

Angelita Bradney
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Sent via e-mail: switchingprogramme@ofgem.gov.uk

Dear Angelita,

British Gas response to Ofgem's Final proposals on DCC's role in developing a Central Registration Service and penalty interest proposals

British Gas is supportive of Ofgem's work to improve the switching process for customers and is committed to working with both Ofgem and industry to deliver this.

We welcome Ofgem's decision to remove the requirement for DCC to draft any code modifications and to proceed with a 'report and direct' framework for setting the penalty interest rate.

However, we still have some outstanding concerns:

- We do not support using a mixture of ex-post and ex-ante price controls for the DCC. We consider it to be confusing to the customers of the DCC, and less efficient than adopting a purely ex-post regime.
- We believe that the regulated revenue threshold of 110% is too high. We see no justification for why it should be greater than our proposed 106%.

Our responses to the specific questions posed by Ofgem are appended to this letter. If you have any questions on our response, please contact Tabish Khan at tabish.khan@britishgas.co.uk.

Yours sincerely,

Sharon Johnson
Director of Regulatory Affairs

Appendix 1: British Gas views on questions posed within the Ofgem consultation dated 17 December 2015 in respect of DCC's role in developing a Central Registration Service and penalty interest proposals

Question 1: Do you agree with our proposed changes to SLC15 of DCC's licence?

Yes we agree that the Central Registration Service should be a mandatory business objective in SLC15.

Question 2: Do you agree with the proposed considerations that we would expect the DCC to take into account when seeking to meet its new objective?

Yes, these considerations are appropriate.

Question 3: Do you agree with our proposed drafting amendments to the price control formula to allow the Authority to include ex-post and ex-ante arrangements as well as uncertainty and incentive mechanisms?

No, we believe that the mixture of ex-post and ex-ante arrangements will be confusing to both the DCC and their direct customers (i.e. energy suppliers and networks). An ex-post regime would avoid the need for uncertainty mechanisms, whilst allowing incentive mechanisms to motivate the DCC's delivery of the service. Any incentive mechanism would need to be balanced with rewards and penalties ensuring that the key milestones and deliverables are achieved.

We remain unconvinced that ex-ante arrangements are more efficient and effective for energy consumers. Our experience suggests that monopoly businesses simply add in premiums to their costs in the knowledge that they will be challenged and reduced. With the DCC's limited direct comparators or competitors, benchmarking the DCC's costs will be more difficult than the energy networks. Therefore we believe that a fully ex-post regime would be the best fit for the DCC and deliver the best value for money for consumers.

Question 4: Do you agree with the proposed timetable and process for agreeing the ex ante procurement costs as well as any uncertainty or incentive mechanisms where these are used?

Whilst we do not agree with the ex ante approach the timetable appears to be appropriate.

We agree that the Central Registration Service should have its own term within the allowed revenue formula. And the DCC should be encouraged to share the breakdown of costs within this allowed revenue variable.

We believe the new variable should include its own correction factor. This will allow for any over or under recovery to be given or collected from those paying for and benefitting from the service.

Question 5: Do you agree with the proposed changes to introduce a new defined term of Fundamental Registration Service capability to ensure that the DCC procures the CRS externally?

Yes, we agree with the proposal.

Question 6: Do you agree with the proposed changes to include CRS as a new service in the Mandatory Business service requirements?

Yes

Question 7: Do you have any views on the proposed consequential changes to the licence?

We consider all the proposed licence and code changes to be appropriate.

Question 8: Do you agree with our proposed amendment to the definition of Regulated Revenue in LC35?

We agree that interest received on service charges above allowed revenue should be returned to users.

We believe that the threshold of 110% is too high, 106% is the maximum as per our comments to the previous consultation. For Ofgem's convenience we have included our previous response on this question within appendix 2.

Question 9: Do you agree with the proposed drafting for the penalty interest rate and that it reflects the policy intent?

Yes, we agree with the licence drafting and that it reflects the policy's intent.

Appendix 2: British Gas response to question from previous consultation

What do you think appropriate thresholds of tolerance should be for over-recovery?

We are unclear on the source of the 110% threshold which has been referred to, in paragraph 5.32 of the consultation document, as “...*threshold precedent over-recovery threshold for penalty interest rates in the networks’ licence...*” Rather, we note the threshold for gas and electricity distribution network operators is 106%. Special condition 1B.14 of the gas distribution network operators’ licences states:

For the purposes of Part D of this condition, the value of the interest rate adjustment PR_t for the relevant Distribution Network is to be treated as follows:

(a) if, in respect of Formula Year $t-2$, Distribution Network Transportation Activity Revenue for the relevant Distribution Network exceeds 106 per cent of Maximum Distribution Network Transportation Activity Revenue, PR_t will have the value of 3;

(b) if, in respect of Formula Year $t-2$, Distribution Network Transportation Activity Revenue for the relevant Distribution Network is less than 94 per cent of Maximum Distribution Network Transportation Activity Revenue, PR_t will have the value of zero; and

(c) in all other cases PR_t will have the value 1.5.

Similarly, special condition 2A.18 of the electricity distribution network operators’ licences states:

For the purposes of Part E of this condition, for Regulatory Years 2017/18 onwards the values of the interest rate adjustments PR_{t-2} is derived as follows:

(f) If, in respect of Regulatory Year $t-2$, RD_{t-2} exceeds 106 per cent of AR_{t-2} , PR_{t-2} will have the value of 3;

(g) if, in respect of Regulatory Year $t-2$, RD_{t-2} is less than 94 per cent of AR_{t-2} , PR_{t-2} will have the value of zero; and

(h) in all other cases PR_{t-2} will have the value of 1.5.

On this basis, we believe the precedent is 106% rather than 110%. On current charges for 2015/16 an over recovery of between 110% and 115% would equate to £17m in 2015/16 up to £32m by 2018/19. We believe this is a significant value that customers are financing; therefore the percentage range should be lower to incentivise greater controls within DCC. By comparison, a 6% threshold would equate to values between £6.8m in 2015/16 to £12.8m by 2018/19, saving customers almost two-thirds of the over recovery.

We believe there is a strong case for setting the threshold below 106% when consideration is given to the sources of volatility that may contribute to under- or over-recovery. NWOs’ allowed revenues are linked to energy consumption, which at times has been difficult for NWOs to forecast. However, DCC’s allowed revenue is linked to customer numbers which has remained relatively stable over time and are inherently less difficult to forecast. We also note that some NWOs have suggested under- or over-recovery is more likely because of their obligation to set ‘use-of-system’ charges up to 15 months in advance; DCC is subject to no such obligation. We suggest parity with the thresholds within the networks sectors is unnecessary for these reasons in this instance and welcome further consultation on this matter.