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Date: 12 December 2019

Reviewing smart metering costs in the default tariff cap: Contingency decision for Cap period four

In October, we published a consultation on updating the way we calculate the allowance in the Default Tariff Cap ("the Cap") for the smart meter rollout (the non-pass through Smart Meter Net Cost Change allowance ("SMNCC")). We proposed a methodology based on the latest assessment made by the Department for Business, Energy and Industrial Strategy (BEIS) of the pace and costs of the smart meter rollout. The consultation period closed on 19 November.[1]

The SMNCC in Cap period four

We update the Cap level every six months. In order to include any new methodology in the next Cap update we needed to publish a decision on that new methodology by 12 December. This is to ensure that the relevant modification would be in effect prior to the next Cap update at the beginning of February.

In the October consultation we also included a proposal for a contingency allowance for Cap period four. We proposed to use this contingency allowance in the event that we needed to make significant changes to the methodology and consult on those proposals, or we could not publish a conclusion on the proposed methodology by 12 December. In their representations, suppliers recommended that we use the contingency allowance.

We have decided to use the contingency allowance for the next Cap update. We will announce that Cap update on 7 February 2020, with effect from 1 April 2020. The changes being made are set out in the Appendix to this letter and take effect through changes to Annex 5 of SLC28AD.

[1] Ofgem (2019), Reviewing smart metering costs in the default tariff cap: October consultation. https://www.ofgem.gov.uk/publications-and-updates/reviewing-smart-metering-costs-default-tariff-cap-october-consultation

Developing the new methodology

We have not yet reached a conclusion about the methodology we proposed in the October consultation. It may be the case that, after further deliberation, we conclude that our proposals set a reasonable allowance, in which case we might proceed to a decision with the intention that these changes in methodology would be in place for the subsequent cap period (Cap period five commencing 1 October 2020). Alternatively, we may conclude that we need to significantly adjust the proposed methodology, or aspects of it, in which case we would consult stakeholders on those changes.

There is a risk that the contingency allowance is higher than the amount that default tariff customers should pay towards the smart meter rollout in Cap period four. If that is the case, then in the October consultation we proposed to adjust future allowances to take account of that additional charge.[2] In doing so, we would seek to ensure that the allowances a customer is charged over the life of the Cap reflect the efficient costs of an average supplier over that period of time. As suggested by some suppliers, we will consider that proposal as part of our decision on the proposed methodology. This document does not conclude on that proposal.

Suppliers' views

Nine stakeholders responded to our October consultation (eight suppliers and their trade association). We thank them for their comments on our proposals and have published non-confidential versions of their representations alongside this decision for Cap period four.[3]

Broadly, most suppliers argued that their expected costs would be, or could be, higher than allowances would provide if we set them using our proposed methodology. Suppliers commented on a series of issues relating to the methodology and consultation process.

In this document we do not provide an issue by issue assessment of suppliers' representations. We will respond on the issues raised as part of any subsequent decision document or additional consultation, as appropriate.

Next steps

We continue to consider suppliers' representations to ensure that the proposed methodology protects customers appropriately, and in doing so we have regard to the other needs set out in the Default Tariff Cap Act 2018.

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[2] It is also possible that the contingency allowance is lower than the efficient costs of an average supplier in Cap period four, in which case we would take that difference into account when setting future allowances.
[3] Ofgem (2019), Reviewing smart metering costs in the default tariff cap: October consultation. https://www.ofgem.gov.uk/publications-and-updates/reviewing-smart-metering-costs-default-tariff-cap-october-consultation

If we conclude that the proposals are appropriate, on the basis of the consultation already conducted, then we may proceed to decision in the New Year.

As set out in the October consultation, if we conclude that we should make significant changes to the proposed methodology (in the light of suppliers' representations or material new developments and data) then we will consult stakeholders on those changes before seeking to implement them.

We will let stakeholders know of our position and the relevant arrangements (if any are required) in the New Year.

Kind regards
Anna Rossington
Deputy Director – Retail price regulation

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PU **Tel** 020 7901 7000
www.ofgem.gov.uk

Appendix: Changes to Annex 5 of SLC28AD

We will make the changes to the SMNCC for Cap period four in the document 'Annex 5 – Methodology for determining the Smart Metering Net Cost Change' referred to in standard condition 28AD of the electricity and gas supply licences.

Within that document, we will make changes to sheet '2a Non pass-through costs', cells K7:R8. The values we will insert are set out in the table below.

Table 5.1: the non-pass-through SMNCC in cap period four (£ per account)

Tariff	Contingency allowance (at TDCV)
Electricity	9.50
Gas	11.77
Implied dual fuel	21.27

Notes:

All values are £/customer, nominal.

Consistent with the first three cap periods, the SMNCC at nil consumption is 69% of the SMNCC at typical domestic consumption value (TDCV).

For the purpose of calculating the variable charge in the Cap, the TDCV is 3,100 KWh for electricity and 12,000 KWh for gas.