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By email: FWP@ofgem.gov.uk

Dear Sirs,

Ofgem draft Forward Work Programme 2019-21: Centrica Response

Executive summary

We welcome the opportunity to comment on Ofgem's draft Forward Work Programme (FWP). In light of the uncertainties, pace of change and current complexities facing the energy sector, a clear vision for the period 2019-21 is essential if the outcomes Ofgem is seeking are to be achieved.

Areas that warrant particular focus over this period are Midata and the ongoing review of the price cap. In the context of Midata, we would highlight that the protection of our customers' data remains a priority for us. In this specific context, and more broadly, we believe it is critical that relevant data protection standards are met and continue to be maintained.

We anticipate the price cap continuing to be an important and strategic focus for Ofgem over this period. Determining the conditions for effective competition that will enable Ofgem to recommend lifting the price cap will be a critical focus. In addition, transparent monitoring of the impact of the cap on competition and consumers will also be important, as will expected and necessary reviews of aspects of the cap methodology.

We agree that innovation in the energy market will remain an important focus for Ofgem and the industry more broadly. It is important to recognise that existing energy suppliers can be equally as innovative and disruptive as newer participants. We believe that a regulatory framework that can create a level playing field between all market actors will give Centrica the opportunity to deliver new market models that will deliver material benefits to our customers.

More broadly, we see the FWP as being an opportunity for Ofgem to outline how it intends to develop and evolve its approach to regulation at what is a crucial time for the sector. Increasingly, concepts such as fairness are emerging as considerations in policy interventions, despite often being difficult concepts to assess objectively. In order to avoid unintended outcomes (including detrimental impacts on competition), it will be critical that clarity is provided about how concepts such as fairness will be assessed in regulatory decision making.

Our observations on the FWP are grouped below according to the 4 key priorities.

Making retail markets work for all

We welcome and support Ofgem's review of supplier licensing arrangements. We have responded separately on this consultation with our views and recommendations. To encourage a more focussed and targeted approach to the review, we believe consideration should be given towards an objective or target that Ofgem should seek to achieve such as the zero mutualisation of the debts of failed suppliers.

Similarly, we support, and will fully participate in Ofgem's planned strategic review of the microbusiness retail market. It is encouraging that Ofgem is approaching this review with an open mind, and without specifying any preconceived outcomes or remedies. Should the review subsequently identify any areas of concern, it will be important that any proposed policy interventions are based on clear and quantified evidence.

We support Ofgem's midata project but are growing increasingly concerned about the ambitious timescales for the implementation. While successful implementation of this project will help to promote consumer engagement and promote innovation and competition in the market, sufficient time must be allowed to ensure the sharing of data meets relevant data protection requirements (including allocating rights and responsibilities to appropriate parties, in accordance with the General Data Protection Regulations (GDPR)).

With that in mind, suppliers should not be expected to begin building and testing a solution to meet the delivery deadline, until the solution design is finalised. In addition to this, we expect robust governance arrangements to be procured and in place before the Supply Licence Condition comes into effect. Given the limited progress on key decisions to date, Ofgem should assess the project timescales critically to avoid delivering a sub-optimal solution that could potentially cause detriment to consumers rather than benefit. We look forward to participating in the policy consultation and impact assessment that Ofgem has committed to publish in the Spring of this year.

We recognise that analysis of customer data, particularly following trials, is increasingly informing policy decision making. While this is a positive development, in that it enables better quality, quantified impact assessments to underpin proposed policy initiatives, it is essential that any requests for data fully respect relevant data protection regulations. The protection of our customers' data is a critical priority for us, and as such we will only share our customers' data if the use of that data is clearly communicated upon request. Furthermore – and in line with relevant regulations - we expect Ofgem to undertake and publish Data Protection Impact Assessments (DPIAs) for each trial / exercise that requires personal data to be shared, as well as providing the lawful basis for each request. More broadly, we encourage cooperation and collaboration when concerning matters of data protection, including with the Information Commissioner where appropriate.

Given UK's imminent exit from the EU, we support Ofgem's planned work to oversee the process by which both licences and codes are modified, in order to ensure they operate efficiently. Due to the imminent deadline, practical action should involve Ofgem seeking to issue a regular update, e.g. an open letter or similar, keeping the industry abreast of progress and the necessary code and licence developments.

We note there is limited focus on the price cap beyond the issue of compliance monitoring. We therefore wish to highlight the importance of related policy work in the following areas:

- Collaboration with the CMA's review of the prepayment (PPM) cap with a view to ensuring timely transition to a properly cost-reflective cap consistent with Ofgem's own bottom-up

cost modelling. Amongst other things, a revised cap should include appropriate allowance for smart costs and overcome current ambiguity and confusion caused by coexistence of two inconsistent caps for SMETS1 and SMETS2 PPM.

- A timely, transparent and thorough review of the smart meter allowance within the default price cap. This necessitates, amongst other things, publication of the Smart Metering Net Costs Change (SMNCC) model, coordination with BEIS on data gathering and BEIS own review to update overall impact assessment, and a transparent process that supports effective and timely stakeholder engagement.
- Detailed and transparent monitoring regarding the impact of the cap on consumers and on competition more broadly. This is necessary to inform stakeholders and highlight (and enable the early addressing of) any unintended consequences.
- Lastly, we support Ofgem's planned work to define the conditions for effective competition that need to be in place for a recommendation to be made to the Secretary of State for the default tariff cap to be removed.

Finally, we welcome the review of the Consumer Vulnerability Strategy, and believe some areas merit special attention. A key example is a complete review of a 'Fit for purpose' status of Fuel Direct. Currently there is a disconnect in the policy approach between Ofgem and DWP. Where DWP considers the use of Fuel Direct as a means only when all payment methods have been exhausted, including threat of disconnection, Ofgem takes the view that Fuel Direct should not be a method of last resort. We strongly encourage Ofgem to work closely with the DWP whilst drafting its strategy. In a revenue constrained world brought about by the price cap, Ofgem must also be mindful to avoid introducing further obligations on suppliers that require additional costs.

We continue to believe that a clearer and more workable definition of vulnerability is considered as a part of Ofgem's review. This is particularly necessary given outcomes that are "fair" and which address consumer vulnerability are increasingly seen as being policy objectives. The concepts of "fairness" and "vulnerability" are often used in a similar context, and often in a vague way. Objective and precise definitions of these concepts are therefore necessary if economic analysis is to continue to ensure that regulatory interventions are in the interests of all consumers, and avoid unintended distortions to competition.

Enabling Future Markets and System arrangements

We welcome Ofgem considering the Future Supply Market Arrangements. At the core of the review should be a consideration of Greg Clark's "market principle"¹, not regulating for any particular business model, proportionality (maximum benefit for minimum cost), and basing it on evidence.

We agree that local energy has the potential to be an important area of change. We welcome the enabling of innovation and removal of barriers to decentralisation where that meets consumer needs. However, there is little detail in the FWP as to how Ofgem will undertake and initiate this.

We welcome the work of the Energy Data Taskforce and look forward to seeing its findings. Increased sharing of data will support more efficient use of the whole system to the benefit of consumers. We encourage Ofgem to take further action to ensure that distribution network

¹ <https://www.gov.uk/government/speeches/after-the-trilemma-4-principles-for-the-power-sector>

operators roll out Low Voltage/Medium Voltage network monitoring so that both network operators and market participants have visibility of where local flexibility is needed.

With regards to improved network access, we note Ofgem's aims to actively evaluate and provide views on developments at distribution level, however we believe that Ofgem may need to take more direct action to avoid conflicts of interest at the distribution level. DNOs need to be fully neutral in facilitating flexibility markets, and areas where potential conflicts exist have been identified in the Open Networks Project Future Worlds work. Without a more direct lead from Ofgem, it will be inherently difficult for the ENA to find a solution to this that meets the needs of market participants.

In relation to decarbonising energy, the decarbonisation of heat is referred to alongside decarbonisation of transport, however lack of detail prevents further exploration on how this may be achieved. Granted, this may be in the early stages however further consideration is needed into how, and to whom, regulation of heat networks will be requested.

We note and welcome Ofgem's planned assessment of the Market Making Obligation (MMO). Centrica's preferred approach to the review would be for Ofgem to suspend the MMO and allow the wholesale market to function without the mechanism, at last for a period of time. The period of observation would help inform Ofgem and market parties to understand whether any regulatory intervention is still required. In the meantime, Ofgem could gather input on ideas concerning how a different, less intrusive, mechanism may better improve liquidity in the electricity market without distorting the way the market works, should it be required. We look forward to working with Ofgem and industry in this area.

Finally, our initiatives show that existing energy suppliers can be equally as innovative and disruptive as new entrants. A regulatory framework that creates a level playing field between all market actors will give Centrica the opportunity to deliver new market models that drive benefits to consumers. Periodic updates that showcase recent innovate models and approaches would be beneficial. Similarly, a commitment to engage Ofgem to share lessons learned from our innovations would further encourage industry participants.

Network preparedness and performance

We urge Ofgem to provide more detail on the revised gas methodologies under the network charging model, to ensure a clearer understanding of expectations and plans in this area. Given the intention is to finalise the new methodology by July this year, there is little detail in the FWP as to what the revisions will focus on, and why.

Excellence in Statutory and Core functions

We also note Ofgem's plans to respond to non-compliance with effective supervisory approaches and enforcement activity. As part of this, we would like to see the more regular reporting of not just enforcement action and investigations, but of compliance issues and the associated industry lessons learned.

Further areas for consideration

We suggest Ofgem reviews the requirement for the six largest suppliers to publish Consolidated Segmental Statements (CSS). Developments have occurred in the market which means that the original rationale and scope for the CSS no longer apply. We echo Ofgem's observations in the 2018 State of the Energy Market report, concerning the reduction

in market concentration and vertical integration², and see the resulting growth of smaller and medium sized suppliers, which now represent around 25% of the domestic market. Similarly, in reference to the CMA's 2016 energy market investigation, Ofgem recognises that the degree of vertical integration of the big six energy suppliers has further reduced³. The sale of generating capacity by the big six energy suppliers has encouraged a growing shift towards decentralisation of generation. With more generators operating within the market, the potential compliance burden that CSS presents becomes more evident. Ideally, CSS requirements should be removed entirely for both domestic and non-domestic suppliers. Alternatively, for domestic suppliers they should be expanded to include all suppliers involved in obligations that are being scaled lower over time, for example the Warm Homes Discount. For non-domestic suppliers, CSS requirements should be expanded to include all suppliers. Overall, there should be a level playing field, ideally the one that involves the least regulatory burden (i.e. no CSS).

We support the scope of Ofgem's work but believe a more thorough explanation into the various activities under the FWP would be beneficial in ensuring a full understanding of the key outcomes and as a result, industry-wide collaboration.

We hope our comments will be taken into consideration and look forward to engaging with Ofgem over the next two years on the key regulatory areas in the evolving energy market.

To discuss our response in more detail please contact Maudlyn.darkwa@centrica.com.

Yours faithfully



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² p.49

³ P.50