Invitation to Comment:
Energy Prepayment Review
Competition and Markets Authority
Victoria House (6th Floor South East)
37 Southampton Row London
WC1B 4AD

By email to: Remedies.reviews@cma.gov.uk

Dear Sir / Madam

Invitation to Comment: Energy Prepayment Review

First Utility welcomes this opportunity to respond to the CMA's initial consultation on whether, and how, the *Energy Market Investigation (Prepayment Charges Restriction) Order 2016* should be reviewed.

We believe a mid-term review on the Prepayment Meter ("PPM") Cap is urgently needed, given there are now two Caps - one set by the CMA, the other set by Ofgem - sitting alongside each other, constructed differently, with different objectives, and therefore leading to inconsistent and detrimental consumer outcomes.

When the Order was introduced in 2016, the CMA proposed limited price protection based on meter type, in recognition it was harder for PPM customers to switch to market-leading, non-PPM tariffs, than other customers as they physically needed to change their meter type to do so.

The proposed mid-term review under consideration was therefore originally designed to consider the rollout of SMETS2 meters in prepay mode given these were seen as a solution to the engagement barrier of changing meters.

Subsequently, however, 2018 Government legislation has introduced a Default Tariff Cap protecting prices for all customers on default rates, including the SMETS2 meters in prepay mode which were exempt from the original CMA Order.

This mid-term review must therefore serve a different purpose to which the CMA originally intended, above all considering

1. Whether the PPM Cap can be set more accurately, given the updated information provided to Ofgem when setting the Default Tariff Cap. In particular:

a. **The PPM Cap should consider the full range of wholesale costs now identified by Ofgem**, including but not limited to forecasting, shaping and Unidentified Gas. It should also follow the more accurate summer / winter weighting of the Default Tariff Cap

b. **The PPM Cap should account for smart costs accurately, using the index agreed by Ofgem under the Default Tariff Cap.** It currently indexes smart costs using inflation (as part of operating costs), whereas the Default Tariff Cap treats as a "pass-through" industry costs such as DCC, Alt-Han, SEGB etc to be passed-through, and proposes a separate "Smart Meter Net Cost Change" index for all other smart costs.

c. **The PPM Cap should use scheme administrator data and charging statements to account for policy coss, rather than Office for Budget Responsibility estimates,** which are backward rather than forward looking, and sometimes substantially so. OBR data is only updated twice a year in March and November. This means a Price Cap set for 1 April, announced in mid-Feb, will use November's view rather than March's.

Although the current PPM and Default Tariff caps are close in price at typical consumption values, the difference set out above means that, from 1 April, the two caps are likely to become divorced in price, with the PPM cap lower, despite both Ofgem and the CMA acknowledging that PPM customers cost more to serve.

This leads to the second priority for any CMA review;

2. The CMA should expressly consider the customer detriment of two PPM caps sitting alongside each other on an inconsistent basis

Under the current regulatory regime, PPM and PPM SMETS1 customers will be capped at the level set by the CMA Order's methodology, with PPM SMETS2 customers capped at another level, that set by Ofgem's Default Tariff Cap model instead.

Given the differential treatment of wholesale, smart and policy costs in the two models, there is a real risk that the Default Tariff Cap will be higher than the PPM Cap from 1 April.

This means that customers moving from PPM or PPM SMETS1 meters to SMETS2 meters will face higher bills, a detrimental outcome to consumers which will make it harder to roll out these meters to the very customers who could benefit the most.

Indeed, the current situation is the very reverse of the objective set by the CMA's PPM Cap in 2016: to support customers move onto SMETS2 meters.

We believe an easy solution exists to both the inaccurate treatment of costs and the detrimental effect of two caps running alongside each other set on a differential basis: wrapping both Caps into one. The CMA could remove the PPM Order, with Ofgem at the same time extending the Default Tariff Cap to PPM customers. This should contain an appropriate payment uplift given the higher Cost to Serve.

Such action should be an early priority for the CMA and Ofgem, given the need to

- Support the SMETS2 rollout
- Simplify the customer experience, with one clear price protection regime
- Ensure suppliers can recover all costs accurately

Yours Faithfully
Natasha Hobday
Group Director of Policy and Regulation