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Protecting energy consumers with prepayment meters

EDF is the UK's largest producer of low carbon electricity. We operate low carbon nuclear power stations and are building the first of a new generation of nuclear plants. We also have a large and growing portfolio of renewable generation, including onshore and offshore wind, as well as coal and gas stations and energy storage. We have around five million electricity and gas customer accounts, including residential and business users. EDF is committed to building a smarter energy future that will support delivery of net zero carbon emissions, including through digital innovations and new customer offerings that encourage the transition to low carbon electric transport and heating.

EDF welcomes the opportunity to comment on Ofgem's initial policy options for protecting energy consumers with prepayment meters after the expiry of the current prepayment charge restriction that was introduced by the CMA following its energy market investigation.

Headlines:

- **Any continued price protection for PPM customers should be implemented through use of the Default Tariff Cap (DTC) and the introduction of an appropriate specific cap level for PPM customers.**

- **Greater transparency is required regarding Ofgem's detailed assumptions and modelling in respect of an appropriate PPM uplift. This will provide stakeholders with the ability to assess the extent to which recovery of efficient costs will be provided for under the cap.**

- **EDF agrees that only default PPM customers should be transitioned under the DTC.**

- **We are currently minded to support the transition of default PPM customers to be incorporated under the DTC as of 1 October 2020, although we recognise the challenge of undertaking the necessary full and effective consultation process during these exceptional times.**

- **Ofgem needs to undertake prompt consideration of how best to reflect within the DTC the significant financial impacts on suppliers that are emerging from the COVID-19 pandemic. The headroom provided is not sufficient to mitigate the impacts suppliers are facing, and without further adjustments would lead to suppliers under recovering their costs under the cap.**

Continued protection for PPM customers

EDF acknowledges that following the introduction of the Domestic Gas and Electricity (Tariff Cap) Act 2018 it is current Government policy that all default energy customers should be subject to price protection measures. Indeed, the Tariff Cap Act provides for default PPM customers to fall within scope of the Default Tariff Cap (DTC) where no other price protection mechanism is in place for such customers. We accept therefore that PPM customers should not, following the ending of the current PPM Cap, be treated differently to those customers with alternative meter type and/or payment methods and should remain subject to appropriate price protection measures.

However, it is on this basis only that we agree for there to be a need for Ofgem to consider how best to protect PPM customers going forward. We do not agree with any assertion that continued protection is required for PPM customers on the basis of technical barriers limiting competition and choice for such customers. For instance, there are an increasing number of PPM customers supplied through a SMETS2 meter (~120K as at February 2020) that do not face the technical barriers that the CMA put forward as a basis for its PPM Cap.

Protection Options

Of the options put forward by Ofgem, we are supportive of the proposal to use the DTC, with adjustments, as a means of providing continued price protection for PPM customers. Of the alternative options put forward, allowing default PPM customers to automatically fall under the DTC, without any other adjustments, would result in such customers being subject to the cap level intended for direct debit customers. This is currently around £50 lower than the PPM Cap Level and would result in suppliers being unable to fully recover their efficient costs of supplying PPM customers. Such an under recovery would be unfair, arguably inconsistent with the objectives of the Tariff Cap Act and is therefore opposed by EDF.

We also do not believe that a case has been made to replace the PPM Cap with another dedicated cap for PPM Customers. Making appropriate adjustments to the current DTC would appear more efficient and would ensure that price protection measures sit under a single price cap. This will allow the annual review process that is undertaken in accordance within the Tariff Cap Act, to apply collectively and consistently (i.e. including as to duration) to all customer types subject to price protection.

The current PPM Cap applies to all customers with non-interoperable meters, including those who have actively engaged in the market and chosen a fixed-term tariff. We note that Ofgem proposes to include only default PPM customers within scope of the new protection for PPM customers. We are fully supportive of such an approach as it is consistent with current Government policy and the intent of the Tariff Cap Act.

Adjusting the DTC

We are supportive of Ofgem introducing a suitable new cap level specific to PPM customers. Further to our comments set out above, there is a clear need to set an appropriate cap level that reflects the additional efficient costs of supplying PPM customers compared to those customers on standard credit or direct debit. Furthermore, we agree in principle with the proposal for a single cap level that applies to all PPM customers who will fall within the scope of the DTC following the expiry of the current PPM Cap.

Ofgem expects to set a DTC level for PPM customers that would provide a similar level of protection as the existing PPM Cap. This is on the basis that many of the cost components are common across all customer types and that that methodology used under both caps had been largely aligned following the CMA's interim review concluded in 2019. In principle, we are supportive of this general assumption; however, Ofgem's approach needs to ensure that a level is set that allows suppliers to recover their efficient costs across all customer types subject to the price cap. As such Ofgem's assessment should include, as a minimum, a review of the payment method uplift, inclusion of a non-pass through SMNCC and headroom allowance (see further comments below).

Operating costs for customers with traditional meters

We understand the logic of Ofgem's proposed approach which to a large degree is designed to maintain the DTC's methodological approach. We observe that this will maintain the current price differential between cap levels for direct debit customers and PPM customer rather than conducting further data gathering and additional assessment. However, in following such an approach it is important that Ofgem provides sufficient transparency regarding its analysis and assumptions in order to provide stakeholders with the opportunity to effectively review its methodology and underlying model and be in a position to make fully informed submissions to Ofgem as part of the consultation process.

For instance, Ofgem proposes to continue with the present cross-subsidisation that exists within the current DTC methodology, where efficient PPM costs that exceed the PPM uplift are spread across other payment methods through the operating cost allowance. Ofgem's preliminary analysis suggests that up to £5 is included in the allowance to account for incremental PPM costs above the PPM uplift. However, without seeing the underlying data behind this assumption, stakeholders are unable to comment on Ofgem's preliminary analysis and undertake any assessment as to whether maintaining the operating cost allowance unadjusted is a proportionate approach to adopt.

Considering the impact of the smart meter roll out

EDF acknowledges the logic of including a specific non-pass through SMNCC for PPM customers on the basis that the net costs of moving from legacy meters to smart meters are likely to differ between legacy PPM and legacy credit meters. In the event that this proposal is progressed, we are supportive of Ofgem using the latest Annual Supplier Reports (ASRs) as a means of assessing the principal differences between the SMNCC model for credit customers and the model for PPM customers. However, we are currently not in a position to provide any detailed comments on the impact of this proposal and the extent to which this allows suppliers to recover their efficient costs, as no detailed analysis has been provided. There is also a clear link to the ongoing wider review of the SMNNC allowance under the DTC. We would urge Ofgem to ensure that stakeholders are provided appropriate access to Ofgem's proposed SMNCC model alongside its detailed proposals for both reviews at the next consultation stage.

Timing of expiry

We are supportive of Ofgem considering how best to transition from the PPM Cap to the DTC with a view to mitigating any potential disruption or risks for customers and suppliers. Of the proposed options presented, we are currently minded to support the transition of default PPM customers to be incorporated under the DTC as of 1 October 2020. Aligning the next cap period (in terms of start date and duration) for PPM customers with that of the DTC and ending the current PPM Cap early, as permitted by the CMA following its mid-term review policy changes, will avoid the need for disruptive mid-winter price changes for both customers and suppliers.

However, the adoption of this proposal relies on Ofgem completing a full and effective consultation in advance of when a final decision on licence modifications would need to be made in order for them to take effect by 1 October 2020. Both Ofgem and stakeholders' ability to undertake this task may be detrimentally impacted by the operational constraints arising from the impacts of the COVID-19 pandemic. Appropriate contingency arrangements will therefore need to be put in place in order to ensure that appropriate price protection for PPM customers is in place at the time the current PPM cap is scheduled to expire.

COVID-19

There is a clear need for Ofgem to consider how best to reflect within the price caps the significant financial impacts on suppliers that are emerging from the COVID-19 pandemic. Although impacts are being seen across most customer types, there are specific impacts that relate directly to the supply of PPM customers including the need for additional measures to ensure such customers remain on supply and that they are fully supported throughout this exceptional period.

The current headroom allowance included within the DTC is insufficient to address the significant financial impacts being faced by suppliers through this period. Although the headroom allowance can be used to mitigate some degree of uncertainty in setting cost allowances under the cap, exceptional events such as these will have adverse impacts on suppliers that are not mitigated by the current level of headroom provided under the cap.

Furthermore, we note that Ofgem has previously argued that the headroom allowance addresses other significant market risks, including mutualisation costs that result from supplier failures. This supports the view that the headroom provided is not sufficient for the current circumstances, and without further adjustment would lead to suppliers under recovering their costs under the cap. Ofgem should look to fairly and promptly make appropriate adjustments to the DTC and the PPM Cap in order to ensure the price caps allows for full recovery of efficiently incurred costs.

Should you wish to discuss any of the issues raised in our response or have any queries, please contact Steven Eyre or myself.

I can confirm this letter is not confidential and may be published.

Yours sincerely

R. Beresford

Rebecca Beresford
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