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Dear Sir / Madam

We are writing in response to your invitation to comment on a proposed review of the Energy Market Investigation (Prepayment Charges Restriction) Order 2016.

This submission was prepared by Citizens Advice. Citizens Advice has statutory responsibilities to represent the interests of energy consumers in Great Britain. This document is entirely non-confidential and may be published on your website. If you would like to discuss any matter raised in more detail please do not hesitate to get in contact.

You seek feedback on whether:

- The CMA should prioritise the Order for review at this time;
- It is appropriate for the scope of the review to consist of the assessment of (i) the progress made concerning the rollout of smart meters and (ii) the CMA's calculations underlying the initial benchmark figures in two areas (the 'policy cost allowance' and the DCC costs element of the 'indirect cost allowance'); and
- Whether there is evidence that additional cost categories or broader elements of the Order should also be subject to review.

In short, our answers to these three questions are Yes, Yes but we think any review of policy costs should be narrowed to only those areas where there is very clear upfront evidence that actual costs have materially deviated from those projected, and No. We set out our reasons for reaching these views in the following sections.

Whether the CMA should prioritise the Order for review at this time

We agree that it should.

In choosing to introduce a time-limited prepayment meter ('PPM') price cap, the CMA recognised that competition in that segment of the market was particularly weak and that this metering limited the ability of those consumers to shop around for the best deals. These were (and still are) typically only available to those customers who have a conventional credit meter. While consumers could get PPMs replaced by conventional credit meters, they might incur a cost, and would definitely incur inconvenience, in doing so. In consequence, consumers on PPMs were largely frozen out from enjoying the benefits of competition and needed particular protection.

The CMA considered that smart meters, which have the ability to be switched between prepayment and credit modes without the need for asset replacement or consumer inconvenience, could solve that structural problem. For this reason, it excluded SMETS2 meters (and any other interoperable smart prepay meters identified by the CMA) from the PPM price cap. The CMA noted that the government was committed to offering a smart meter to every household in Great Britain by 2020, and therefore considered that a sunset clause on the PPM price cap could be tied to that date. However, it recognised the possibility that smart rollout could progress faster or slower than that timeline, and committed to a review in January 2019[1]:

> *'there is some inherent uncertainty over exactly when the roll-out of smart meters in the domestic retail energy markets will be completed. Accordingly, while we would propose to incorporate a sunset provision into the PPM Price Cap Remedy that is linked to the current forecast of the successful completion of the roll-out of smart meters, we also propose to conduct a focused mid-term review in January 2019 of the progress that has been made concerning the roll-out of smart meters. In the event that the roll-out of smart meters were materially ahead of schedule, we would consider whether to terminate the price cap early (ie an early termination provision would be included).*
>
> *In the event that, at the date of the mid-term review, the roll-out of smart meters does not appear likely to be completed by 31 December 2020, we would consider whether to encourage Ofgem to review the situation and take whatever action it considers appropriate (including whether to introduce a similarly structured price cap in the prepayment segments as from the start of 2021). We believe that this approach is more proportionate than extending the PPM Price Cap Remedy for a further specified period. While this creates some uncertainty about the possibility of a price cap being in place beyond 2020, this uncertainty is narrowed to the issue of the extent of roll-out.'*

We think that the CMA should honour its 2016 commitment to conduct a review in January 2019 for two reasons.

The first is a simple one of general principle: that it is good practice that regulators (and, indeed, other policy-makers) do what they say they will do. If they establish a

[1] Text extracted from paragraphs 14.337 and 14.338 of the Energy Market Investigation Final Report, CMA, June 2016.

pattern of not doing so, it may start to call in to question whether other current or future commitments are 'bankable', damaging both consumer and investor confidence in the regulatory framework.

The second is that there are now clear reasons to believe that a review of the termination date of the PPM cap is merited, even had that earlier commitment to review not been made. This is because there is extremely strong evidence to suggest that the roll-out of smart metering will not be complete by 2020. This calls into question whether a sunset date of 2020 for providing price protection to PPM consumers remains appropriate.

For further evidence of progress towards the 2020 target, we would particularly point the CMA towards the National Audit Office ('NAO')'s recent report, 'Rolling out smart meters.'[2] The NAO was explicit and unambiguous in its view that the roll-out of smart metering will not be complete by 2020, and that 25-30% - perhaps more - of homes and small businesses will not have received a smart meter by that date:

> *'The number of smart meters installed by 2020 will fall materially short of the Department's original ambitions. The Department originally aimed for all consumers to have a smart meter by 2020. Suppliers' licences require them to submit ambitious rollout plans to Ofgem annually, which must either aim for 100% rollout by 2020 or explain why this cannot reasonably be achieved. In the most recent set of plans accepted by Ofgem, energy suppliers have said they will only be able to install smart meters in around 70% to 75% of homes and small businesses by 2020. Suppliers attribute this to limited consumer interest and delays to SMETS2. Actual rollout by 2020 may fall short even of these estimates if the DCC infrastructure encounters further problems or if suppliers encounter further difficulty persuading consumers to accept installations.'*

It therefore appears inevitable that the PPM Order will lapse while millions, perhaps tens of millions, of 'dumb' meters remain on walls. The CMA should therefore consider how to ensure those that are on traditional - or non-interoperable smart - PPMs remain protected after 31 December 2020. This should include considering whether to recommend to Ofgem that it should introduce a replacement cap from the start of 2021, noting that the CMA does not have power to extend its Order.

For the avoidance of doubt, we are unaware of any reason to believe that the specific impediments to engagement and choice that affected PPM consumers at

[2] 'Rolling out smart meters.' National Audit Office, November 2018.

the time of the CMA's market investigation have been resolved by any other market developments or regulatory interventions in the period since the investigation.

Should the scope of the review consist of the assessment of (i) the progress made on the rollout of smart meters and (ii) the CMA's calculations underlying the initial benchmark figures in two areas (the 'policy cost allowance' and the DCC costs element of the 'indirect cost allowance')?

Yes.

In the case of assessing progress in the roll-out of smart meters, for the reasons given above.

The consultation document is ambiguous on whether the CMA intends to review all policy costs, or only those relating to smart meter rollout and the DCC. In our view, there is a stronger case for the latter given that the motivator for this review was always signposted as being tied to smart rollout. We are also mindful that the broader the range of cost categories that are brought into scope, the more complex and time-consuming the review may be. Given that the cap is due to expire in under two years, and that any review now is likely to be necessarily less exhaustive and public than the 2014-16 market investigation itself, we encourage you to keep this review as narrowly focused as possible. Notwithstanding this, we consider that if the CMA has credible evidence that wider policy costs have materially deviated from those that were envisaged when the cap was introduced, it would be reasonable for it to consider reviewing and resetting those wider costs allowances. If this is the case, we encourage you to publish and consult on relevant data early in the process both to facilitate meaningful external challenge and to manage stakeholder expectations.

In conducting its review, we encourage the CMA to be mindful of the work that Ofgem has done in developing its wider price cap methodology and that there may be significant merits in trying to ensure consistency in the approach taken across the two caps.

Whether there is evidence that additional cost categories or broader elements of the Order should also be subject to review.

We are unaware of any evidence to suggest that additional cost categories or broader elements of the Order should be brought into the scope of the review.

The PPM Order is, unsurprisingly, controversial within the sector because of the constraint that it places on affected suppliers revenue streams. It is therefore highly likely that respondents may come forward with a 'bucket list' of things that they would like to change about it, including possibly to re-open the question of whether it should even exist - but very probable that many of these grievances will have been heard before, in the context of the 2014-16 market investigation. This review should not become an opportunity to relitigate or undermine the conclusions of the market investigation.

We are mindful that the Order expires in under two years and that it could not be extended by the CMA - that if there is a need for ongoing price protection beyond that date, that this would be for Ofgem to enact. We are also mindful that Ofgem has (i) recently developed its own price cap methodology for the wider default tariffs cap that may extend beyond 2020 and (ii) has indicated that it considers it likely that some form of enduring price protection for vulnerable consumers may be needed after that cap has ended. Given this context, it may be appropriate that if there are any wider issues with the design of the cap that the CMA seeks to address these through a recommendation to Ofgem rather than attempting its own temporary fix.

I trust that this response is clear, but would be happy to discuss any matter raised within it in more depth if that would be helpful.

Yours sincerely

Richard Hall
Chief Energy Economist