

Smart meter targets framework: years 3 and 4

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| Lead department | Department for Energy Security and Net Zero |
| Summary of proposal | To set targets and tolerance values for energy suppliers for the final two years (2024 and 2025) of the four-year smart meter framework introduced in 2022. |
| Submission type | Impact assessment (IA) – 11 May 2023 |
| Legislation type | Secondary legislation |
| Implementation date | 1 January 2024 |
| Policy stage | Final |
| RPC reference | RPC-DESNZ-5261(2) |
| Opinion type | Formal |
| Date of issue | 21 June 2023 |

RPC opinion

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| Rating¹ | RPC opinion |
| Fit for purpose | The RPC considers the EANDCB and SaMBA to be sufficient. There are some areas of the IA for improvement, particularly around the assessment of wider impacts, such as innovation. |

Business impact target assessment

| | Department assessment | RPC validated |
|---|------------------------------|---|
| Classification | Qualifying provision | Qualifying provision (IN) |
| Equivalent annual net direct cost to business (EANDCB) | £35.2 million | £35.2 million (2019 prices, 2020 pv) |
| Business impact target (BIT) score | £176.0 million | £176.0 million |
| Business net present value | £181 million | |
| Overall net present value | £1,301 million | |

¹ The RPC opinion rating is based only on the robustness of the EANDCB and quality of the SaMBA, as set out in the [Better Regulation Framework](#). RPC ratings are fit for purpose or not fit for purpose.

RPC summary

| Category | Quality | RPC comments |
|---|---------------------|--|
| EANDCB | Green | The IA's direct/indirect treatment of different categories of benefits to energy suppliers is in line with the IA for the first two years of the new smart meter policy framework. |
| Small and micro business assessment (SaMBA) | Green | The IA includes information on the number of small and micro businesses affected and discusses exemption, disproportionality and mitigation. The IA addresses medium-sized business considerations. |
| Rationale and options | Satisfactory | The IA summarises the rationale for intervention and describes the preferred option in detail, but would benefit from providing more information on other options considered and why they were rejected. |
| Cost-benefit analysis | Good | The Department has provided a highly-monetised assessment of societal impacts. The IA would benefit from greater discussion of risks and consumer behaviour, or from providing clearer references to where further information is available in the Department's cost-benefit analysis. |
| Wider impacts | Weak | The IA monetises environmental impacts but would benefit from discussing innovation, competition and consumer impacts in more detail. |
| Monitoring and evaluation plan | Good | The IA usefully discusses the range of data and evidence that will be collected to monitor and evaluate uptake and performance against targets. The IA would benefit from discussing further how the M&E will feed into future decisions on the overarching policy. |

Summary of proposal

The proposal sets annual targets and tolerance values for energy suppliers for smart meter installation for 2024 and 2025; the third and fourth years of the new smart meter policy framework that started on 1 January 2022.

The Department estimates a net present value (NPV) of £1,301 million, a business NPV of £181 million and an EANDCB of £35.2 million. Costs are incurred by energy suppliers for (a) purchasing metering assets (smart meters, in-home displays, and communications hubs) and (b) installing meters. Business users of smart meters will benefit indirectly from energy savings, and energy suppliers will benefit, for example, from avoided site visits, reduced customer service enquiries and lower costs to serve pre-payment customers.

EANDCB

Direct/indirect classification

The Department has classified the benefits to business into direct and indirect in line with the impact assessment for the first two years (2022 and 2023) of the new smart meter policy framework. This classification was agreed with the RPC in its scrutiny of that measure.² This involved re-classifying a number of benefits to energy suppliers, such as improved debt handling and network benefits, on the basis that these benefits rely upon customers and suppliers acting on information provided by smart meters. Other benefits, such as lower costs to serve pre-payment customers and streamlined change of tariff processes, were accepted as direct on the basis that they did not depend on customers changing their behaviour in response to having a smart meter installed. The IA's BIT section would benefit from setting out explicitly which benefits are treated as direct or indirect and the reasoning behind the classifications, drawing upon RPC guidance as appropriate.³

Assumptions

The IA would be improved by providing further explanation of the assumptions underpinning installation costs to business, in particular how the two hours per installation estimate was calculated.

Counterfactual/baseline

The IA notes that there has been a change in the approach to the counterfactual since the consultation stage IA (paragraph 32, pages 10-11). The change involves factoring in real-world data on underperformance in installation in the first year of the new framework (2022) in the assumed profile of installations in 2023. It appears that

² RPC opinion: RPC-BEIS-5035(2) 'Smart meter policy framework post-2020', 3 June 2021.

³ <https://www.gov.uk/government/publications/rpc-case-histories-direct-and-indirect-impacts-march-2019>

this means assumed installations are lower than previously assumed in 2023Q1 and Q2 but with a ‘catch-up’ in Q3 and Q4. The IA could, however, be clearer on this point, including on assumed levels of compliance by business in both the counterfactual and policy scenarios. The IA would also benefit from discussing further the realism of the assumed profile of installations, given the historical downward revisions to thresholds and extended timeframes in the smart meter rollout.

Comparison to direct business impact estimates in final stage IA for years 1 and 2 and consultation stage IA for years 3 and 4

The estimates of direct costs and benefits to business are lower than those in both the final stage IA on years 1 and 2 and the consultation stage IA for the present proposal. The reductions in costs and benefits are of a broadly similar magnitude, so that the EANDCB is similar to previous estimates. However, the IA would benefit from discussing the factors behind these changes, in particular how information and data collected during consultation have refined the estimates at table 2 (page 18) of the IA.

SaMBA

The SaMBA is sufficient. The IA notes that each energy supplier’s targets and minimum installation requirements will continue to be set as a proportion of its overall consumer base, to ensure that the task facing each supplier will be commensurate to its size. The IA explains why the Department has not been able to obtain information on energy suppliers by the number of employees, and includes an analysis by turnover. This analysis indicates that 17 out of 57 energy suppliers covered by the smart meter obligation are small businesses. Although around nine of these businesses were “behind” on their rollout of smart meter at the end of 2022, the IA explains that financing arrangements enable deployment costs to be spread over the lifetime of a metering asset, mitigating any disproportionate burdens. The IA also notes that these smaller businesses will be able to use newer, lower-cost technology than was available for past installations, and benefit from technical issues having been resolved as a result of industry collaboration. The IA would benefit from discussing disproportionality further in the context of other current or recent pressures on smaller suppliers, such as high wholesale energy prices and associated exit of a number of suppliers from the market.

Medium-sized business considerations

Based upon its turnover analysis, the IA estimates that six suppliers could be considered to be medium-sized businesses (MSB). As with small businesses, the IA addresses the issue of MSB exemption satisfactorily.

Rationale and options

As noted above, the proposal relates to the third and fourth years of a newly-implemented smart meter policy framework. In view of this, the IA provides relatively limited coverage of the rationale for intervention and options considered. This is sufficient, although the IA could signpost more clearly where further information may be found. For example, on rationale, this could be the relevant sections of the 2019 Smart Meter Roll Out: cost-benefit analysis. The Department consulted on proposed options for a new policy framework in September 2019 and states that the Government's response to the consultation in June 2020 confirmed the policy approach, having considered different options. The Department has also reviewed, and consulted on, its proposals for the final two years of the current framework. The IA sets out the preferred option in some detail (pages 6-7) and helpfully discusses alternative approaches that were considered (pages 7-8). The IA would benefit from providing a summary table of the alternative options or approaches that were considered for, and more recently within, the new smart meter policy framework.

The IA would also benefit from discussing whether measures that could, potentially, deliver additional consumer benefits, such as smart pricing or automatic switching, might also help improve customer uptake, and considering whether implementing those measures could be achieved through modifications to the preferred option and/or complementary regulation. The IA could also benefit from discussing other potential measures to assist achievement of targets, such as requiring new homes to have smart meters installed as a default and measures that could assist with take-up in remote and hard-to-reach areas (including high-rise flats).

Cost-benefit analysis

The Department has provided a highly-monetised assessment of societal impacts. The IA sets out the evidence, data and modelling used (in particular at pages 11-14), which are in line with that used in previous assessments. There are areas, however, where the assessment could be strengthened.

Assumptions, assessment of risk and sensitivity analysis

The IA includes a sensitivity analysis and discussion of factors affecting smart meter rollout but would benefit from an explicit section on risks. The IA discusses briefly the issue of installer resource (paragraph 90) but would benefit from discussing consultation responses on the potential impact of skills shortages, following the pandemic and associated reduction in labour market participation, on the achievability of the rollout. Given the references to problems expressed by suppliers relating to the number of installers, the IA could also discuss cost and quality of service risk associated with training, retaining and deploying installers across longer

distances around the country, including potential negative impacts on consumer experiences.

Impact of the energy cost of living crisis

The IA would benefit from discussing how the recent, very large, increase in energy prices might affect the analysis, such as public attitudes to smart meters. This could include the recent measures incentivising consumers not to use energy during peak periods, touched upon in the IA under 'wider impacts'. The IA would also benefit from discussing the impact on consumers with prepayment meters who are less likely to take up smart meters, the cost to energy suppliers of maintaining a traditional meter network on a smaller customer base and the impact on vulnerable consumers of any resultant increase in tariff.

Links to the 2019 overarching smart metering CBA

The IA notes that the 2019 overarching smart metering cost-benefit analysis (CBA) forms the basis for the modelling underpinning this, and previous, smart meter impact assessments. The IA refers to this CBA in places, for example in explaining that the eleven-year appraisal period used in the IA aligns to this analysis (paragraph 47, page 16). The IA would benefit more generally from further explanation and linkages to the 2019 CBA, including why the CBA modelling continues to provide a robust underpinning to the smart meter IAs. This could include discussing the on-going validity of some assumptions (given the lower-than-expected number of installations), such as around number of available installers and estimates of consumer savings.

Comparison to estimates in final stage IA on years 1 and 2 and consultation stage IA for years 3 and 4

Estimates of indirect business benefits, consumer and environmental benefits are lower than at the consultation stage, although the latter are higher than estimated in the final stage IA for years 1 and 2. In line with the comment above on comparison of direct business impact estimates, the IA would benefit from discussing how these estimates of wider impacts have changed since the previous two IAs.

Presentation

Although not affecting the EANDCB figure, the Department should check the figures provided for customer benefits in table 2 (page 18) of the IA as they differ from those in the EANDCB calculator.

Wider impacts

The IA monetises carbon and air quality benefits and provides a reasonable discussion around equalities impacts. The latter would be improved by addressing regional disparities, noting the lower take-up in ‘hard-to-reach’ areas and London. The IA would benefit from proportionately discussing *innovation, competition* and *trade* impacts. This should include discussing further the role of the proposal regarding “stimulate innovation” (paragraph 73, page 24). This could link to incentives around innovation in the context of additional costs in supplying hard-to-reach areas, including high-rises as well as geographically remote areas. The IA could also discuss the dependency of innovation on suppliers having sufficient capital to invest, linking to the pressures around wholesale price increases noted above.

The IA states that smart meter rollout enables *energy system flexibility* by reducing the amount of generation and network needed to meet peak demand and that this is forecast to reduce system costs by up to £10 billion a year by 2050 (page 3). The IA also states that these benefits have not been monetised in this assessment (page 2). The IA would benefit from briefly describing at how the £10 billion figure was arrived, or where such details can be found (such as the location in the document at the footnote reference).

The IA would benefit from addressing the points for improvement in the 3 June 2021 RPC opinion on the IA for the first two years of the framework, or explaining why these are no longer applicable. These points include, in relation to *consumer impacts*:

- discussing evidence on consumer confidence in smart meters and information on awareness or information campaigns, and who will bear the costs; and
- discussing benefits from sharing information, in particular the possibility of making customers’ detailed utilisation available to rival suppliers and its associated potential consumer-switching benefits and risks.

The IA refers to analysis indicating sufficient consumer demand and installer resource to enable suppliers to meet their targets (paragraph 90, pages 27-28) but would benefit from providing more details of this, in particular given concerns around skill shortages post-pandemic.

A very recent report by the National Audit Office set out key findings on the smart meter rollout, drawing upon surveys by Smart Energy GB, consultation responses and other data.⁴ The IA would benefit from being updated to reference this report

⁴ <https://www.nao.org.uk/reports/update-on-the-rollout-of-smart-meters/>. Published 14 June 2023.

and discussing any factors relevant to the analysis. These could include the need for more up-to-date data on consumer savings, greater data reporting on costs of the rollout and consideration of the financial stability of suppliers on system benefits.

Monitoring and evaluation plan

The IA includes a useful reporting and monitoring section. This refers to the smart meter rollout having an established programme of monitoring and evaluation, delivered by the programme's Benefits Realisation team. There is a short summary of how this informed the review of performance against year 1 targets and fed into the proposed targets for years 3 and 4. Most usefully, the plan discusses the range of data and evidence that will be collected to monitor and evaluate uptake and performance against targets. The IA could usefully provide more details of the review of the first years of the new framework and (as noted above) the support for the conclusions presented at paragraph 90, pages 27-28. The M&E plan could usefully highlight how the installation data to date will help inform future decisions of the overarching policy driving the targets and evaluate the balance of costs and benefits over time.

Regulatory Policy Committee

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