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By email: fwp@ofgem.gov.uk

### **Forward Work Programme 2018/19**

We welcome the opportunity to comment on the draft Forward Work Programme (FWP) for the year 2018/19. We support Ofgem's drive to facilitate competition and enable innovation to deliver better customer outcomes.

Giving stakeholders visibility of upcoming reforms allows them to prepare. To further facilitate preparation, it would be beneficial if Ofgem included an indicative change timetable in the final version of the FWP<sup>1</sup>. Having more transparency of expected delivery timeframes from Ofgem would be useful for planning purposes.

We agree that changes are needed in the regulatory landscape, but believe that more could be done to identify and explain how they interact. We welcome Ofgem's focus on innovation through its Future of Retail Regulation (FRR) and Future Supply Market Arrangement (FSMA) programmes. However, Ofgem is proposing a large and complex programme of work for domestic consumers, and it would be helpful if Ofgem set out in the FWP how the changes Ofgem is proposing interact. For instance, we would like to understand how Ofgem's reforms to promote consumer engagement interact with its proposals to introduce price caps, which we expect to have the opposite effect. We believe this would be helpful in informing how the various work programmes could be scheduled, and their effectiveness monitored.

Last year, we saw Ofgem reaching a preliminary view and making a final decision more quickly than it has done historically, as detailed in the appendix of our response. While we agree that Ofgem should move quickly where appropriate, in doing so it should not sacrifice full and thorough impact assessment. We ask Ofgem in the coming year to place a greater focus on considering the full consequences of all policy options before reaching a preliminary and final view.

For our response, we have chosen to comment on those areas we consider likely to have the most material impact for our customers. These are:

- Price caps;

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<sup>1</sup> We note that Ofgem has committed to publish a list of all planned activities for 2018/19. An accompanying timetable for the full year would be very useful

- Faster, more reliable switching;
- Supplier conduct and customer engagement;
- Regulating networks;
- Future supply market arrangements; and
- Further areas for consideration.

We hope our comments provided in this response are useful and will be taken into consideration.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Tim Dewhurst', written in a cursive style.

Tim Dewhurst

Head of Regulatory Affairs, UK & Ireland

## **Appendix**

### **Price caps**

Despite our profound concerns about the negative consequences of price caps for consumers and competition, we have implemented the extension of the PPM price cap to customers on the Warm Home Discount (WHD). Ofgem must urgently review the methodology behind setting the level for the cap before it proceeds any further. If further price protection is introduced, it is vital that it is set at an appropriate level that suppliers can recover their efficiently incurred costs when serving vulnerable customers. It will not serve the long-term interests of vulnerable customers if price caps impose a commercial penalty on suppliers who cater for vulnerable customers.

We are concerned how Ofgem has arrived at decisions on price caps to date. For example, we do not believe that Ofgem took proper account of stakeholders' responses to the consultation on extending the PPM cap to WHD before issuing the consultation on introducing a further price cap for vulnerable customers. There was only a two week gap between the decision on the former and consultation on the latter. For such a major intervention, it is even more important to follow a full and thorough consultation process, taking sufficient time to deliver robust regulatory decisions.

It is critical that Ofgem ensures that there is sufficient time to consider – and appropriately consult on – all methodologies prior to setting any wider cap on all standard variable and fixed-term default tariffs.

### **Faster, more reliable switching**

To make sure the outcome of the Switching Programme is right, Ofgem needs to strike the right balance between seeking flexibility for future market innovation, and potential reduction in delivery risk and cost to implement offered by the re-use of existing industry systems. We expect that the costs to consumers will be minimised through the efficient procurement process for Centralised Switching Service providers, that starts in 2018.

As the next step, we urge Ofgem to develop a realistic plan for the Design, Build and Test phase of the programme, incorporating lessons learnt from previous large scale industry programmes. With so many complex processes being affected by the programme, the plan must allow sufficient time for robust design and test activity, prioritising finding the right solutions over shorter timescales.

### **Supplier conduct and consumer engagement**

In 2017/18 Ofgem has made positive changes to enable suppliers to better engage customers. For example, Ofgem removed the obligation for customers to move to an evergreen tariff at the end of their fixed term contract, which will enable us to introduce a new fixed term default tariff that will better prompt engagement than our Standard Variable Tariff (SVT). We agree that customer engagement should remain an important focus in 2018/19.

Arguably the biggest positive change to supplier conduct will come from the introduction of principles based regulation (PBR) to customer communications, and removal of unnecessary prescription. Supplier and Ofgem research has found that customers find the communications they receive from their supplier confusing and difficult to engage with. Ofgem's working paper with initial proposals on how it intends to move towards PBR for customer communications has been a welcome step. We believe the draft principles require further refining before Ofgem progresses to a policy consultation. We expect that the final principles, due in 2018/19, will enable suppliers to innovate and personalise their communications with customers, increasing engagement.

It is encouraging that Ofgem will be revisiting its Consumer Vulnerability Strategy (CVS) in 2018. The definition of "vulnerable" has evolved since the initial CVS was issued in 2013. We strongly believe that all requirements upon suppliers must be aligned, removing any small supplier exemptions. All vulnerable customers should be afforded the same benefits (e.g. WHD) and services, irrespective of which supplier they are with, and customers who are with smaller suppliers should bear the costs in the same way as customers of larger suppliers. It is vital that markets work for all customers and Ofgem does not inadvertently create a situation where financially vulnerable customers are deterred from engaging because legacy suppliers are the only ones offering financial support such as WHD and the vulnerable customer price cap.

We note that Ofgem intends to trial new ways of helping customers engage in the market in 2018/19. We support the concept of trialling, given that this promotes the development of evidence-based regulatory policy. However, Ofgem should recognise that suppliers have limited capacity in undertaking trials, and therefore factor in opportunity cost into trial planning.

## **Regulating networks**

Network regulation continues to be at the forefront of the regulatory agenda, particularly because of the increased public and political focus on appropriate returns. Several changes planned by Ofgem in 2018/19 may help regulate monopoly network providers more effectively.

Regulating monopoly network providers and setting them appropriate targets in price control delivers a better deal for customers. The targets should be put through an appropriate analysis, before they are approved. A specialist forum, aimed at reviewing any outputs coming out of the price control working group, would help to ensure full scrutiny.

While we believe Ofgem should keep retrospective reviews at a minimum, we understand the potential need to have a Mid-Period Review (MPR) to RIIO-ED1. We have responded to the recent consultation on the potential RIIO-ED1 MPR, where we provided our comprehensive views. We continue to believe that Ofgem should introduce an output relating to the Distribution Network Operator (DNO) performance in facilitating the smart meter rollout. The Service Level Agreement (SLA) is an insufficient incentive for networks to perform effectively and the raised modification to the DCUSA, if implemented, would lack a performance management framework to hold DNOs to account. Setting an explicit output

would provide this transparency as the level of performance must feature in an assessment of the efficient use of funding.

We are concerned about Ofgem's approach to targeted charging review ('Charging Futures' forum), particularly the evaluation of options. We believe that Ofgem might be discarding some options too early. At the same time, some of the solutions that are still being considered are costly, compared to perceived benefit. For example, the current arrangements of recovering revenue through usage related charges should not be dismissed. Making limited well-designed changes to current arrangements could address the most significant distortions and minimise the costs of implementation. Before Ofgem proceeds with any decision in the charging review, it should undertake a thorough impact assessment of all the options available, including those already rejected.

### **Future supply market arrangements**

In November 2017, Ofgem launched its review into future supply market arrangements, issuing a call for evidence to market participants. We agree that regulation of the energy market needs to be reviewed to ensure that it keeps up with innovation in the sector, and are fully supportive of this piece of work.

Centrica has already launched several innovative projects that demonstrate how the market is changing and may change in future:

- We are a market leader in Connected Home products. Our Hive smart thermostat and other Hive services help our customers manage their energy use more effectively.
- We have invested in LO3, a pioneer in using blockchain technologies that worked on a first of its kind blockchain microgrid project in Brooklyn, New York.
- With a £19m investment, we are creating a local energy market (LEM) in Cornwall that will include a virtual marketplace enabling domestic and business customers to trade energy with flexibility amongst themselves, and with the grid.
- Our Distributed Energy and Power division has been established to help customers gain competitive advantage from energy, delivering intelligent end-to-end energy solutions that power performance, resilience and growth. These solutions include working with business customers to deliver energy efficiency, demand side response, combined heat and power, back-up generation and battery storage.

Our work illustrates that market disruptors do not necessarily need to come from outside of the industry. Given the right conditions, established market participants can also deliver innovative market solutions. When creating new market arrangements, Ofgem must ensure a level playing field between current market participants and new entrants. If one set of market participants, i.e. existing energy suppliers, face more onerous regulations than new entrants, this would have an adverse impact on competition as the former would be prevented from innovating and customers will ultimately lose out through less attractive propositions.

## Further areas for consideration

We support the scope of Ofgem's work but believe even more could be done to better protect customers and promote engagement.

In December 2016, we wrote to Ofgem asking it to urgently review its policies and procedures to protect consumers from irresponsible and unsustainable business models operated by new and potential new market entrants. Since then, there have been increasing calls for action from a variety of stakeholders, and a growing body of evidence which suggests that consumers are being exposed to unacceptable risks. Despite these developments, we have not observed any substantive action from Ofgem in this area besides operating the current Supplier of Last Resort (SOLR) mechanism. We strongly reiterate our request that Ofgem urgently reviews its policy and procedures for protecting consumers from irresponsible and unsustainable business models operated by new and potential new market entrants.

To help customers more, in November 2017 we published a series of commitments – a comprehensive change package that we are currently preparing to deliver. In addition, we have asked Ofgem and the Government to consider seven areas, outside of our control, that would help make the market fairer for customers:

1. Phase out Standard Variable Tariffs altogether;
2. Level the playing field on social and environmental policy costs included in the bill;
3. Move the funding of all government policy costs out of energy bills. They should rather be paid for through general taxation;
4. Make the smart meter rollout more efficient and effective;
5. Be more consistent in the way vulnerable customers are treated, through better definition of vulnerability;
6. Simpler bills; and
7. Refresh the calculation of the price cap for customers on pre-payment meters.

We believe Ofgem should consider the merits of these proposals and endorse those changes that require Government intervention, such as levelling the playing field on the costs of social and environmental policy. We welcome the position adopted by Ofgem in its response to the National Infrastructure Commission Assessment<sup>2</sup> consultation, highlighting lack of level playing field across market participants. We hope Ofgem continues to press for the removal of certain supplier obligations and/or small supplier exemptions in the future.

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[https://www.ofgem.gov.uk/system/files/docs/2018/02/ofgem\\_national\\_infrastructure\\_assessment\\_response\\_1.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/02/ofgem_national_infrastructure_assessment_response_1.pdf)