



OVO Energy response to Ofgem's Open Letter - Half Hourly Settlement: the way forward

29th January 2016

EXECUTIVE SUMMARY

OVO broadly agrees with the points raised by Ofgem in the Open Letter. We view moving to elective half-hourly settlement (**HHS**) as essential to fully unlocking the potential of the smart meter rollout and are keen to play an active role in facilitating the transition at the earliest feasible opportunity. While we believe the benefits of HHS are clear, we have concerns with regard to the proposals to introduce mandatory HHS via a significant code review (**SCR**). We think that the focus should be on solving the operational issues associated with enabling elective HHS before any decisions are made on the need to introduce mandatory HHS.

This response contains a description of the issues we believe need to be overcome in order to facilitate the transition to HHS in a cost effective manner. OVO wish to make it clear that in spite of the number of issues we outline in this response, we are confident that the existing code and industry governance procedures are sufficient to effect the changes necessary to introduce cost effective HHS. We would therefore strongly advise Ofgem against using a significant code review as a means of effecting the changes we describe as necessary.

OVO also believe that the focus should be on developing processes that will function effectively and independently of other major operational changes, such as DCC Go Live. This would ensure that elective HH Settlement is not dependent on these projects, which could be subject to delays. Processes should be designed to be equally effective for SMETS1 and SMETS2 meters to avoid early movers in the Smart Meter roll out being penalised.

Throughout this response we have divided the list of issues we identify as barriers to cost effective HHS into three broad categories: operational and system related issues, cost related issues, and social and regulatory issues. These categories are not intended to be mutually exclusive however.

OPERATIONAL AND SYSTEM RELATED ISSUES

Change of Measurement class

- The Change of Measurement Class process used to switch a site to HH settlement needs to be reviewed. In particular, the process needs to be able to deal with sites switching in and out of HHS and also be able to handle Change of Tenancy and Change of Suppliers. It may also be necessary to ensure that processes can deal with situations where a Change of Measurement Class needs to be applied retrospectively.

Half hourly data and system capacity

- There currently exists a sizeable cost barrier in relation to the appointment of a HHDC agent compared to the NHH equivalent. We are supportive of the Settlement Reform Advisory Group's (SRAG) recommendations relating to the requirements of HHDC agents for HHS domestic customers and feel they are likely to bring down costs. However, further clarity is required in this area, in particular relating to how suppliers should get HH data from the meter and into settlement.
- We also have concerns regarding the capability of central systems to cope with a significant take up of elective HHS. If it transpires that this is a major constraint then planning for any upgrades should start now.

Use of half hourly data in settlement

- Section Removed

COST ISSUES

The effect of FiT spill on GCFs

- A significant amount of output generated by installations supported by Feed in Tariff (**FiT**) is unmetered. During periods of high FiT output, the increased quantity of unmetered electricity can significantly depress the value of the group correction factor (**GCF**) within the relevant grid supply point (**GSP**) region. A reduction in the value of the GCF decreases

the settled, and hence billed, volumes meaning that all profiled sites within a given region benefit from a decreased GCF.

- GCFs are not currently applied to a HHS customer, therefore HHS customers will forgo this benefit. Forgoing this benefit represents an opportunity cost to switching a domestic customer to HHS. While the long term solution is clearly to have all FiT installations metered, a short term solution would be to continue applying GCFs to HHS domestic customers. We believe this can be achieved by changing the scaling weight applied to measurement class F in the settlement calculations.

TNUoS charging

- We believe that charging Transmission Network Use of System (**TNUoS**) on Triads is not suitable for HHS domestic customers and creates an unnecessary risk to both suppliers and customers. Our proposal is that the existing non-half hourly (**NHH**) charging mechanism be applied to elective HH settled domestics (i.e. consumption in settlement periods 33-38). We believe this change strikes the correct balance between maintaining an incentive to shift load away from peak periods, without exposing domestic customers to the risk of punitive charges.

BSC cost recovery

- The costs associated with the operation of the BSC are recovered through the BSC Specified Charges mechanism. Currently the charge is £0.6 per site per month, being approximately ten times that for an NHH site. We understand that the cost is expected to reduce following the introduction of P272, however cost parity between domestic customers settled half hourly and non-half hourly is essential. We propose that that elective HHS domestic customers are charged the same as NHH customers.

SOCIAL AND REGULATORY ISSUES

Vulnerable customers

- We have concerns that the movement of a subset of customers to HHS may increase costs for customers that remain settled via profiling. Our specific concern is that many of the customers that remain settled via profiling might be inactive and/or vulnerable. We believe it is crucial to the timely implementation and success of HHS that the likelihood of any negative distributional effects on vulnerable customers is well understood and can be easily mitigated, with perhaps a well targeted social policy.
- With regard to mitigating any adverse effects associated with the movement of domestic customers to HHS, we have consistently called on the CMA to introduce a remedy specifically targeted at vulnerable customers. In light of the CMA's proposal to introduce a safeguard tariff, we are confident that this remedy would adequately protect vulnerable customers from being subject to the distributional effects associated with a move to HHS, such as higher peak energy prices.

Regulatory issues

- The compatibility of certain regulatory requirements with HHS needs to be reviewed. Customer demand for new products will determine the success or failure of transitioning to HHS. It is therefore important that market rules, such as RMR, or rules that prescribe specific technologies, such as the requirement to install in home displays (**IHDs**), do not continue to hamper innovation and product development.

NEXT STEPS AND RECOMMENDATIONS

We believe that the Settlement Reform Advisory Group (SRAG) has made good progress in addressing a number of the issues we have outlined but much more work is required to build on this to fully enable elective HHS. We encourage Ofgem to set up a working group to progress all outstanding issues immediately to avoid any loss of momentum and OVO would be very keen to be represented on any such group.

We believe that the focus for Ofgem and the industry at this time should be on enabling and incentivising elective HHS as opposed to planning for mandatory HH Settlement. For this

reason we do not think a significant code review is an appropriate avenue to effect the necessary changes.

We are also supportive of the draft legislation to give Ofgem increased powers to make the changes necessary to facilitate elective HH settlement in a timelier and more cost-effective fashion.

In light of the foreseeable benefits to introducing HHS for domestic customers, OVO is keen to play an active role in solving the issues we have raised in this response. We are more than willing to continue discussing any of the solutions we have proposed further with Ofgem and have attached our contact details in the hope that Ofgem will continue to engage with us throughout all phases of the transition to HHS.

Yours sincerely,



Stephen Harris

Trading Director, OVO ENERGY

Please use the following email address if you wish to discuss our response further:
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1. INTRODUCTION

BENEFIT OF INTRODUCING HALF HOURLY SETTLEMENT (HHS)

- 1.1. OVO believes that introducing HHS represents a major opportunity to significantly reduce energy costs to domestic energy customers. OVO also envisages that the

move to HHS will unlock the potential of the smart meter rollout, facilitating Demand Side Response (**DSR**) and creating the demand for other innovative products that will allow the Smart Meter roll out to succeed fully.

- 1.2. Allowing customer's consumption to be settled half hourly is a more accurate and cost reflective way of operating the energy market. The cost to supply a customer would accurately reflect the periods of the day in which the energy was actually consumed. Those customers who are successful in shifting their consumption patterns should benefit as their collective actions are contributing to the achievement of all three of the so called energy policy pillars; improving security of supply, reducing carbon emissions and reducing the price of energy.
- 1.3. With careful planning and design of the means by which HHS is enabled, all customers should benefit from having the ability to alter and reduce their energy consumption. If done correctly, the introduction of HHS should spawn a virtuous cycle, whereby the existing energy infrastructure is used more efficiently, reducing the cost of maintaining and upgrading it. This in turn should ultimately decrease the system costs for all, allowing customers to realise these savings and further prompt them to engage in additional beneficial behavioural and consumption changes.
- 1.4. In light of these benefits, we welcome Ofgem's open letter on HHS, particularly the focus on removing the barriers to elective HHS as the means of effecting the transition. Introducing HHS on an elective basis provides all industry parties with the opportunity to "learn by doing" and encouraging a level of innovation that should result in a sizeably more competitive retail market.
- 1.5. The final point we wish to make with regard to the benefits of introducing cost effective HHS is that we believe the changes can be made relatively swiftly using the existing code governance system, with perhaps some guidance from Ofgem. We think there is potential for suppliers to effect the transition of the first tranche of customers to HHS by the end of 2016. In light of this timeframe it is clear that other major

operational changes must remain decoupled from the ability to implement HHS in a timely manner.

IMPORTANCE OF DECOUPLING HHS FROM DCC LIVE

- 1.6. OVO believe that the focus should be on developing processes that will function effectively prior to DCC Go Live to ensure that elective HH Settlement is not dependent on the DCC Project. All processes should therefore be designed in such a way as to be equally effective for SMETS1 and SMETS2 meters to avoid early movers in the Smart Meter roll out being penalised.
- 1.7. As such we were heartened that Ofgem drew specific attention to the importance of incorporating existing meter types into a half hourly solution, and SMETS1 specifically, in its open letter dedicated to introducing domestic HHS¹
- 1.8. We note however, that the primary focus of the SRAG was the facilitation of smart meters enrolled with the Data and Communications Company (DCC) being settled half hourly. We would therefore caution Ofgem against making the introduction of elective HHS dependent on the date the DCC goes live. Our concern in this regard relates to:
 - a) The potential for the DCC live date to be delayed once again, and
 - b) Our assertion that any processes introduced to enable HHS must not discriminate between SMETS1 and SMETS2 meter types.

BENEFIT OF AN ELECTIVE APPROACH

- 1.9. Building on our assertion that the transition to HHS should be pursued on an elective basis, we would not support the introduction of mandatory HHS, particularly if the proposal was to deliver the necessary industry changes via a significant code review (SCR).

¹ Ofgem (2016); Half-hourly settlement: the way forward

- 1.10. Customer demand for innovative products should be the driving factor behind introducing HHS. Allowing suppliers to innovate and offer compelling products facilitates the demand pull that will make such a transition successful. OVO's concern is that if the transition to HHS is made mandatory then the focus will shift from creating an attractive customer offering, to focusing on trying to simply solve the sizeable operational challenges associated with a big bang approach go live date.
- 1.11. With regard to the potential for Ofgem to launch a HHS based SCR we are aware that DECC has recently published draft legislation to provide Ofgem with powers to directly modify industry codes and to facilitate major industry changes such as faster switching and HHS. We wholeheartedly support these changes and consider them to be the most appropriate means of effecting the changes to bring about elective HHS.

STRUCTURE OF THIS RESPONSE

- 1.12. The purpose of this response is to outline the barriers to elective half-hourly settlement that we have identified. Many of the issues we describe below have featured prominently in the detailed end-to-end review of the HHS process carried out by SRAG.
- 1.13. Our understanding is that SRAG are due to report on their findings to the BSC Panel on 11th February 2016 with a broad range of recommendations and concrete actions to remove the issues associated with moving to elective HHS. We are confident that the implementation of SRAG's recommendations will go a long way towards achieving cost effective HHS.
- 1.14. That said, a number of issues that we raise in this response were out of the scope of the SRAG's review - and thus are left to other industry bodies to solve. As a result we feel it is worth highlighting areas of significant uncertainty that remain a barrier to elective HHS. By way of summary, at the end of each section we have listed the issues as we see them and highlighted what we believe to be the next steps required for their resolution.

- 1.15. In this response we have organised our description of the various issues under three broad headings. They are; operational and systems based issues, cost related issues and social and regulatory issues. These categories are not intended to be mutually exclusive however.

2. Operational and systems based issues

CHANGE OF MEASUREMENT CLASS (COMC)

The issue outlined

- 2.1. The Measurement Class (MC) is the method by which metering systems are classified; as per BSC Modification P300 there are seven MCs. In the domestic market "A" is for standard NHH sites and "F" is for elective HH sites. Therefore, in order to settle a domestic customer on a HH basis the CoMC process needs to be followed to make the change from A to F.
- 2.2. Currently the CoMC guidance is heavily focused on the implementation of P272, i.e. the mandated HH settlement of PCs 5-8. The guidance is dense, unsuited to the domestic market and there is some uncertainty in application of the process to domestic sites where the smart meter is already in place. In addition, the current CoMC process following meter registration agreement working practice 66, is a complex set of processes requiring multiple data flows to be sent to multiple parties with tight time constraints.
- 2.3. Another area of concern relating to the existing CoMC process is the likelihood of issues arising from the Change of Tenancy (CoT) and Change of Supplier (CoS) processes and their interaction with the privacy framework for a customer's HH data. As discussed above, the current processes have been developed for traditional HH

meters and the mandated HH settlement as per P272. In addition, the focus of the SRAG was on the processes to get meters into HHS and did not consider in detail the processes for swapping a customer in and out of HHS.

The effect of this issue on elective HHS

- 2.4. It is generally recognised that the current CoMC process requires a great deal of manual oversight, intervention and overhead. A number of timing issues arise when there is a meter exchange at the same point as the CoMC. While this may not be an issue for the majority of domestic elective CoMCs (since the smart meter is likely to be already installed), the scale of the domestic market requires that processes need to be designed to be as simple as possible. This high level of coordination and manual oversight is unsuited to the scale of the domestic market and will present a considerable barrier to processing a large number of HH domestics.
- 2.5. It is conceivable that a site may move in and out of HHS and the processes need to be able to efficiently cope with this. The current solution is unworkable for such circumstances and, further, it is unclear whether the current central systems could cope with the volume of such switches.
- 2.6. Additionally, we have concerns with the lack of clarity surrounding the Change of Tenancy (CoT) process will operate. The SRAG have noted some of the issues but have not presented any concrete proposals for how to proceed. The responsibilities of the supplier are currently unclear for many of the common CoT scenarios where the data preferences of the incoming and outgoing tenants differ or are unknown.
- 2.7. Similar issues arise in relation to the CoS process, particularly if the new supplier is not set up to deal with HHS. The concern therefore is that a supplier on the receiving end of a CoS will be unclear whose responsibility it is to process the CoMC. It is clear therefore that the interaction of the CoMC process with the CoT and CoS processes present considerable barriers to the progression of elective HHS.

2.8. In summary, it is clear that the current processes of moving domestic customers into elective HHS at any appreciable scale are currently unworkable.

The solution to this issue

2.9. We propose that the CoMC process be reviewed and simplified to address these issues. However we are unclear as to which industry body should be made responsible for achieving this. In addition, it is absolutely essential that any improvements to the CoMC process work seamlessly for both SMETS1 and SMETS2 meters. While the SRAG have stated this intention, there is uncertainty around how this will be achieved in practice.

2.10. A pragmatic approach could perhaps be to default all CoTs back to NHHS - however this approach will lead to a considerable volume of CoMCs and is suboptimal. Moreover the fact that a CoT has even taken place is often discovered by suppliers considerably after the fact. In cases where the incoming and outgoing tenants have different data preferences it unclear under which regime the incoming customer should be settled and from which dates. Questions such as these remain unresolved and given that CoTs represent approximately 20% of the switching market, it is clear that this is an issue that cannot be ignored.

Issue Summary: Change of Measurement Class	
Issue Outline	CoMC process is not designed to cope with the volumes that will be likely should domestic customers elect for HHS en masse.
Effect of this issue on HHS	The current CoMC process creates numerous operational problems that may restrict the ability of customers to change tenancy or supplier
Solution	Ofgem to find the best means of altering the CoMC process Further thinking required on the issue of CoTs and CoSs

Section Removed

APPOINTMENT OF THE HHDC

Issue Outline

- 2.11. In the traditional HH market the role of the HHDC is to collect, validate and process data from metering systems to determine the consumption to feed to settlement. Currently HHDC agency costs are in the order of £50 per HH meter per year compared to approximately £2 for a NHH site. The cost differential as it currently stands makes it uneconomical to switch sites to elective HHS.
- 2.12. While we recognise that such matters are between a supplier and their agents, any uncertainty surrounding the roles and responsibilities of both the supplier and the HHDC agent for elective HHS will result in increased costs.
- 2.13. We welcome the SRAGs recommendations on data validation, protocol testing and proving testing. Given that domestic smart meters are built to the SMETS specifications we feel that it is appropriate that the obligations on suppliers and their agents are softened in comparison to traditional HH metering systems. These recommendations should go a long way to address the cost differential.
- 2.14. That said, we feel there is still considerable uncertainty in the precise obligations on both supplier and their agent. The SRAG recommends that the supplier is responsible for error validation resulting from alerts as well as being able to validate the data itself. It is currently unclear what additional requirements, such as being accredited and/or audited, will be imposed to allow the performance of these functions.
- 2.15. Finally, another significant issue is the fact current HHDC systems are designed to cope with the traditional, relatively small, HH market. The introduction of P272 will have led to systems development to cope with the additional 170,000 or so meters

entering the market. However, it is not clear whether the current HHDC agent's systems could cope with the scale associated with the domestic market. The lead time on any systems development on the part of HHDCs may act as a barrier to progressing elective HHS in the short term.

The effect of the issue on elective HHS

- 2.16. The uncertainty surrounding the definition of the role and responsibilities of the HHDC makes it unclear as to what the likely costs are for securing HHDC services. In the case where the marginal benefit of switching a customer from NHH to HHS, is small any uncertainty related to a particular cost makes it likely that a risk averse supplier would not consider switching such a customer.

The solution to this issue

- 2.17. The SRAG have made significant progress in the removal of the short term barriers, which we support, however the lack of clarity in the medium to long term still presents a significant impediment to meaningful progress. We welcome the SRAG's recommendations surrounding proving tests, protocol testing and site visits for SMETS meters.
- 2.18. While we support the SRAGs recommendations, we feel that there is further progress to be made in ensuring the submission of HH data into settlement works efficiently at the scale of the domestic market. The SRAG's recommendations propose that existing validation and estimation methods (designed for traditional HH metering systems) can be applied to HH domestics. We believe there is further scope to simplify these procedures. Given the fact that the specifications of domestic smart meters are standardised, the role of both the supplier and the agent should be to submit the data into settlement as seamlessly as possible. The need for data validation and data estimation for HH domestics will still exist, however the process should be reviewed to be as simple and as effective as possible.

2.19. The SRAG have discussed the possibility that in the future there is the scope for a new agent role to perform both the DC and DA roles for HH and NHH meters. This proposal seems sensible and could allow such an agent to avail of economies of scale which presumably would reduce the overall industry cost.

Issue Summary: Appointment of the HHDC	
Issue Outline	No clear definition of the role of the HHDC, uncertainty whether existing HHDC system is scalable
Effect of this issue on HHS	Uncertainty with regard to costs of securing HHDC services
Solution	Build on SRAG work, Ensure that the requirements for HH data submission are made clearer

3. COST RELATED ISSUES

FIT SPILL AND THE EFFECT ON GCFS

The issue outlined

- 3.1. In the UK electricity market the Group Correction Factor (GCF) is used in settlement to ensure that the total electricity allocated to suppliers in each of the GSP regions is equal to group take (the net electricity consumption within each of these regions). The GCF is only applied to consumers with non-half hourly (NHH) meters (predominantly domestic customers) via the profiling process used in settlement for volume allocation.
- 3.2. These demand profiles are relatively simple and the GCF acts to correct profiling errors while also sweeping up unallocated/erroneous volumes from sources such as theft, meter read errors and unsettled microgeneration. In a perfect world the sum of

HH and profiled NHH consumption would match the group take and the GCF would be 1.

- 3.3. In recent years however, large volumes of unmetered export energy from feed in tariff supported sites (particularly solar installations) have been 'spilling' on to the network and have resulted in GCFs as low as 0.7 at solar peak. This effect has resulted in annual GCFs averaging to less than 1 thus reducing settled NHH volumes and resulting in the distribution of 'free' FiT energy to NHH sites.

The effect of the issue on elective HHS

- 3.4. The GCF scaling weights applied to Measurement Class F sites are currently 1 which means that the GCF wouldn't be applied to domestic HHS sites. Consequently a domestic customer who switches to elective HHS would lose out on this 'free' FiT energy. We estimate that for a standard, non-economy seven customer transitioning to HHS would result in a 1% increase in their annual cost of commodity. This amount therefore represents a sizeable opportunity cost to switching to HHS.
- 3.5. It is especially important to note that the opportunity cost associated with switching to HHS increases as the number of sites being settled half hourly increases. Currently there are a large number of domestic sites receiving a relatively small benefit from the effect of FiT spill. If the number of HHS sites increases then, by extension, the number of NHH sites will decrease. This means that the same amount of FiT spill is shared out among a smaller number of NHH sites and thus the benefit each NHH site receives increases in real terms.
- 3.6. If the FiT spill energy problem didn't exist and GCFs averaged approximately to 1, the GCF could act to help initiate switching to HHS. From a cost perspective, under profiling the sites that can be classified "peaky" (i.e. those sites that consume a greater proportion of their energy on average in peak periods) do better than they would do if they were HH settled, while "non-peaky" sites do worse.

- 3.7. Assuming that the first sites switched to HHS are “non-peaky” the GCF would then compensate for this by making the remaining profiled settled customers more-peaky. This would act to drive up the price of profiled settlement and mean that it now makes economic sense for a new batch of customers to switch to HHS.

The solution to this issue

- 3.8. OVO’s view is that the best way to remove this barrier to HHS is to settle energy from FiT sites, returning the GCF average to approximately 1 and thus creating the economic incentive to switch to HHS. We understand that Elexon proposed this solution in their response to the recent DECC consultation on a review of the FiT scheme.
- 3.9. Ideally this solution would be implemented by metering FiT export on new and installed sites and submitting the generation output into settlement. However installing the required number of smart meters would require a significant amount of time and resource. We are also aware that DECC have ruled out introducing smart meter requirements into the FiT scheme at this stage.
- 3.10. In the absence of the ability to submit metered data into settlement we would support any proposals to profile FiT export on a regional basis. Under such a solution the revenue generated from sale or cash out of FiT energy could be redistributed to suppliers through the levelisation process based on market share. However, we recognise that this solution would also take some time to implement and we think that for the reasons we identified in paragraph 3.5 this barrier to introducing cost effective HHS should be removed as soon as possible.
- 3.11. In light of the difficulties associated with solving the issue of FiT spill in a timely fashion, the SRAG have proposed that Elexon review the application of the GCF to measurement class F. We would support this proposal provided that the application of the GCF to measurement class F can be achieved with the same scaling weights

that are applied to measurement class A (NHH metered sites). We think this would suffice as an interim solution.

Issue Summary: FiT spill and the effect on GCFs	
Issue Outline	FiT spill benefits NHH sites by reducing GCFs
Effect of this issue	Customers in HHS do not receive this benefit, creating an opportunity cost for transition to HHS
Solution	Long term: Meter all FiT sites and settle FiT export Short term: Apply GCFs to HHS

TRANSMISSION USE OF SYSTEM CHARGES (TNUOS)

The issue outlined

- 3.12. TNUoS charges represent a significant proportion of the cost of supply and have historically been charged on either the “triad” basis or on the profiled volume consumed in evening peak (i.e. demand in settlement periods 33 to 38) depending on whether the site is HH or NHH settled respectively. There is scope to review the current charging arrangements in light of the proposal to move domestic customers to elective HHS.
- 3.13. Following the implementation of P272 the current arrangements imply that HH domestics will be charged on the basis of the triad rather than on consumption in the evening peak. This presents two specific issues. Firstly, the uncertainty in the case of a site switching between HHS and NHH in the space of one charging period and secondly whether the triad is the most appropriate charging methodology for the domestic market.

The effect of the issue on elective HHS

- 3.14. With regard to the first issue there were a number of implementation details that arose from P272 to deal with those cases where a site switched into HHS mid-year to

resolve any potential double charging. These have been addressed in CMP241 and CMP247, but since they are aimed at solving the issue for PCs 5-8 they are essentially a solution for the “one-way” change to HHS.

- 3.15. As discussed previously in paragraph 2.3 it is conceivable that a site may switch between HHS and NHHS multiple times. There are currently no concrete proposals to deal with these issues.
- 3.16. The second point we highlight is whether the triad is a fair and appropriate charging method for domestic customers, who may be less capable of altering their energy consumption at short notice. Under the present system of charging a HHS domestic customer would be charged on the basis of the energy they consume in three half hour periods in the year. Our concern is that this method of charging is unnecessarily penal and would either deter customers from opting for HHS or unduly punish those customers that elect to be HHS.
- 3.17. We wish to also highlight our concern that the nature of the triad mechanism raises the potential for regressive distributional impacts amongst domestic customers. Specifically it creates a mechanism by which the most engaged and well informed customers - who are likely to be more affluent² - avoid these specific high cost periods, with the disengaged and potentially vulnerable customers incurring these higher costs.

The solution to this issue

- 3.18. We support changing the TNUoS charging mechanism for elective HH settled customers to mirror that for NHH settled customers and will seek to raise a CUSC modification in the near future to this effect. We believe that cost recovery from domestic consumption in evening peak is an appropriate mechanism for TNUoS. It facilitates block time-of-use tariffs and provides a predictable incentive for customers to shift demand from the most expensive periods of the day.

² GfK (2015) Domestic retail energy survey commissioned on behalf of the CMA.

Issue Recap: Transmission use of system charges	
Issue Outline	Current Triad mechanism is unduly penal for domestic customers
Effect of this issue	Potential deterrent for customers to elect to be HHS, while also increasing the potential for adverse socio-economic effects associated with customer inactivity & vulnerability.
Solution	Raise a CUSC modification to apply existing NHH TNUoS charging to HHS for domestic customers

4. Social and Regulatory Issues

IMPACT OF HHS ON VULNERABLE AND INACTIVE CUSTOMERS

The issue outlined

- 4.1. The benefits of introducing HHS are relatively clear for domestic customers. Appropriately targeted time of use tariffs will allow domestic customers that consume energy during off peak periods (when power prices and network charges are lower) to reduce their energy bills. Domestic customers that have the ability to shift their energy consumption to off-peak periods would also realise these savings.
- 4.2. Unfortunately there are likely to be a number of domestic customers that are either incapable of shifting their demand or might be unaware of the savings of switching to HHS. OVO consider it important to distinguish between customers that cannot shift their energy consumption (inelastic customers) and those that are unaware of the benefits of shifting their consumption to off-peak periods (inactive customers).

The effect of the issue on elective HHS

- 4.3. With regard to inelastic customers the specific concern is that some may be vulnerable customers who are dependent on electricity for either medical equipment or heating. Under NHH profiling these customers are insulated to a certain extent

from the premium attached to consuming electricity during periods of high demand (most likely cold winter evenings). Switching these customers to HHS would expose inelastic customers to the true cost of consuming electricity during peak periods which would increase the cost of their energy bills.

4.4. With regard to inactive customers (who are more likely to be vulnerable as the CMA has found) we have two specific concerns. The first is that inactive customers that consume energy during off peak times, and would therefore benefit from being switched to HHS, fail to switch to HHS due to either a lack of appreciation of the benefits or because they are unaware of their ability to switch tariffs. The second concern is that, by virtue of the introduction of mandatory HHS, inactive customers are switched to HHS and are unaware of the economic consequences of continuing to consume electricity during peak periods.

4.5. A final concern we wish to raise is that the movement of a subset of customers to HHS may increase costs for customers that remain settled via profiling. The likelihood is that many of the off peak customers will be amongst the first to transition to HHS. This implies that the burden of the charges these customers will avoid - as they will be now settled on a HH basis - will fall on those customers that remain settled via NHH profiling.

The solution to this issue

4.6. We believe it is crucial to the timely implementation and success of HHS that the likelihood of any negative distributional effects on vulnerable customers is well understood and can be easily mitigated, with perhaps a well targeted social policy.

4.7. While we have concerns with regard to the impact of HHS on vulnerable customers it is also important to recognise that with suitable levels of engagement HHS will create

benefits for all customers. Industry initiatives, such as partnerships with charities and organisations such as Smart Energy GB, should be specifically targeted at vulnerable customers to ensure that they are sufficiently aware of the benefits of HHS. The goal should therefore be to ensure that vulnerable customers are amongst the first to benefit from the transition to HHS.

4.8. Given that vulnerable customers who are inelastic customers are unlikely to be capable of shifting their energy consumption, we think a decision to introduce mandatory HHS would be unwise at this time. In the long run technology innovations such as batteries will provide the means for vulnerable customers to reduce their exposure to peak period power and network charges. Our suggestion is that a social scheme, funded through general taxation should be introduced to provide vulnerable customers with inelastic demand with the means of purchasing technologies such as batteries to reduce their energy consumption during peak periods.

4.9. With regard to mitigating any adverse effects associated with the movement of domestic customers to HHS, we have consistently called on the CMA to introduce a remedy specifically targeted at vulnerable customers. In light of the CMA’s proposal to introduce a safeguard tariff, we are confident that this remedy would adequately protect vulnerable customers from being subject to the distributional effects associated with a move to HHS, such as higher peak energy prices.

Issue Recap: Impact of HHS on vulnerable and inactive customers	
Issue Outline	Vulnerable customers are less likely to be able to alter their demand and avoid peak charges
Effect of this issue	Risk that vulnerable and inactive customers will pay more for their energy than average customer
Solution	Target resources at engaging vulnerable customers Introduce a social scheme to protect inelastic customers.

	Ensure that the proposal for the CMA's safeguard tariff are sufficiently targeted at vulnerable customers.
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OTHER REGULATORY ISSUES

- 4.10. As we have stated in our introduction (paragraph 1.1), we anticipate that new tariffs and products will significantly influence the success of transitioning to HHS. It is therefore important that existing market rules do not interfere with suppliers' ability to innovate in order to create demand for HH settled tariffs or products.
- 4.11. With regard to innovative tariffs, OVO have concerns that the four tariff rule, introduced under RMR may constrict the ability of suppliers to offer new tariffs. We recognise however that the CMA is likely to offer a solution to this issue and thus it is beyond the scope of Ofgem to effect any changes in the short term.
- 4.12. In relation to products, the current mandate for suppliers to install in home displays (IHDs), creates an additional cost to introducing alternative products based on the use of IHD alternatives such as customer access devices (CADs). OVO currently leads the way with regard to innovative products by virtue of our OVO Live platform which allows customers to view their consumption in real time. The requirement to provide an IHD currently represents a significant cost to offering customer's access to OVO live. Once again we recognise that the solution to this problem is beyond the scope of Ofgem.