

Diego Villalobos
Senior Economist
Ofgem
9 Millbank
London
SW1P 3GE

Regulatory Affairs
1st Floor, Lakeside West
30 The Causeway
Staines
Middlesex
TW18 3BY

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Dear Diego,

Review of typical domestic consumption values

1. We welcome Ofgem's review of the Typical Domestic Consumption Values (TDCVs). These values play an increasingly important role in the industry today, from their use in defining the cost of a particular tariff at 'average' consumption to their use in various impact assessments and economic models. It is therefore important that Ofgem ensure they genuinely represent 'typical' domestic consumption as much as possible. Given the focus on improving the energy efficiency of domestic premises, and the consequential reduction in levels domestic demand, it is right that Ofgem are review the values used and how they may be maintained in the future.
2. We also strongly welcome the decision to use the values eventually agreed through this review in informing the assumptions used in the weekly Supply Market Indicators¹ (SMI) report. The SMI is taken by customers and commentators alike as an indication of the level of profit earned in the retail market today. The model currently assumes a far higher level of domestic consumption than we believe accurate, with the impact being that the estimated profit margin reported in the SMI is higher than that actually earned. Ofgem's decision to update these values in the autumn should improve this situation materially.
3. We have provided detailed comments on the proposals below. We have also highlighted a number of areas where we have concerns about the proposals, and hope Ofgem will take this opportunity to address them.
 - We agree with the proposed TDCVs, and ask Ofgem to implement them as soon as possible. We agree with the methodology Ofgem have used to reach the revised TDCVs, and the proposed values themselves. We also welcome the decision to use them to update the SMI methodology. Given the importance these values play in consumer decisions regarding tariff selection, energy policy impact assessments and the SMI margin estimates, Ofgem should move to implement the new values as soon as possible.
 - The methodology should be refreshed annually, not every two years as proposed. Whilst we appreciate the administrative impact associated with more regular reviews of the TDCVs, the benefits of more accurate TDCVs outweigh the potential administrative costs associated with more regular updates to the values. We therefore believe that the TDCVs should be updated annually, based on a rolling two year historic view of consumption.

We agree with the proposed TDCVs, and ask Ofgem to implement them as soon as possible

¹ Review of typical domestic consumption values, page 1.

4. We agree with the methodology Ofgem have proposed for calculating the TDCVs, and believe that they will result in a more accurate set of values than are used today. The proposal to use the DECC sub-national energy consumption statistics as the source for the TDCVs is particularly welcome, and will ensure that the resulting data is underpinned by robust quality control.
5. We also agree with the proposals use the median, rather than the mean, consumption value to set the TDCVs. Ofgem's data highlights the impact that estimated accounts with little previous consumption history can have on the mean consumption value², and how that would in turn undermine the resulting TDCVs. Using the median value will avoid this risk and provide a more accurate outcome.
6. We also recognise the trade off between using more or less historical consumption data (i.e. volatility versus ability to accurately capture demand destruction), and agree that Ofgem's proposal to use the last two years consumption data strikes the right balance.
7. Having agreed with the methodology Ofgem have proposed using, we also find that the resulting TDCVs are broadly consistent with our own view of 'typical consumption' and represent a material improvement on the current values. These values will improve the quality of tariff information given to customers (including in the proposed Tariff Comparison Rate), will improve the quality of policy decisions based in part on assumed consumption values, and provide a more accurate view of supplier profit margins through an updated SMI methodology. We consider these benefits are all material, and therefore urge Ofgem to implement these new values as soon as possible.

The methodology should be refreshed annually, not every two years as proposed

8. We welcome Ofgem's suggestion that there should be a regular review of the TDCVs in future. We are however concerned that – given energy demand is reducing between 4-7% per annum, depending on the underlying economy and weather - a review every two years will allow the TDCVs to become materially inaccurate. This risks impacting the accuracy of the proposed Tariff Comparison Rate, has potential impacts for any policy impact assessments based in part on a view of average consumption, and may lead to inaccuracies in the estimation of supplier margins.
9. Given this, we place a premium on accuracy over administration. We therefore argue that Ofgem should commit to providing annual reviews, based on a rolling assessment of the last two years historic consumption data. This will ensure that the TDCVs remain as accurate as possible.
10. We recognise that this may have an impact on those organisations, like suppliers, who use the TDCVs for purposes such as tariff comparisons. The measures Ofgem have set out in this review however, such as a commitment to provide sufficient notice of the new values and a set date from when the new values will apply from, mitigate these concerns, and enable annual updates.

Conclusion

11. We welcome the proposed new TDCVs and believe they are broadly accurate. They will have a material benefit in the market, and as such, they should be implemented as soon as possible. Given the importance maintaining accurate values has, Ofgem should consider moving to annual reviews of the TDCVs.
12. If you would like to discuss this response, or require any more information on the points made within it, please do not hesitate to telephone me on 07789 570501.

Yours sincerely

David Watson

Head of Market Design & New Energy, British Gas

² Review of typical domestic consumption values, paragraph 2.12.