

Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

Email to: retailpriceregulation@ofgem.gov.uk.

3 May 2018

Working paper #4: Treatment of environmental and social obligation costs

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, storage, and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including residential and business users.

Key points:

- **In general, we are supportive of the direction Ofgem's current thinking is taking on the treatment of social & environmental costs.**
- **We are concerned that neither this nor any of the other working papers deals with smart metering costs.**
- **We agree that for the majority of the schemes, suppliers have little control over the costs.**
- **Ofgem is right to adopt an approach that would set the cap in a way that reflects the policy costs incurred by a fully obligated supplier and allows for such costs to be fully recovered for those schemes where suppliers have no control over the costs.**

Ofgem's current view

In general we are supportive of the direction Ofgem's emerging thinking is taking regarding the treatment of social and environmental costs and welcome that Ofgem is duly considering the points raised by the industry in previous consultations.

We agree that there needs to be some thought around how the cost of meeting social and environmental obligations is reflected in the price cap as we do not believe the current methodology for the prepayment price cap gives a robust approach.

Use of benchmarking

We agree that for the majority of the schemes that fall under the social and environmental obligation basket, suppliers have little control over the costs. Such that Ofgem is right to adopt an approach that would allow a fully obligated supplier to fully recover the costs of such schemes.

We agree that to some extent suppliers do have some control over the costs that fall under the Renewables Obligation and Energy Company Obligation and that Ofgem is right to consider how such should be treated under the cap, informed by the cost information provided by obligated suppliers.

Setting the baseline level of the cap

The working paper sets out three options for calculating the historic costs of each scheme for the purposes of setting the baseline. We agree that Ofgem should consider using different options for different schemes, as it should use the most appropriate source for obtaining reliable data for each scheme.

The current PPM cap methodology does not allow updates to the base period index value. If Ofgem were to use a similar approach for indexing as the CMA they should allow for retrospective updates to the base data where these become available.

How policy costs vary with consumption

We agree with Ofgem that the majority of policy costs vary with consumption and we believe this should be reflected in the price cap, for both standard and Economy 7 meters.

Obligation thresholds

Consistent with the approach taken in the existing safeguard tariffs, we agree that the cap should reflect the costs incurred by a fully obligated supplier in steady state.

Updating the cap using cost forecasts

Ofgem should review its chosen approach frequently when the price cap is in place, to ensure it accurately covers the costs of suppliers meeting social and environmental obligations and to ensure it reflects any new policy costs, or fundamental changes to current schemes (such as EII exemptions and ECO3).

We agree that Ofgem should consider whether any changes to the use of OBR forecasts are required, particularly in the context of ECO and EII. For EII, converting OBR forecasts to £/MWh estimates would appear to address the issue, although we note that the working paper does not make this clear. In terms of ECO, we believe that adding an explicit forecast for ECO, based on BEIS recent impact assessment may be an improvement on the current methodology.

Smart metering costs

We are concerned that neither this nor any of the other working papers have focussed on the costs of smart metering. The smart programme is a significant and growing costs to

consumers, and it is not adequately reflected in the current PPM cap methodology. It is essential that suppliers who are continuing to invest in their programmes are able to recover their costs. We believe Ofgem should carry out analysis of the costs, identifying what was included in the benchmark under the current PPM cap and collect cost data from suppliers in order to ensure the real costs faced by suppliers are fully accounted for in the cap level. We would welcome early clarity from Ofgem as to its emerging thinking on the treatment of smart metering costs.

Should you wish to discuss any of the issues raised in our response or have any queries, please contact me on 0203 219 6937.

I confirm that this letter may be published on Ofgem's website.

Yours sincerely,

A handwritten signature in blue ink that reads "Paul Delamare".

Paul Delamare
Head of Customers Policy and Regulation