E.ON UK
Newstead Court
Little Oak Drive
Annesley
Nottinghamshire
NG15 0DR
eonenergy.com

Email: tracey.wilmot@eon-uk.com
Mobile: 07771 974812

26 October 2018

Anna Rossington
Deputy Director
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

By email only: retailpriceregulation@ofgem.gov.uk

Dear Anna,

Renewable Obligation: Number of ROCs Presented Towards 2017/18 UK Obligation

I wanted to raise with you our concerns around this year's shortfall in ROCs presented and the possibility that the failure by many suppliers to meet their obligations could result in a significant additional financial liability on compliant suppliers that has not been adequately reflected in the calculation for setting the level of the default tariff cap. In addition, should any, or several, of these currently defaulting suppliers fail, yet more unanticipated and uncontrolled costs will be imposed on remaining suppliers through the Supplier of Last Resort (SoLR) process.

On 22 October 2018 Ofgem published its report on the number of Renewable Obligation Certificates (ROCs) that had been presented by licensed electricity suppliers to meet their obligations. Where a supplier does not present enough ROCs to meet its obligation, it has the option of making a buy-out payment to compensate. We are concerned to note that your report indicates that this year there is a very large shortfall in the buy-out funds of almost £103m as a result of 34 suppliers failing to meet their total obligations.

Although suppliers have an opportunity to make late payments by 31 October 2018 (subject to an additional interest payment), both the number of suppliers failing to meet their obligations, and the size of the financial shortfall show a significant increase over the previous year (16 suppliers and a value of c£18.7m). I understand that should any significant amount remain outstanding after this time, then a mutualisation process would result in all compliant suppliers making up the shortfall based on their market share. Such cost must be taken fully into account by the price cap.

The significant increase in the number of suppliers failing to meet their obligations by 1 September 2018 would appear to be a symptom of the current market conditions – and/or of the financing strategies adopted by some market players. To date in 2018, there have been five suppliers[1] that have failed resulting in an SoLR being appointed by Ofgem; our expectation is that further failures may result in the near future, not least because of the need to make payments into the buy-out fund or, indeed, as a result of the default tariff cap.

Therefore, as well as being an indicator that additional SoLR directions (which themselves result in additional cost to the wider supplier community) may need to be issued by Ofgem, there is a further risk of compliant suppliers being required to pick up the significant socialised cost of the ROC buy-out fund shortfall. We do not believe this has been sufficiently factored into the calculations for setting the level of the default price cap; either through the risk element of the headroom, which we already believe is wholly insufficient, or any other mechanism (such as a correction factor) to retrospectively recover a cost such as this which is completely out of the control of a compliant supplier.

Not taking this into consideration would be an unacceptable outcome for E.ON; especially when set against an environment post implementation of the default tariff cap where even Ofgem's own draft impact assessment (IA) of the recent statutory consultation recognised *"the overall market EBIT margin will reduce to approximately -1%, representing a reduction of approximately 4 percentage points relative to the counterfactual EBIT margin"* (paragraph 4.58 of the IA). Failure adequately to reflect the impact of any socialised costs of a buy-out fund shortfall will lead to an increased detrimental effect not only on suppliers who may not be able to recover these unaccounted-for costs through tariff pricing, but also the wider market and ultimately on customers through reduced competition.

I would expect Ofgem to ensure that any such costs incurred by suppliers are fully reflected in Ofgem's calculations when setting the level of the default tariff cap. I would be happy to discuss the content of this letter with you.

Yours sincerely

TWilmot

Tracey Wilmot
Head of Retail Market Regulation

[1] Future Energy, National Gas & Power, Iresa, GEN4U and Usio.