

Guidance

Derogation requests for renewable tariffs from the default tariff cap

Publication date: 6 November 2018

Contact: Marko Jovanovic, Head of enforcement casework

Team: Conduct and Enforcement

Tel: 020 7901 7000

Email: renewablederogations@ofgem.gov.uk

This document sets out our guidance on the process for requesting a derogation from the default tariff cap for renewable tariffs.

We have published a derogation questionnaire and renewable financial information templates that suppliers will need to complete to apply for a derogation. This guidance document explains:

- how to apply for a derogation
- the evidence we expect suppliers to provide when requesting a derogation
- how we will assess applications for a derogation.

The guidance will be kept under review and may from time to time be updated.

© Crown copyright 2018

The text of this document may be reproduced (excluding logos) under and in accordance with the terms of the [Open Government Licence](#).

Without prejudice to the generality of the terms of the Open Government Licence the material that is reproduced must be acknowledged as Crown copyright and the document title of this document must be specified in that acknowledgement.

Any enquiries related to the text of this publication should be sent to Ofgem at: 10 South Colonnade, Canary Wharf, London, E14 4PU. Alternatively, please call Ofgem on 0207 901 7000.

This publication is available at www.ofgem.gov.uk. Any enquiries regarding the use and re-use of this information resource should be sent to: psi@nationalarchives.gsi.gov.uk

Contents

Contents	3
Summary	4
1. Introduction	5
Background	5
Derogations	6
Duration of derogations.....	7
2. Guidance on derogations	8
When would a derogation be considered?	8
Submitting a request and timelines	8
Our assessment of any requests	9
Demonstrating each of the outcomes.....	10
Next steps	13
Annex 1 – Two stage process and prioritisation criteria	14
Optional stage one: expedited review of derogation requests, feeding into provisional decision and final decision to provide a time-limited derogation	14
Stage two: in-depth review of derogation requests with decision on an enduring derogation	15
Prioritisation of derogation requests	15

Summary

This document constitutes our guidance on the approach we will take for assessing derogations for renewable tariffs from the default tariff cap. We have consulted on the approach we intend to take with regard to derogations¹ but we will keep this guidance under review and may from time to time update it.

We have published our decision for setting and updating a default tariff cap in accordance with the Domestic Gas and Electricity (Tariff Cap) Act 2018. The Act required us to consult on whether a renewable tariff exemption was appropriate, and if so, how to exempt the respective tariffs.

We published our decision on 6 November 2018. We decided that the default tariff cap should apply to all SVTs, but we will provide a route for suppliers to apply for derogations for renewable tariffs where certain outcomes are met.

Suppliers can apply for a derogation where they believe they have an eligible SVT. We have published templates that suppliers will need to complete to apply for a derogation.

¹ Ofgem (2018), Default tariff cap – statutory consultation: Appendix 10 – Exemptions
https://www.ofgem.gov.uk/system/files/docs/2018/09/appendix_10_-_exemptions_0.pdf

1. Introduction

- 1.1. This document sets out our guidance on the process for requesting a derogation from the default tariff cap for renewable tariffs.
- 1.2. We have published a questionnaire and renewable financial information templates that suppliers will need to complete to apply for a derogation. This guidance document explains:
 - how to apply for a derogation
 - the evidence we expect suppliers to provide when requesting a derogation
 - how we will assess applications for a derogations.
- 1.3. Appendix 10 of our decision document on the default tariff cap sets out the policy behind allowing a route for renewable SVTs to seek a derogation from the default tariff cap.²

Background

- 1.4. The Domestic Gas and Electricity (Tariff Cap) Act (2018) (the Act) places a duty on Ofgem to introduce a default tariff cap for domestic consumers on Standard Variable Tariffs (SVTs) and default tariffs.
- 1.5. The Act provides some discretion for Ofgem to exempt certain groups from the default tariff cap.³ This includes:
 - SVTs that have been chosen by the consumer and that appear to the Authority to support the production of renewable gas or electricity, and
 - vulnerable consumers that may also be benefitting from a safeguard tariff.
- 1.6. We decided that the tariff cap should apply to all SVTs, but we provided a route for suppliers to apply for derogations for renewable electricity and renewable gas SVTs that have been chosen by the suppliers' customers.
- 1.7. In our decision we set out the following:

² Ofgem (2018), Default tariff cap – decision: Appendix 10 – Exemptions www.ofgem.gov.uk/publications-and-updates/default-tariff-cap-decision-overview

³ Section 3(2) notes that tariff cap conditions may provide for the conditions not to apply in relation to (a) domestic customers who benefit from a cap imposed by the Authority on rates or amounts charged for, or in relation to, the supply of gas or electricity to customers who appear to the Authority to be vulnerable by reason of their financial or other circumstances; (b) standard variable rates which apply only if chosen by domestic customers if, or to the extent that, the rates in question appear to the Authority to support the production of gas, or the generation of electricity, from renewable sources.

- by default the tariff cap will apply to all SVTs, but suppliers will be able to apply for derogations for renewable electricity and renewable gas SVTs that suppliers' customers have chosen to be on
- all suppliers will be required to have a default tariff that is compliant with the cap, irrespective of whether they have received a derogation for a tariff that a consumer has chosen
- we may grant a derogation if a supplier demonstrates its renewable SVT delivers three outcomes: materially higher costs due to supporting renewables, support for renewables beyond existing subsidies, and only applies to customers who have chosen the SVT
- as a transitional measure only, we will run a two-stage derogation process; fast-tracking priority derogation requests to provide a decision on a time-limited derogation, followed by an in-depth review of derogation requests to provide a decision on a more enduring derogation
- there will be an ongoing enduring process, as we have not set a deadline for receiving derogation requests, so suppliers would be able to apply for a derogation at any point during the lifetime of the default tariff cap
- it is likely that if we do not receive a full and complete application within one week from inviting derogation requests that we will not be able to make a provisional decision that can take effect in time for the start of the default tariff cap
- where necessary, we will prioritise derogation requests against criteria that aim to minimise any potential consumer detriment, such as prioritising tariffs with a large number of customers.

Derogations

What is meant by a derogation?

- 1.8. A derogation is a direction from the Gas and Electricity Markets Authority relieving a licensee from its obligation to comply with a licence condition in specific circumstances and to a specified extent.
- 1.9. When a derogation is granted, we consider whether to place conditions and/or alternative requirements on the supplier to comply with. A derogation would normally have an expiry date so that the need for it can be systematically reviewed. The derogation will also normally have provisions for circumstances in which it could be revoked. For example, if the supplier submitted inaccurate information or if the supplier (and where applicable, its representative) does not comply with any requirements or conditions of the derogation.
- 1.10. If granted, a derogation will not normally apply to a period before the date the direction is issued.

Duration of derogations

1.11. Where Ofgem grants a derogation it may do so on the basis of different durations:

- Definite – continues for a period of time specified in the direction
- Lifetime – continues for the lifetime of the scheme, tariff or other relevant initiative in relation to which the licensee seeks a derogation
- Indefinite – continues until a further derogation is made or the derogation is revoked.

1.12. As a matter of policy, the longer the duration of any derogation, the more likely it is that Ofgem would consider it to be appropriate to include alternative obligations as a condition for granting a derogation and that the decision to grant the derogation would be subject to periodic reviews.

2. Guidance on derogations

This chapter sets out when a derogation will be considered, the process of submitting a request and timelines. It also sets out how we will approach the assessment.

When would a derogation be considered?

- 2.1. A derogation may be granted if a supplier demonstrates that its renewable tariff delivers on the following high-level outcomes:
- **Outcome 1:** the tariff is an SVT that consumers have chosen to be on.
 - **Outcome 2:** by consumers being on the tariff, support is given to renewables to an extent that is materially greater than that which is brought about as result of subsidies, obligations or other mandatory mechanisms.
 - **Outcome 3:** the cost to the licensee of supplying electricity/gas by virtue of the tariff is materially greater than the level of the default tariff cap for reasons that are directly attributable to the support that the tariff provides to renewables.

Submitting a request and timelines

How to apply

- 2.2. Suppliers applying for a derogation need to complete the questionnaire and templates⁴ that have been published alongside this guidance document. This guidance document should be read alongside the questionnaire and templates.
- 2.3. The renewable financial information template contains specific guidance on what information should be provided on a question-by-question basis. Suppliers should ensure they provide as detailed a cost breakdown as possible and complement this with evidence. The renewable financial information template contains a range of cost categories and indicates where explanations and evidence are required. The list of costs is non-exhaustive and there is space for suppliers to add additional costs. Where costs are specified in the template, suppliers will still need to provide evidence and justifications that these costs are valid in their particular case.
- 2.4. Once the templates are complete, they should be sent to Ofgem at renewablederogations@ofgem.gov.uk. Please do not PDF the templates when you submit them.
- 2.5. We will confirm receipt of your application.

⁴ Ofgem (2018), Guidance: Derogation requests for renewable tariffs from the default tariff cap: <https://www.ofgem.gov.uk/publications-and-updates/guidance-derogation-requests-renewable-tariffs-default-tariff-cap>

Timelines

- 2.6. As a transitional measure we will run a two-stage derogation process; fast-tracking priority derogation requests to provide a decision on a time-limited derogation, followed by a more in-depth review of derogation requests to provide a decision on a more enduring derogation.
- 2.7. If we receive many requests within a week of inviting them, we may run a prioritisation process. The two stage process and prioritisation criteria are set out in Annex 1 to this document.
- 2.8. If you submit your request by 13 November 2018 we will aim to provide a minded to decision by 1 December 2018, but otherwise we will aim to provide a decision as soon as possible.
- 2.9. Ahead of providing a decision or a minded-to decision, we may consult on our proposed decision.
- 2.10. If you have any questions, send these to renewablederogations@ofgem.gov.uk.

Our assessment of any requests

- 2.11. Each request will be considered on a case-by-case basis. Our assessment will be based on checking that appropriate evidence has been provided by the supplier to demonstrate that the tariff meets the three outcomes to be eligible for a derogation.
- 2.12. It is important that the default tariff cap continues to protect SVT customers, particularly those in vulnerable situations. Our assessment of derogation requests is intended to ensure that only genuine cases receive a derogation. We are mindful of gaming risks that would undermine the protections of the cap. We will carefully assess whether the tariff in question meets the requirements before granting derogations because of the risk to undermining these protections.
- 2.13. We may follow up with the licensee making the request initially to clarify points relating to the derogation request and for the licensee to satisfy itself that there is a need for a derogation. We may ask an applicant for additional information that we need to assess a derogation request.
- 2.14. If, during the assessment, we identify any potential risks that may arise from the granting a derogation, for example any possible negative impact on consumers (including protections for disengaged customers and all customers' ability to make an informed choice about paying more for their energy to support renewable generation), we would raise the issues with the supplier and seek evidence on how they will mitigate the risks before considering whether a derogation can be granted.
- 2.15. For consistency, we take into account the nature of derogations we have already granted, the circumstances under which they were granted, and the conditions attached to them. Besides evidence submitted by the applicant, we may also consider evidence gathered through our monitoring activities and from other sources including from third parties, when necessary.

- 2.16. Ofgem will maintain a record of derogations that have been granted and may in some cases decide to incorporate additional derogation monitoring activity (for example review periods).

Demonstrating each of the outcomes

- 2.17. We will consider the case for granting a derogation based on whether all of the outcomes have been met.

Outcome 1: the tariff is an SVT

- 2.18. The Act defines an SVT as “a rate or amount charged for, or in relation to, the supply of gas or electricity under the contract that is not fixed for a period specified in the contract.”

- 2.19. The supplier should demonstrate that the tariff meets this definition. This could be through providing the relevant definitions from the contract they enter with their customers.

Outcome 1 cont.: the consumer chose to be on the SVT

- 2.20. To receive a derogation, the supplier will need to demonstrate that consumers made an active choice to be on the SVT. We do not propose to be prescriptive in setting out how suppliers must demonstrate this. However, we can clarify the following:

- We consider that a consumer has not made an active choice if they have defaulted onto the SVT from a fixed-rate tariff or are on a deemed contract.⁵
- We expect a supplier to demonstrate that at the point the consumer chose to join the SVT, it was clearly advertised as a tariff that supports renewables.

- 2.21. The onus will be on suppliers to demonstrate that consumers made an active choice to join the SVT. One way in which suppliers could demonstrate this could be through requiring consumers to specifically opt-in to the tariff that is derogated, with those consumers that do not opt-in being consequently moved to a default tariff that complies with the cap.

- 2.22. We will consider the impact of the proposed derogation on the protections for disengaged customers provided for by the default tariff cap, and how the supplier will ensure that only customers who have made an active choice to pay more for their energy from renewable sources are covered by the scope of any derogation.

Outcome 2: the SVT supports renewables

- 2.23. We will assess each application based on the evidence submitted to demonstrate that the tariff supports renewables to a materially greater extent than that required under

⁵ Typically a deemed contract will occur where a consumer moves into a new property and has not agreed contractual terms with a supplier who is supplying energy to that property or where a fixed term contract expires and there are no explicit provisions for terms and conditions for the period immediately after expiry.

existing government schemes, licence obligations, or other mandatory mechanisms, with the objective of increasing renewable generation or production capacity.

- 2.24. Whether a tariff and associated activity supports renewables beyond existing schemes and obligations may depend on the specific circumstances. It is for each supplier to set out how a tariff meets outcome 2 and provide appropriate evidence.
- 2.25. This list is not exhaustive, but below we set out factors and information we will take into consideration in our assessment.
- The Act specifically refers to tariffs which support the production of gas, or the generation of electricity, from renewable sources. We will not consider other activities such as electricity storage or carbon offset activities that do not directly support renewables.
 - We will not consider activities and costs associated with subsidies, obligations or other mandatory mechanisms, for example, costs for purchasing Renewable Energy Guarantees of Origin (REGOs; the costs of which we note are immaterial); participating in the Feed-in Tariff (FIT) scheme (even where voluntary); funding the Contracts for Difference (CfD) scheme; or purchasing Renewable Obligation Certificates (ROCs) – even where purchasing more than obligated to (noting that now the Renewables Obligation is closed to new generators, over-purchasing ROCs wouldn't encourage new generators to enter the market).
 - For any activities or costs associated with purchasing renewable gas certificates we will consider whether the generation has received support from existing subsidies, eg the Renewable Heat Incentive. Where generation has received support from a subsidy we do not expect to consider the purchasing of renewable gas certificates as additional support.
 - We will consider whether the support for renewables arises due to the SVT; if a supplier would carry out an activity regardless, then we would not consider it as support for the purposes of the derogation request. For example, this includes PR and general communication activities.
 - We will consider whether we think suppliers are attempting to game the derogations framework, such as by assessing whether suppliers are potentially allocating activities or costs from their wider portfolio to the renewable SVT. For example, if activities across a supplier remain the same but there has been a recent reorganisation of renewable generation to certain tariffs.
 - We will consider the extent to which there is long-term commitment to the renewables sector and activities that are supporting renewables.
 - We will consider the types of renewable generators the activities support and details of the support. For example, suppliers should provide a description of the generators (eg small generators below 1MW) and length of PPA support.

Outcome 3: the supplier incurs materially higher costs

- 2.26. When assessing whether costs are materially higher we will take into account the evidence the supplier provides regarding the renewable specific costs related to the tariff and also the overall cost of the tariff.

- 2.27. Suppliers should explain and provide evidence relating to the costs they face solely from the support they provide to renewables, and which they would not otherwise face. Activities that do not support renewables (in accordance with the guidance above regarding outcome 2, such as purchasing REGOs), will not contribute towards costs associated with supporting renewables.
- 2.28. Suppliers should demonstrate there is a relationship between the overall cost of the tariff, the renewable specific cost and the need to price materially above the default tariff cap. Our assessment of materiality and the reasoning for why a supplier is requesting to price above the cap, will be on a case-by-case basis, with the onus being on the supplier to clearly separate and justify why costs are renewable specific additional costs. We expect a supplier to separately demonstrate that there is a relationship between these materially higher renewable costs and the need to price the tariff above the cap.
- 2.29. We may, on a case-by-case basis, require suppliers to provide information on the efficiency of their spending on supporting renewable generation. Regardless of any assessment we may carry out on the efficiency of costs, where a supplier asserts that they are incurring materially higher costs, they will have to clearly evidence where these costs are incurred and that they are materially higher cost when compared to non-renewable equivalents. We expect the supplier to verify that renewable costs are valid and evidenced, including that they:
- are related to activities that are in scope in terms of supporting renewables (for example, costs for purchasing Renewable Obligation Certificates (ROCs) would not be valid, as we do not consider that purchasing ROCs provides additional support for renewables in the context of our definition of outcome 2)⁶
 - haven't been incurred in an attempt to game the derogations framework (for example, by unnecessarily spending on renewables in the run up to requesting a derogation in an attempt to reach a level of costs that is considered material).
- 2.30. The following list is not exhaustive but sets out other factors and information we may take into consideration in our assessment:
- Costs must be reported in the templates to a sufficiently detailed level. Costs must be directly linked to an activity associated with supporting renewables and clear assumptions and supporting evidence provided. For example, just providing a proportion of a group of shared costs will not be sufficient. Also, explaining these are higher in general because of the renewable component of the tariffs would not be sufficient justification or evidence. The renewable financial information template provides further guidance on how costs should be broken down.
 - Given our case-by-case approach to efficiency we recognise there is a buyer beware risk and expect suppliers to not overstate Ofgem's assessment of the tariff in customer communications. However, we reserve the right to consider efficiency, particularly where we consider costs have been inefficiently incurred in an attempt to demonstrate material costs thereby gaming the derogations framework.

⁶ Outcome 2: by consumers being on the tariff, support is given to renewables to an extent that is materially greater than that which is brought about as result of subsidies, obligations or other mandatory mechanisms.

Confidentiality and disclosure

- 2.31. Any information provided to Ofgem relating to the affairs of an individual or a particular business will be subject to statutory restrictions on disclosure under section 105 of the Utilities Act 2000. However, you should note that there are exceptions to the statutory restrictions, including where the disclosure is necessary to facilitate the statutory functions of Ofgem (eg the publishing of information to promote the interests of consumers) or other public bodies.
- 2.32. You should note that Ofgem cannot provide any assurances in relation to the treatment of information which may be the subject of a request made under the Freedom of Information Act 2000 ('FOIA') or the Environmental Information Regulations 2004 ('EIR'). However, Ofgem will always consider whether the statutory restrictions on disclosure apply to the requested information and therefore whether one or more of the FOIA/EIR exemptions apply.
- 2.33. Before deciding whether to publish any information relating to the affairs of a particular licence holder, Ofgem is required to consider whether it is appropriate to redact any information on the basis that the information would or might, in our opinion, seriously and prejudicially harm the interests of that person ('confidential information'). Where appropriate, we may seek further representations from licence holders at a later stage in respect of any specific information Ofgem is proposing to publish.

Next steps

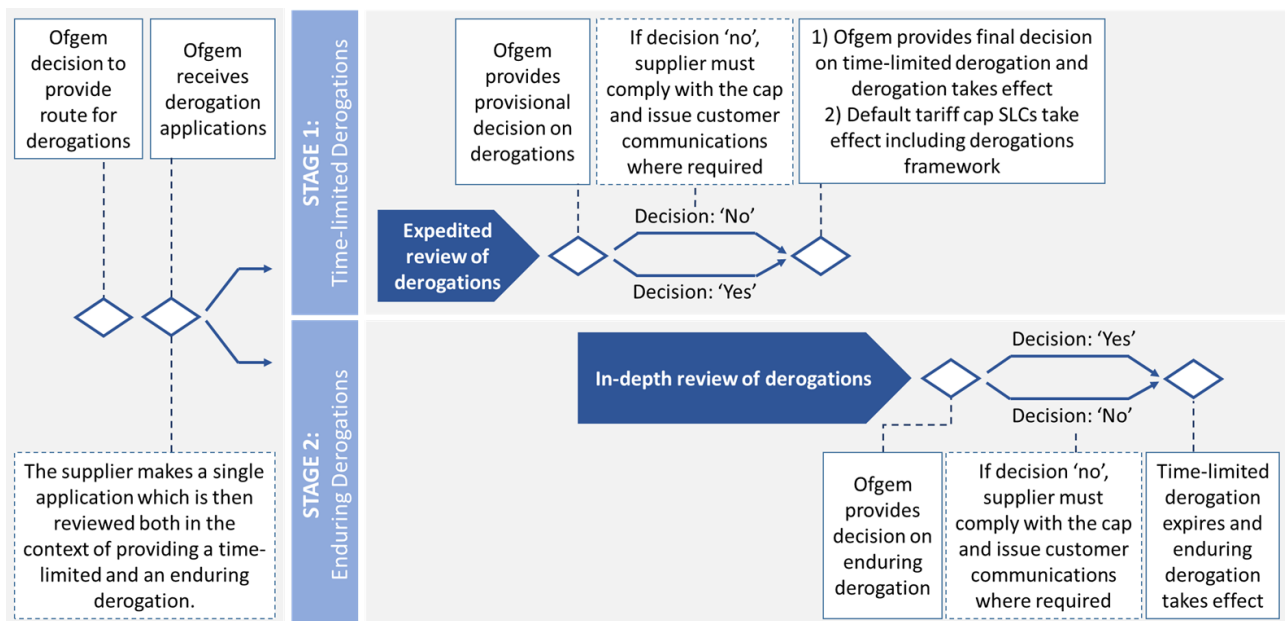
- 2.34. We acknowledge that as the market develops and adapts to the default price cap, our approach to derogations may need to be amended. Consequently, we will keep this guidance under review and may update it from time to time, consulting on any updates as appropriate. In particular, we will reflect on our experience with the first derogation requests to determine whether any immediate changes are necessary.

Annex 1 – Two stage process and prioritisation criteria

We invite derogation requests with immediate effect. We intend to carry out up to two stages of assessment, and after each we may provide a derogation. The two stage process will be transitional only.

There will be an ongoing enduring process, as we have not set a deadline for receiving derogation requests, so suppliers would be able to apply for a derogation at any point during the lifetime of the default tariff cap.

The two-stage process



Optional stage one: expedited review of derogation requests, feeding into provisional decision and final decision to provide a time-limited derogation

If suppliers submit a derogation request within a week of this decision document being published, we will aim to carry out an expedited review of those requests. The aim of stage one is to fast-track requests, prioritising if we need to (for instance, those tariffs affecting a large number of customers) for a time-limited derogation decision until we can provide a decision on whether to grant an enduring derogation. The expedited review of derogation requests will be a less in-depth assessment than we would ordinarily carry out. As such, if we issue a derogation based on an expedited review, we expect it to be a time-limited derogation, and it will expire after a number of months. Because of the risks of gaming, we will carefully assess whether the tariff in question meets the requirements before granting a derogation, whether temporary or enduring.

The sooner we receive derogation requests, the more likely we will be able to provide a provisional decision on a temporary derogation far enough in advance to avoid the supplier having to temporarily comply with the default tariff cap. It is likely that if we do not receive a full and complete application within one week from inviting derogation requests that we will not be able to make a provisional decision that can take effect in time for the start of the default tariff cap. If we receive many requests, we may have to prioritise our assessment of requests to minimise the risk of consumer detriment.

We will aim to carry out an expedited review and provide provisional decisions on whether we will provide a derogation as soon as possible, and ideally no later than 30 days ahead of the default tariff cap taking effect. We will aim to issue a final decision on the time-limited derogation (based on our expedited review that fed into our provisional decision) once the licence conditions take effect, which will align with when the decision on the default tariff cap takes effect. We reserve our right to issue a different derogation decision to our provisional decision.

Stage two: in-depth review of derogation requests with decision on an enduring derogation

Once we have completed our expedited review, we will carry out a more in-depth review of derogation requests. We will aim to conclude that review ahead of any time-limited derogations expiring. If we consider that the derogation request meets the criteria, we would issue an enduring derogation to take effect upon expiry of the time-limited derogation. If we are not satisfied, then the time-limited derogation will expire and the supplier will be required to comply with the default tariff cap.

We have not set a deadline for receiving derogation requests, so suppliers would be able to apply for a derogation at any point during the lifetime of the default tariff cap.

If a supplier receives a time-limited derogation (under stage one) but does not receive an enduring derogation (under stage two), they will not have to rebate their customers.

After the transitional arrangements relating to the introduction of the default tariff cap (ie the short period during which we will carry out the optional stage one expedited review), we will retain only the in-depth (stage two) review as the sole approach to processing derogations.

Prioritisation of derogation requests

For the purposes of our expedited review of derogation requests, we may prioritise our assessment of derogation requests. Our prioritisation would be based on:

- how many customers are on the renewable SVT (prioritising tariffs with more customers)
- how many customers are on the renewable SVT, as a percentage of the relevant suppliers' entire customer base (prioritising suppliers with a higher percentage)
- whether we consider the derogation request may represent an attempt to game the default tariff cap for a tariff that isn't genuinely supporting renewables (deprioritising these suppliers)
- the quality of the submission (those that do not provide at the earliest opportunity a sufficient level of detail for us to make a decision will necessarily take longer to process).

The sooner we receive derogation requests, the more likely we will be able to provide a provisional decision far enough in advance to potentially avoid the supplier having to comply with the default tariff cap.