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Prepayment price cap or 'safeguard tariff'

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Introduction

- In June 2016, the CMA released its final report following its two year investigation into the energy market.

- The CMA remedies included a temporary cap on the amount suppliers can charge prepayment customers, to be introduced from April 2017. It has also set the methodology used to determine the level of the cap.

- The safeguard tariff is designed to give prepayment customers – who have not been able to benefit from competitive prices in the same way as other customers - a better deal in the period before the smart meter rollout is completed.

- Ofgem is responsible for administering the safeguard tariff and publishing the cap levels each year in February and August (separate values will be published for each meter type and region).

What is the prepayment safeguard tariff?

- The cap places a restriction on the amount suppliers can charge their prepayment customers for a given level of consumption.
- The safeguard tariff will apply to all customers on a tariff which requires them to prepay, apart from those on “fully interoperable” smart meters, which will be excluded from the cap
- Different levels of the cap will apply to distinguish between standard electricity meters with a set rate, and electricity meters with different peak and off peak rates, for example economy 7 meters.
- The safeguard tariff is a transitional measure running from April 2017 until December 2020, when the roll out of smart meters is expected to be completed.
- Initially, the safeguard tariff will apply to about 4 million households, mostly those on pre-payment meters. Over time, this number is likely to fall as prepayment customers gradually move onto “fully interoperable” smart meters.

Why a safeguard tariff for prepayment customers?

- Prepayment customers are denied the best deals on the market which are available to those that pay using other payment methods. Tariffs are generally more expensive and even those who switch save much less

- The CMA report found that prepayment customers face particularly high levels of detriment as a result. They are also more likely to be in vulnerable circumstances, and more likely to be in debt.

- Unlike other customers, where prepayment customers face too high a price, they may not be able to top up – leading to 'self disconnection'

Why is the safeguard tariff temporary?

- Smart meters will lower suppliers' costs to serve customers on pre-payment meters which should result in more competitive deals
- Smart meters are likely to result in a wider choice of prepayment tariffs being made available to prepayment consumers.
- Smart meters will enable consumers to switch more easily between credit and prepayment methods.
- Smart meters will provide greater flexibility for consumers' credit arrangements in both conventional and emergency situations, for example by allowing customers to top up online
- Consumers will be able to monitor and add credit where necessary throughout the day, allowing greater flexible energy usage.

How is the safeguard tariff set?

- To calculate the level of the cap, we begin by taking the initial benchmark, calculated by the CMA

- This is then updated using three indices, to reflect broad trends in suppliers' costs since the benchmark was set. The indices are:
  - An index of wholesale prices covering the 6 months prior to the cap being set
  - Environmental levy forecasts from the Office for Budget Responsibility
  - The Consumer Price Index (inflation)

- An allowance for network charges is also calculated into the cap, based on network companies' published charges. This component causes the cap to vary by region.

- Finally, the cap includes a degree of "headroom", designed to allow suppliers to offer competitive deals underneath it

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Updating the safeguard tariff

- Every six months, we will publish the level of the cap that will apply in each region, for each meter type. The cap is expressed in pounds, excluding VAT.

- Levels of the cap are published for a customer that does not use any energy, and for a customer that uses a pre-set amount of energy, *m* (similar to typical consumption levels). The level of the cap for all other possible consumption levels can then be derived using these values.

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