

Ofgem
9 Millbank
London
SW1P 3GE

Email to: futuresupply@ofgem.gov.uk.

22 December 2017

Future supply market arrangements – call for evidence

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, storage, and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including residential and business users.

The energy system is going through a significant transition as the sector decarbonises and smart technologies and new energy services develop across the sector. We are seeing a rapid growth in decentralised generation and the increasing ability of consumers to play an active role. EDF Energy wants to play a key role in this transition and is finding innovative ways to support the move to a smarter, more flexible energy system.

The retail regulatory framework fundamentally shapes the competitive response of energy suppliers and the attractiveness of the sector to new entrants. There are some significant benefits from lowering the regulatory burden and the simplification of the existing rules. It is therefore important to periodically review the regulatory framework to ensure it is producing the best outcomes for consumers and facilitating effective competition and beneficial innovation in the market. EDF Energy is willing to play a constructive role in any review by Ofgem of the current market structure.

Summary

- **It is right for Ofgem to undertake periodic reviews of the market framework in order to ensure its design continues to effectively protect the interests of consumers, including by promoting competition and facilitating beneficial innovation.**
- **Regulatory equivalence would ensure consumers continue to receive appropriate protection and that there is fair and effective competition for customers' energy needs.**
- **It is essential that the energy system continues to be balanced and settled effectively. All 'supplier' participants (of whatever type) must be responsible for balancing and for facing the costs they impose on the system.**
- **Any growth in behind the meter generation is likely to exaggerate the network, policy and system cost avoidance issues associated with such**

EDF Energy
40 Grosvenor Place, Victoria
London SW1X 7EN
Tel +44 (0) 20 7752 2187

edfenergy.com
*EDF Energy plc.
Registered in England and Wales.
Registered No. 2366852.
Registered office: 40 Grosvenor Place,
Victoria, London SW1X 7EN*

generation. This highlights the importance of reforming the network and policy cost charging arrangements.

- **Another important distortion in the current market is the small supplier exemptions in respect of environmental and social policies. We believe this is an opportunity to consider how best to ensure that all market participants support schemes in a fair way.**
- **EDF Energy is committed to engaging its customers, and helping them to choose the right products for them. We believe an opt-out collective switch scheme would introduce significant risks and is a significant intervention over individual and corporate rights.**
- **In an evolving market place, we do not consider that indirect regulation of parties (through a licensed supplier) is sustainable. Effective regulation needs to follow supply activity, irrespective of the party undertaking such activity, in order that consumers receive appropriate protection and standards of service.**

Our detailed responses are set out in the attachment to this letter. Should you wish to discuss any of the issues raised in our response or have any queries, please contact me on 020 7752 2187.

I confirm that this letter and its attachment may be published on Ofgem's website.

Yours sincerely,

A handwritten signature in blue ink that reads 'Paul Delamare'.

Paul Delamare
Head of Customers Policy and Regulation

Attachment

Future supply market arrangements – call for evidence

Supplier hub arrangements

In an evolving market, EDF Energy agrees that it is right for Ofgem to undertake periodic reviews of the market framework in order to ensure its design continues to effectively protect the interests of consumers, including by promoting competition and facilitating beneficial innovation. On that basis, a review of the supplier hub arrangements and the extent to which they continue to meet these objectives would appear sensible.

The supplier hub arrangements have been in place for over 20 years and have successfully delivered real benefits for all energy consumers. Most notably the arrangements have:

- Provided a single commercial interface for the consumer with respect to its energy needs
- Continually balanced the energy system and maintained security of supply
- Facilitated mass new entry and allowed suppliers to differentiate through new business models
- Enabled licensed suppliers to be generally sustainable, with few supplier failures
- Been flexible enough to enable the delivery of social and environmental programmes on behalf of Government; and
- Continued to aid the delivery of significant industry reforms, including the current faster switching and settlement reforms.

Given these significant benefits, any reform needs to continue to build on the consumer benefits provided by the current hub arrangements. It is important that the full impact of change is fully assessed and that reform does not put the energy system at risk for small/uncertain gains or increase costs for the majority of consumers. For instance, the impact on industry costs, the environment and the introduction of potentially more complex systems need to be properly weighed against the perceived benefits of any reform. It is therefore important that at early stage in the review process there is a shared view of the desired consumer outcomes that will arise from moving away from the current regime.

While we agree that unnecessary barriers to innovation should be removed, it is important that irrespective of how consumers engage with the market that they continue to receive effective consumer protection and a fair standard of service. There will therefore be a need for the regulatory framework to keep a pace with innovation and the entry of new energy service providers. In particular, there is a need to establish a level regulatory playing field in order to ensure consumers continue to receive appropriate protection and that fair and effective competition for customers energy needs can be maintained. This is discussed further below.

EDF Energy's response to your questions

Q1. What are your views on the above criteria? Are there other criteria that should guide our assessment of current and possible future market arrangements?

Largely, we believe the proposed criteria form an appropriate basis in which to guide any potential regulatory reform. However, we believe Ofgem should further consider the following:

- The criteria should include reference to 'regulatory equivalence' in that we believe it should be the activity that is regulated, not the type of participant. Such that all parties pay their fair share of the costs of participating in the energy market and are subject to the same regulatory obligations for the activity they undertake such that consumers remain appropriately protected.
- The use of 'reasonable price' is a subjective term and clarity will be required as to how Ofgem will assess what is 'reasonable'.

Q2. What are the most significant barriers to disruptive new business models operating in the retail market? Please draw a distinction between regulatory barriers and commercial barriers (e.g. there may not be enough potential consumer demand to justify market entry).

EDF Energy has recently been granted a 'Regulatory Sandbox' in respect of a proposed innovative trial that involves a peer-to-peer (P2P) local energy trading platform. The platform aims to allow residents in urban areas to source their energy from local renewables and trade that energy with their neighbours, increasing self-consumption of low carbon energy and reducing overall energy costs. As part of developing our proposal, we are working with Ofgem in order to fully understand any compliance risks that may arise in respect of meeting supply licence obligations.

In addition to the above, we are also participating in the newly formed Elexon Innovation Sandbox Workgroup which has been established to introduce BSC arrangements that will facilitate an electricity market sandbox allowing innovations to be tested in a live BSC settlement environment. We are supportive of both Ofgem's and Elexon's sandbox initiatives as a means of developing beneficial innovations and gaining an understanding of how such models can be appropriately treated within the regulatory framework.

Some P2P innovations may present significant technical challenges to industry systems. For instance, reference is made by Ofgem to the inability to have multiple suppliers servicing a single consumer, and knock on challenges with balancing and settlement. We are of the view that where significant industry change and cost is needed to facilitate parties delivering additional energy services, a fair solution would be for such parties to bear the costs of resolving such issues in order to avoid extra costs being faced by others.

Any growth in P2P could potential coincide with an increase in behind the meter generation and therefore is likely to exaggerate the network, policy and system cost

avoidance issues associated with such generation. This highlights the importance of reforming the charging arrangements for network charges and policy costs.

For instance, further reforms are needed to network charging. We support Ofgem's proposals for a Targeted Charging Review and are aligned with the working paper published at the beginning of November. Reform is needed to ensure that network costs are allocated fairly between all parties who use the networks. If parties rely on having access to the transmission and distribution networks, they should make a fair contribution to the costs. The current charging arrangements do not achieve these principles, have not kept pace with market and technology change and do not reflect the different ways in which people are using the network. Similarly, the fair recovery of social and environmental costs and BSUoS costs also needs consideration.

In looking to facilitate innovation, it is essential that the energy system continues to be balanced and settled effectively. It will therefore be important that all 'supplier' participants (of whatever type) must be responsible for balancing and for facing the costs they impose on the system.

Q3. What other supply market arrangements would provide a better default for disengaged consumers, whereby they are protected adequately and are able to access the benefits of competition?

EDF Energy is committed to engaging its customers, and helping them to choose the right products for them. We have demonstrated that customer engagement is achievable for suppliers who make the effort to make it happen, unlike some of our largest major competitors, we have approaching 50% of our customers on fixed price products that they have actively chosen. We continue to actively explore innovative ways to engage with all of our customers, including interacting with customers according to their circumstances, rather than treating all customers who are currently on a standard variable tariff (SVT) as the same.

EDF Energy believes that healthy and robust competition is the best way to serve customers' needs over the long term. We therefore welcome Ofgem's continuing work to promote customer engagement and make it easier to switch tariffs and suppliers. For example, we support Ofgem's recent moves to reduce the prescriptive regulations around the end of fixed term contracts and provide better flexibility in terms of the content and format of key communications provided to customers in order to improve engagement. We believe this will allow us to better target the needs of our customers and to differentiate in our customer propositions.

Notwithstanding these measures it is inevitable that a proportion of customers will either actively choose not to engage or feel that they are unable to do so. It is right therefore to keep under consideration the extent to which such disengaged customers, including vulnerable customers need additional measures.

We note that Ofgem has recently made on a number of occasions reference to the option of some form of opt-out collective switching auction arrangement. While it is currently unclear how in practice such a scheme would operate, we consider there would be significant risks in adopting such a scheme, namely:

- It would have a detrimental impact on incentives for consumers to engage; there would be a consumer perception that regulated arrangements were a better deal than actively engaging
- It could undermine the incentive for suppliers to enter or remain in the market and to offer a high quality customer service level
- It would be a significant intervention over individual and corporate rights which could deter innovation and investment; and
- Long-term benefits would be uncertain given the lack of precedence for such a scheme.

We also note that such a scheme would appear to be directly focussed on price and not take account of other factors such a customer service performance. This may, for instance, result in an outcome for vulnerable customers that does not best meet their needs and expectations.

Alternatively, amending the current default arrangements and the obligation to supply may also have significant impacts on competition, innovation and market entry. While the current obligations result in suppliers incurring significant costs, we believe the principle of regulatory equivalence should be maintained. Consequently, we would not support limiting the obligation to provide such arrangements to only a subset of the supplier community.

Q4. How big an issue is it that we do not currently regulate intermediaries in the energy market? Is there a case for doing so? If so, how would we best do it? We are especially interested in frameworks that enable a wider variety and increased number of market participants to provide supply.

In terms of promoting innovation and reducing any perceived barriers to entry, simplification of the regulatory framework, while ensuring consumers remain appropriately protected, is a positive step. However, in terms of adopting any alternative regulatory model, there is a need to justify why a reliance on general consumer protection law is inadequate.

Energy suppliers face significant obligations by virtue of their licensed status. In an evolving energy market where an increasing number of new parties are looking to enter the market and offer a variety of services to consumers, there is a risk that such parties will not be subject to similar obligations, or even appropriate consumer protection regulation specific to the activities they undertake. This to a certain extent is already happening with third party intermediaries, such as price comparison websites and those operating in the

business sector, undertaking customer facing marketing activities but who are not subject to direct regulation, instead at times regulated indirectly by being treated as a 'representative' of a licensed supplier.

In an evolving market place, we do not consider that indirect regulation of parties is sustainable. We believe it is essential that consumers continue to be afforded effective protections irrespective of the party who engages with them for their energy needs and that fair and effective competition remains. We see regulatory equivalence as an important part of a fair market; effective regulation needs to follow supply activity in order that consumers receive appropriate standards of service. Consequently, we would support due consideration of the options available, with a view to ensuring that the scope of regulation appropriately captures all parties who are actively engaging with consumers regarding their energy needs. This should, for instance, include the extent to which a general authorisation regime, as opposed to the existing supply licence model, would be more effective in protecting consumers.

In terms of existing reform, we are supportive of Ofgem's move to a greater reliance on principles based regulation as opposed to extensive prescriptive regulations. We believe a regulatory model that has a focus on consumer outcomes is the right approach. There are clear advantages in such a model where the regulator is able to step back from prescribing specific actions suppliers must take to one where it appropriately sets out the consumer outcomes it expects suppliers to achieve. Such a model promotes innovation and provides suppliers with the ability to determine the operational practices and actions within their business to achieve a consumer outcome, in the most efficient and effective manner.

Furthermore, we believe there is merit in assessing the potential options for addressing the complex and resource intensive industry codes, as a means of increasing the accessibility of the market for both existing and new players. This could include consideration of the extent to which consolidation of codes (including across electricity and gas) could be achieved. We are aware that Ofgem is currently proposing, as part of its faster switching reform, the adoption of a Retail Energy Code which, depending on its scope, has the potential to address some concerns in this area.

Notwithstanding the above, we believe that where regulatory burdens are lowered in order to promote innovation and new entry, there is an increased risk that without changes to market entry requirements, that certain business models may fail. We would like to see Ofgem take a more proactive role in assessing market entrants and monitoring the financial health of suppliers, in a similar way to the monitoring that takes place in the banking sector. This is all the more important given the cost of insolvencies are likely to be socialised across other suppliers under the Supplier of Last Resort (SoLR) provisions, and therefore ultimately borne by energy customers.

EDF Energy
December 2017