

All stakeholders

Email: RetailPriceRegulation@ofgem.gov.uk

Date: 1 June 2021

Dear all,

Price Cap – addendum to consultations on reviewing the credit and PPM SMNCC allowances

On 29 April 2021, we published two consultations on the Smart Metering Net Cost Change (SMNCC) allowances in the default tariff cap ('cap') – one for credit meters and one for prepayment (PPM) meters.¹ This document is a short addendum to both of these consultations. We refer to these collectively as the 'April 2021 consultations' for the remainder of this addendum.²

The Department for Business, Energy and Industrial Strategy (BEIS) announced on 1 June 2021 that it has decided to extend the 'all reasonable steps' framework for the smart meter rollout for six months. This addendum sets out the implications of this decision for our April 2021 consultations. We are publishing this addendum to allow stakeholders to consider our preferred approach in this new context ahead of submitting their consultation responses. Given the publication of this addendum, we are extending the closing date for the April 2021 consultations from Friday 11 June 2021 to **Tuesday 15 June 2021**.

We are seeking views from stakeholders on our proposal to adopt a contingency allowance based on the SMNCC model for cap period 7 (which begins in October 2021). We are continuing to seek views from stakeholders on our proposals from the April 2021

¹ Ofgem (2021), Price Cap – final consultation on updating the credit SMNCC allowance.
<https://www.ofgem.gov.uk/publications-and-updates/price-cap-final-consultation-updating-credit-smncc-allowance>

Ofgem (2021), Price Cap – final consultation on updating the PPM SMNCC allowance.
<https://www.ofgem.gov.uk/publications-and-updates/price-cap-final-consultation-updating-ppm-smncc-allowance>

² As this is a short addendum, it should be read alongside the April 2021 consultations. The April 2021 consultations provide more detail on the concepts we discuss in this addendum.

consultations in relation to cap period 8 (which begins in April 2022). We will issue a short consultation in the autumn on the impact of BEIS's decision for the rollout profiles included in the SMNCC model for cap period 8.

Context

As part of our April 2021 consultations, we set out our proposals for taking account of BEIS's proposed new smart metering rollout framework in the SMNCC model. BEIS consulted on the annual tolerances associated with this rollout framework in November 2020.³

BEIS has now published the government response to the consultation.⁴ In particular, BEIS has decided to extend the current 'all reasonable steps' rollout obligation for six months. This means that the proposed new rollout framework will take effect from 1 January 2022, rather than 1 July 2021.

We review the SMNCC allowance annually. The current annual review covers two cap periods – cap period 7 (October 2021 to March 2022) and cap period 8 (April 2022 to September 2022). We discuss the implications of BEIS's decision for each of these cap periods separately in the sections below.

Our immediate priority is to set an appropriate SMNCC allowance for cap period 7, which we must do by early August 2021. When doing this, we must protect default tariff customers, in line with the objective of the Domestic Gas and Electricity (Tariff Cap) Act 2018.⁵

We also want to make progress towards setting the SMNCC allowance for cap period 8, building on the April 2021 consultations and the work stakeholders will have done to consider these already.

Our ongoing annual review process means that we will include actual rollout data when it becomes available, and use this to recalculate the SMNCC for previous cap periods. We will then take into account (through advanced payments) any discrepancy between this recalculated SMNCC and the allowance previously provided. The profile we use to project

³ BEIS (2020), Smart meter policy framework post 2020: minimum annual targets and reporting thresholds for energy suppliers. <https://www.gov.uk/government/consultations/smart-meter-policy-framework-post-2020-minimum-annual-targets-and-reporting-thresholds-for-energy-suppliers>

⁴ BEIS (2021), Smart Meter Policy Framework post 2020: Government response to a consultation on minimum annual targets and reporting thresholds for energy suppliers. <https://www.gov.uk/government/consultations/smart-meter-policy-framework-post-2020-minimum-annual-targets-and-reporting-thresholds-for-energy-suppliers>

⁵ Domestic Gas and Electricity (Tariff Cap) Act 2018, section 1(6). <http://www.legislation.gov.uk/ukpga/2018/21/section/1/enacted>

rollout therefore only has a temporary impact on the amounts that customers pay and suppliers receive under the cap.

Next steps for cap period 7 (October 2021-March 2022)

In light of BEIS's decision, **we now intend to adopt a contingency allowance for cap period 7**. Our April 2021 consultations were based on the policy on which BEIS consulted in November 2020, rather than an extension of 'all reasonable steps'.

In our April 2021 consultations, we said that – should we need to adopt a contingency allowance – we proposed to use the SMNCC model as a starting point. This remains our proposal, for the reasons set out in our April 2021 consultations.⁶ BEIS's decision does not require extensive changes to our proposals from the April 2021 consultations – we are therefore still able to rely on the SMNCC model as the starting point for our contingency allowance.

We intend to take into account the extension to 'all reasonable steps' when considering how to adapt the SMNCC model to set the contingency allowance for cap period 7. We propose to take the following steps.

- We propose to assume that rollout in Q3 and Q4 2021 (for our proposed rollout profiles)⁷ will be the same as the supplier forecasts for Q2 2021 provided to BEIS.⁸ We consider that this is the best available information on the progress suppliers can achieve under 'all reasonable steps'. This is because it is recent information, for a period without the most significant societal restrictions due to COVID-19.
- We then propose to start estimating rollout using the new framework from 1 January 2022.

As we have not yet had time to calculate revised rollout profiles based on the latest data, we cannot provide a revised forecast of the SMNCC allowances. However, our current expectation is that they will not be significantly different from our April 2021 consultation

⁶ Ofgem (2021), Price Cap – final consultation on updating the credit SMNCC allowance, paragraphs 6.12 and 6.19 to 6.20.

<https://www.ofgem.gov.uk/publications-and-updates/price-cap-final-consultation-updating-credit-smncc-allowance>

Ofgem (2021), Price Cap – final consultation on updating the PPM SMNCC allowance, paragraphs 7.26 and 7.28 to 7.33.

<https://www.ofgem.gov.uk/publications-and-updates/price-cap-final-consultation-updating-ppm-smncc-allowance>

⁷ A market leader rollout profile for credit and an average rollout profile for PPM. We are not seeking to project overall market rollout in the second half of 2021.

⁸ The rollout information that we have for 2021 is the numbers of meters installed. We therefore intend to make the following assumptions when calculating cumulative rollout percentages for 2021: that each supplier's customer numbers are unchanged since the end of 2020, and that the only change in a supplier's smart meter customer numbers is due to new installations. We consider that these minor assumptions are appropriate over a short period of time.

proposals, and that they will likely be lower than the current SMNCC allowances used for cap periods 5 and 6.

We do not otherwise propose to alter the proposals we set out in our April 2021 consultations. As part of these consultations, we already indicated that we intended to take account of certain aspects of BEIS's decision, such as the final tolerance values. This is unaffected by BEIS's decision to extend 'all reasonable steps'.

Implications for stakeholder comments on cap period 7 in response to the April 2021 consultations and this addendum

We welcome comments from stakeholders on the approach described in this section. In particular, we welcome views on:

- whether we should use a contingency allowance to set the SMNCC for cap period 7
- (if we adopt a contingency allowance) what type of contingency allowance we should use – a contingency allowance based on the SMNCC model or a different approach, such as using the same SMNCC values as in cap periods 5 and 6
- our proposals to amend the rollout profile in the SMNCC model by using Q2 2021 forecasts to estimate Q3 and Q4 2021 and by starting to estimate rollout using the new framework from 1 January 2022 when estimating the contingency allowance (under our proposed approach of a contingency allowance based on the SMNCC model).

Given our proposal to adopt a contingency allowance based on the SMNCC model, we continue to welcome comments on the matters discussed in our April 2021 consultations. These matters are still relevant to cap period 7 under our proposal. This is because we would still use a rollout profile based on the new framework from the start of 2022,⁹ and because the non-rollout matters discussed in our April 2021 consultations do not just apply to the years when the new framework has effect.

Next steps for cap period 8 (April-October 2022)

The April 2021 consultations still provide the opportunity to comment on most of our proposals for cap period 8. Most of our proposals from the April 2021 consultations are unaffected by the extension of 'all reasonable steps'. Stakeholders will therefore be able to provide full responses to our April 2021 consultations in these areas, and we expect them to do so.

⁹ When modelling the SMNCC, we calculate the net costs of smart metering for each calendar year, and we use rollout inputs at calendar year level. The SMNCC allowance for a winter cap period is the average of SMNCC allowances for the two calendar years which cover parts of that cap period. For cap period 7, this means 2021 and 2022. The rollout profile used in 2022 therefore affects the SMNCC allowance for cap period 7.

However, we have more time available before we need to take a decision on the SMNCC allowances for cap period 8 (than we do for cap period 7).

Therefore, **we intend to issue a short consultation in early autumn 2021** ('early autumn consultation').¹⁰ This will focus on the impact of BEIS's decision for the rollout profiles included in the SMNCC model – specifically the impact on the period before the new framework takes effect (ie the second half of 2021). At this point, we will also be able to publish revised proposed SMNCC allowances for cap period 8. Stakeholders may also use this opportunity to provide any further representations on the impact of BEIS's decision.

This early autumn consultation would be much shorter than our April 2021 consultations. It would not cover all the same issues as our April 2021 consultations, given that most of our proposals are unaffected by the extension of 'all reasonable steps'. We also do not intend to conduct a disclosure process alongside the early autumn consultation – we consider that we can provide sufficient transparency on how we would amend the rollout profiles through our published consultation document.

We will consider responses to both the April 2021 and early autumn consultations when reaching our decision for cap period 8. Stakeholders therefore do not need to repeat points from their responses to the April 2021 consultations when responding to the early autumn consultation. We expect stakeholders to focus their responses to the early autumn consultation on the new information provided.

We will publish a decision on the SMNCC allowance for cap period 8 by early February 2022. We will respond to stakeholder comments on both consultations through this decision. As a consequence, our August 2021 decision will only confirm the SMNCC allowances for cap period 7, and will not set out SMNCC allowances for cap period 8.

We consider that this two-stage process is the most proportionate approach available. It seeks to make the best use possible of the April 2021 consultations, which we have already published and which stakeholders have already started to consider.

Implications for stakeholder comments on cap period 8 in response to the April 2021 consultations and this addendum

Stakeholders should respond to the matters discussed in the April 2021 consultations.

We also welcome any comments from stakeholders on the two-stage process described above, including any suggestions for elements we should discuss in the early autumn consultation.

¹⁰ By "short consultation", we mean that this would be a short document. The consultation would still last at least four weeks.

Closing date for consultations

Given the publication of this addendum, we are extending the closing date for the April 2021 consultations from Friday 11 June 2021 to **Tuesday 15 June 2021**. This is to give stakeholders additional time to consider this addendum (and relevant elements of BEIS's decision) when preparing their responses. We have outlined above the areas where we are particularly seeking comments for cap periods 7 and 8 – we expect stakeholders to provide any representations on these areas by the closing date.

We recognise that this is a short extension. However, we are unable to provide further time. We must publish a decision on the SMNCC allowances for cap period 7 by 5 August 2021, and we must have sufficient time to consider responses before this. Based on our experience of previous consultations, we consider that we should plan for a period of at least this length when making a decision of this nature and complexity. As the new issues raised are limited in scope, we consider that stakeholders will have sufficient time to respond.

Contact details

If you have any questions about this addendum, please contact us at:

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Yours faithfully,

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