By email:
Anna Rossington
Deputy Director, Retail Price Regulation
Ofgem

30th August 2019

Dear Anna,

RESPONSE PAPER #2: REVIEWING SMART METERING COSTS IN THE DEFAULT TARIFF CAP – DATA GATHERING

Thank you for the opportunity to respond.

We welcome Ofgem's Request for Information (RFI) relating to Premature Replacement Charges (PRCs) and additional net advertising costs. However, it is essential that Ofgem has a full dataset on which to assess the efficient costs for calculating the SMNCC. We are particularly concerned that Ofgem does not plan to collect additional information regarding IT and wider prepayment costs.

PRCs

Our response to the RFI will include information on PRCs for prepayment meters (PPMs). PPMs are a significant proportion of our meter base, and are typically new and more expensive assets with higher PRCs.

We also note that there is no allowance for PRC charges for SMETS1 meters and that this effectively means that Ofgem assumes a 100% success rate in the Enrolment and Adoption Programme. Ofgem's response to this concern was that there was no policy reason requiring suppliers to replace SMETS1 meters early. Whilst this may be theoretically correct, it significantly misrepresents the reality of the Enrolment and Adoption Programme. We would be interested to see evidence from Ofgem of any major migration programme of this complexity that achieved a 100% migration success rate. To support a full understanding of PRC charges Ofgem should seek information from suppliers about their assumptions on migration success rates for SMETS 1 meters, supported where possible by experience to date in the Enrolment and Adoption programme. We will be providing this information in response to the RFI.

Advertising costs

It is important that the scope of the RFI extends to cost categories which suppliers consider relate to encouraging customers to participate in the smart meter rollout, as distinct from usual advertising activities (media, mailshots, website, etc). A key area to consider is that Call Centre efforts to engage customers about smart have significantly ramped up as part of the deployment effort. The associated increase in call handling times and investment in additional agents would not have been captured in the 2017 opex baseline.

Areas where Ofgem does not intend to gather data

Ofgem's position regarding the recovery of suppliers' IT costs is unduly dismissive. There is no justification offered for the inappropriate use of a 15 year amortisation period. Reliance on a 2010 RFI does not provide us with confidence that initial IT costs were adequately recognised and there is the matter of increased IT costs since 2017. We have repeatedly expressed our concern about the opacity of the cap allowance for IT costs, that we have previously calculated as being potentially short by £3-7 per meter. Such materiality justifies a separate RFI to bring greater certainty regarding the accuracy of the SMNCC in this area.

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We do not agree that cost data in relation to PPM is irrelevant to the SMNCC under the default cap, for two reasons.

Firstly, in its November 2018 decision on the default tariff cap, Ofgem said it would consider using a specific prepayment method uplift when sufficient data on prepayment costs are available and after further consultation. With increasing levels of SMETS2 prepayment meter deployment and imminent commencement of the Enrolment and Adoption programme for SMETS1 prepayment meters, the number of smart prepayment meters subject to the DTC is set to increase significantly, and there should be much better visibility of relevant costs than in November 2018.

Secondly, the CMA decided that there will be no non-pass through (NPT) SMNCC allowance in the revised Prepayment Cap Review (PCR) with effect from 1 October 2019. It considers that since the PCR applies only to prepayment customers without an interoperable smart meter, it is not appropriate to include costs relating to the ‘roll-out and installation of actual smart meters’ (i.e. NPT costs). This means that, unlike credit meters where smart rollout costs are smeared across all customers (whether they have a smart or traditional meter), the NPT cost of smart prepayment meter rollout must be recovered solely from customers with fully interoperable smart prepayment meters. Suppliers who have invested in a SMETS1 prepayment solution will have incurred costs from procuring and installing a smart meter that will become interoperable once enrolled into the DCC. It is unclear how these costs will be recovered. Please clarify.

Accordingly, we believe that Ofgem should address these issues and gather additional data to ensure that all smart prepayment costs are recoverable.

We would be happy to discuss these issues further.

Yours sincerely,

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