be appropriate for an allocation procedure to operate in such a way that would ensure that the payments are made to those suppliers who are most likely to be entitled to them.

However, there are features of the Change Proposal where there is insufficient evidence to assess whether this approach achieves this aim and there are risks of unintended consequences were the Change Proposal to be made.

The introduction of a retrospective incentive carries with it the risk that winners and losers from the allocation mechanism will be decided by chance rather than suppliers being able to properly assess the risks involved to take the necessary steps to manage those risks.



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Were the Change Proposal only to deal with unallocated transactions that were to occur in the future, then industry participants would be able to prepare and invest in the necessary arrangements to take advantage of the new arrangements.

However, as it is also aimed at dealing with the sums currently held by PPMIPs, there is a risk that the allocation mechanism will unduly reward suppliers who may not have been exposed to the same degree of customer switching and are therefore less likely to have incurred loss through unallocated prepayment transactions.

This is particularly acute given the claims by some respondents that the Change Proposal would operate against the interests of small suppliers or new entrants with substantial volumes of prepayment meters. Again, there is no evidence to suggest that the Change Proposal has been devised with due consideration to the effect of changes of supplier or changes of meters as being the root cause of unallocated transactions and whether those factors should be reflected in the allocation mechanism. Without that assessment there is a risk that the allocation mechanism may operate to the benefit of some suppliers and the detriment of others.

Therefore we cannot conclude that the Change Proposal would better facilitate competition as required by standard licence condition 23.3 of the Electricity Distribution Licence.

Additionally, we have concerns as to the robustness of the drafting of the proposed modification.

The Change Proposal relies on change to the text of MRA Agreed Process (MAP) 14 "Procedure for the Allocation of PPM Payments Transacted Against and Incorrect Device". We are concerned the text of the Change Proposal does not set out a clear and robust description of the process. In particular we note that:

- The Market Share Report[7] determines the method by which the market share is calculated, based on the number of MPANs for each supplier associated with different prepayment meter technologies. However it is not specific as to the point in time that market share is assessed. Whilst we have no particular view as to which date should be chosen, without certainty on this point there will significant ambiguity as to how the MRA Secretariat[8] should prepare the Market Share Report.
- The linkage between the drafting of the change to MAP 14 Appendix 3 "Transaction Reporting" and the definition of an unallocable prepayment transaction defined in 2.7.3.1 is unclear.

We consider that these issues are essential to the interpretation of how the allocation methodology is intended to operate. As currently written the rules are ambiguous and open to interpretation.

Given the weaknesses in the drafting of the modification to MAP 14 that would be introduced by the Change Proposal, we cannot conclude that the Change Proposal better facilitates an efficient, co-ordinated, and economical system required by standard licence condition 23.3 of the Electricity Distribution Licence.

[7] The Market Share Report is introduced by the Change Proposal as a modification to the text of MAP 14 at clause 2.7.3.2

[8] The Change Proposal requires the MRA Secretariat to perform the calculations necessary to prepare the Consolidated Allocation Run Report that determines the shares of unallocated transactions.



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**Recommendations**

Consideration should be given to what further work could be undertaken to managing the problem of unallocated prepayment transactions. We would ask MEC (pursuant to Clause 9.6.1 of the MRA[9]) to consider the following:

1. That a modification proposal to the MRA be developed to introduce a methodology for the allocation of unallocated prepayment transactions.

2. That the modification proposal be accompanied by analyses confirming how it will better facilitate the requirements of the MRA as stated in Standard Licence Condition 23 of the Electricity Distribution Licence.

3. Whether independent advice should be sought as to whether the arrangements governed by the MRA for dealing with both unallocated and misdirected prepayment transactions are appropriate for achieving the requirements of the MRA, as stated in Standard Licence Condition 23 of the Electricity Distribution Licence, and securing the confidence of MRA parties.

4. Whether there is any action that MEC or other governance bodies should be taking to limit and reduce the occurrence of unallocated or misdirected prepayment transaction.

We look forward to receiving confirmation from MEC that they will consider these issues.

**Colin Sausman**
**Partner, Retail Markets and Research**
Signed on behalf of the Authority and authorised for that purpose

[9] Clause 9.6.1 of the MRA states: *"[MEC shall] give due and prompt consideration to any matter referred to it in writing by the Authority".*



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