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Dear Dan

Future of Domestic Price Protection - Discussion Paper

EDF is the UK's largest producer of low carbon electricity. EDF operates low carbon nuclear power stations and is building the first of a new generation of nuclear plants. EDF also has a large and growing portfolio of renewables, including onshore and offshore wind and solar generation, as well as energy storage. With over five and a half million electricity and gas customer accounts, including residential and business users, EDF aims to help Britain achieve net zero by building a smarter energy future that will support delivery of net zero carbon emissions, including through digital innovations and new customer offerings that encourage the transition to low carbon electric transport and heating.

Given the impending implementation of Market-wide Half Hourly Settlement (MHHS) and an expectation that the retail market will become more diverse in the future, it is welcome that Ofgem is starting discussions around the role of price protection in a more dynamic retail market.

Retail Market Design

It is essential that individual topics such as the future of domestic price protection are not considered in isolation, but rather within the context of the wider objectives and working of the retail market and energy system. To do otherwise, risks creating conflicting and overly complex interventions which then have unintended consequences for customers and the development of the wider market.

We need the right regulation and infrastructure in place to support a healthy, well-functioning and resilient retail energy market which can deliver great service for customers, protect those most in need, provide fair value and support our Net Zero future. This must allow suppliers to make sustainable, fair returns and provide the right conditions for suppliers to reinvest in the market to the benefit of consumers.

We must also ensure we learn the lessons from our recent past and do not repeat mistakes such as encouraging entry and competition based on unsustainable business models or

excessively focusing on single metrics or measures of success (e.g., switching levels between suppliers). Market events since the introduction of the cap, including significant supplier failures, have, for example, demonstrated Ofgem's previous approach of promoting an open and competitive retail market through low barriers of entry together with a significant focus on customer switching did not deliver beneficial consumer outcomes. Key to achieving this will be ensuring that policy and regulation is delivered agilely so that it can evolve to react to different external pressures and developments. Rigid, overly complex regulatory solutions cannot achieve this.

Smart metering

Taking the above into account, maximising the benefits of Market-wide Half Hourly Settlement (MHHS) ultimately relies upon a smart and flexible energy system, for which a successful smart meter rollout is a prerequisite.

The smart meter rollout has already achieved a great deal, and EDF continues to strive to meet the ambitious targets. Especially during an energy and cost of living crisis millions of customers have benefitted from smart meters, enabling them to understand, control and reduce their energy consumption.

However, Ofgem must now work with Government to review and update the regulatory framework for the installation of smart meters. It is clear that the current framework, based on installing as many new meters as possible, is not driving the best outcomes for customers. At this stage of the programme, we are concerned that continuing with the current target-based rollout framework, which requires suppliers to continue to attempt to install meters in premises where customers don't want them, or where the potential benefits of smart in terms of behaviour change are unlikely to be realised, risks undermining the value of smart metering to both GB and individual customers. The next phase of the programme should instead focus on two priorities, enabling engaged customers to make the most of their smart meter, and helping disengaged customers appreciate the value having smart meters could bring.

Future Price Protection

EDF welcomes Ofgem's discussion paper and the start of the conversation on how price protection may evolve in future.

EDF recognises that the Default Tariff Cap (DTC) has brought benefits to consumers by providing confidence that they are being charged fair prices and offering a simple framework which allowed government support to reduce consumers prices during the energy crises. However, evidence shows that the design of the current DTC, despite recent positive changes, has overall led to unreasonable and unmanageable risks for suppliers, which in turn damaged the stability of the retail market, increased costs for consumers, and continues to risk undermining the progress that is required to reach Net Zero.

We also note and agree with Ofgem's initial assessment that the continuation of a universal, flat and stringent price cap is not fit for purpose in an evolving retail market. A large number of customers already benefit from static TOU tariffs (such as Economy 7) to support the use of storage heaters for example. As MHHS is implemented there will be a growth in the use of static TOU tariffs which will also be incentivised by electricity becoming a larger proportion of householders' costs through the electrification of heat and transport. Therefore, it is essential that work on price protection progresses in a timely manner to ensure it does not act as a barrier to evolving the sector and allowing for innovation in product and service offerings.

However, as a precursor to the discussion on the potential benefits of each of the options, there is a need to reassess, determine and communicate a clear set of priorities and objectives of any future price protection arrangements. Only by being clear on what issues price regulation is trying to mitigate and what market outcomes are being targeted can Ofgem and Government determine what mechanism(s) are needed. The current DTC is, for example, flat, universal and stringent, because of the objectives set for it by Government ahead of its introduction. To understand to what extent each of these categories remains important depends on what the forward-looking objectives are.

We note that the current DTC was implemented initially on the expectation that it would be a temporary intervention which could be extended annually up to the end of 2023. The retail market today, and how it is expected to transition in the future, is not the same as it was at the time the legislation for the DTC was introduced. Given this, any consideration of the future role of price protection should not be constrained by the existing objectives or the matters that Ofgem must have regard to (as set out in the Default Tariff Cap Act 2018).

With this in mind, in considering the future of the price protection and the options set out in the paper, the following objectives, and topics must be considered and balanced to help determine the extent to which future price protection mechanisms need to be flat, universal, or stringent. Where appropriate we have also sought to include our top-level views of the options being considered by Ofgem:

Affordability

Despite how it is often perceived and wrongly presented, the affordability of energy has never been an objective for the DTC. It is also a challenge that all the options presented in the Ofgem paper are fundamentally ill-suited to address. Affordability is best dealt with as a matter for social policy that requires action from Government to introduce meaningful changes that can effectively better support households with their energy needs.

The best way to support such customers is via a targeted social tariff, or similar targeted support. It is vital Government urgently follows through on its previous commitment to introduce a meaningful social tariff, which we continue to consider would ideally be government funded rather than by other energy consumers.

Therefore, Ofgem must continue to make the case to Government for such a targeted intervention to support customers who cannot afford to pay their energy bills.

Importantly, however, there is a need to ensure that any interventions to support vulnerable customers do not result in such consumers being excluded from accessing the benefits which can be achieved by engaging with the market, including smarter tariff options, where these are appropriate for their needs. This should be a key consideration when developing any additional support for vulnerable customers.

Engagement and loyalty

Perhaps the primary objective of the current DTC was to address stakeholders' concerns around disengaged customers being charged more than engaged or new customers (often referred to as the 'loyalty penalty'). Whilst the current cap has contributed to mitigating this risk, the Ban on Acquisition only Tariffs (BAT) is the simplest approach to ensuring suppliers current customers can benefit from the same tariff choices as new customers.

Both the market basket cap and the supplier relative cap are aimed at limiting default tariff prices based on comparisons to either average tariffs in the competitive market or to each individual supplier's cheapest tariffs. However, both, particularly as means of addressing any loyalty penalty, would be very complex to implement and open to gaming, especially in a future retail market (e.g. MHHS). In addition, all they would achieve is limiting the variance between what new and existing customers pay, rather than ensuring all are able to benefit from the same range of choices. For these reasons, as we explore further in our detailed responses, the relative cap options do NOT merit further investigation at this stage.

Conversely, we note that a BAT, as an enduring feature of the market, offers the simplest option to mitigate the key risks of loyalty penalties. EDF consider a BAT is an essential protection for loyal customers, even with the current DTC. In the absence of BAT these customers, who currently make up a majority of the market, could be forced to switch supplier if they want to access the cheapest deals. Retaining the BAT as an enduring feature of the energy supply market, as has been done in the insurance market, ensures that suppliers are encouraged to focus on supporting all of their customers, including their existing customer base, by for example investing in high customer service levels and innovative offerings.

A further advantage of the BAT is that it would mitigate the risk of the reintroduction of unsustainable and irresponsible business models and pricing practices and, ultimately, unnecessary instability into the market. As the history of this market demonstrates, this presents real risks to end consumers who will ultimately be asked to foot the costs of a destabilised market.

Efficiency

A key focus for EDF is ever increased efficiency in how we deliver support and products to customers. This has always been a concerted area of focus for us and we are proud of the progress we have made. However, drives for greater efficiency must not be at the expense of services that customers expect and deserve, such as would be achieved through reducing customer service levels by for example reducing contact centre opening times.

Ofgem has described the current DTC as stringent because it is calculated using a bottom-up approach based on a notional efficient supplier. This design was primary as a result of concerns at the time around supplier efficiencies and its impact on the costs consumers faced.

Ofgem must, however, recognise that the market has evolved since the DTC was established and this must be considered in any revised approach to price protection. It is not clear that there is a need for regulatory interventions to drive efficiency over and above that which the market and competition brings.

In particular, Ofgem must be mindful of the risks of continuously incentivising cost reductions from suppliers that put at risk ensuring that high levels of customer service and Net Zero innovation are also brought forward. Any options that overly focus on driving down costs, for example by constantly favouring a lower quartile cost benchmark in different areas, will make it challenging for suppliers to deliver the improvements in levels of customer service standards that customers expect, and which suppliers want to be able to deliver. It is welcome that Ofgem itself recognised in a recent workshop that differences in cost to serve between suppliers can be attributed to differences in customer bases and business models rather than efficiency levels per se.

It is vital that any future price protection provides sufficient financial scope to allow all efficient and resilient suppliers, including small suppliers and those with innovative business models, to stay solvent, deliver high quality customer service and innovation for Net Zero. On this basis, in the absence of more significant broader price protection reform, Ofgem should move away from using lower quartile approaches in the current DTC and instead adopt average benchmark approaches. Ofgem has already adopted such an approach under the price cap for other allowances such as smart metering, COVID-19 and additional support credit (ASC) bad debt costs. This would allow suppliers to have greater freedom to differentiate how they serve and create value for customers, leading to more choice, innovation and an active market.

Net Zero, Time of Use and Flexibility

While not really considered at the time of the caps introduction, given Ofgem's evolving duties, a key objective of price regulation and energy policy more widely should also be to support customer engagement with energy suppliers who can provide support and help achieve ambitious net zero pathways through tailored products and services. In considering how to increase engagement Ofgem should consider whether a universal cap is acting as a barrier to this, given that universal protection reduces the incentive for customers, who would otherwise be able and would benefit from, engaging with the market. Universal protection therefore acts as a barrier to engagement as such customers are aware that they will receive a 'fair price' even where they do not actively engage.

We expect, for example, as MHHS is fully implemented, suppliers will deploy more innovative tariff structures, including time of use options, in response to customer demand and to access commercial opportunities. This would allow price protection to be focussed on those who cannot engage rather than act as a barrier to engagement for those that can.

The significant proportion of benefits from MHHS, in terms of the domestic market, will be realised with static time of use tariffs. While dynamic pricing may become more prevalent via innovative tariff offerings as the market develops, the benefits of encouraging greater flexibility in the time of electricity usage may also be delivered via alternate means to the tariff offering, such as reward schemes. It is, therefore, important Ofgem ensure that in any future approach that innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

Given the above, we do not currently believe the time is correct to consider dynamic ToU based approaches to price regulation. The benefits of dynamic ToU tariffs will only be achieved with the active engagement and behaviours by consumers. Such tariffs are best left to the market to innovate and deliver value to engaged consumers. Such tariffs only present a very small share of the market currently, and this is not expected to change quickly, therefore the key risk is that regulation acts as a barrier to customer adoption.

Fair Returns

Finally, EDF remains committed to working constructively with Ofgem to develop and introduce measures that promote a healthy, well-functioning market that allows efficient and sustainable businesses to attain a fair margin and enable continued innovation and investment to the benefit of consumers. We recognise that it is vitally important for the long-term reputation of the market that profits are fair. Equally important is that the design of any ongoing form of price protection should not act as

a barrier to profit, but rather create the right conditions for suppliers to reinvest in the market as part of the transition to net zero and in the long-term interests of consumers.

If there are, however, remaining concerns around the levels of profits being made in the sector, the options described by Ofgem as 'Margin caps' may be appropriate for further consideration. However, careful consideration is needed to ensure that such a form of financial regulation can encourage greater levels of investment in service levels and net zero solutions (e.g. the need to also establish a 'reinvestment mandate'). Furthermore, it would also be essential to ensure that retail suppliers can make fair returns, even where there are systematic issues which impact costs, for example, at times of prices escalation due to external factors.

In summary, given the above, a continuation of a universal, flat and stringent approach to price regulation is neither possible nor desirable for an evolving retail market. An overhaul of the approach is needed to ensure that customers are supported through increased competition in a market which supports a variety of business models and suppliers are investable by making a fair margin.

Meeting these priorities will, however, involve a balancing act as there are intrinsic tensions between competing objectives. We are currently minded that the most sensible approach to future price protection will in fact be a combination of solutions, addressing different issues and delivering different objectives, in a manner no single solution is likely to be able to do simply without unintended consequences.

The Current Cap

It must also be recognised that even if change is brought forward this will take some time. We, therefore, urge Ofgem to also continue its activity to update and improve the current methodology of the DTC and making it work more effectively for customers and suppliers. We set out our detailed views on how this can be achieved in our responses to the questions. However key areas include moving away from lower quartile cost efficiency, greater use of pass-through mechanisms for industry costs outside of suppliers' control, more flexibility to develop varying static TOU tariffs and a review of smart cost placement and recovery and incentives to further drive the rollout given the current challenges.

We also call on Ofgem to make timely progress on the development of an enduring solution to the recovery of debt-related costs that better protect the interests of both suppliers and all customers. Continuing to use the price cap as a means for suppliers to recover their efficient bad debt costs is flawed as it risks distorting competition and creating 'uneconomic to serve' customers (as Ofgem recognised at a recent industry workshop). EDF has previously called for consideration of a levy approach to address two key moral hazards i.e., customers moving to fixed tariffs and avoiding costs, or suppliers unable to fully recover costs through customers moving to other suppliers. The introduction of such a levy could simplify any price

protection needed moving forward (as would be separate to this and cover all customers) and could be designed in a way that still incentivised suppliers to minimise debt levels.

Our detailed responses are set out in the attachment to this letter. Should you wish to discuss any of the issues raised in our response or have any queries, please contact Steven Eyre, or myself.

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

Yours sincerely



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Attachment

Future of Domestic Price Protection - Discussion Paper EDF's response to your questions

Q1. Do you have any reflections on our list of the cap's successes and challenges?

EDF recognises that the Default Tariff Cap (DTC) has brought benefits to consumers by providing confidence that they are being charged fair prices and offering a simple framework which allowed government support to reduce consumers prices during the energy crises. However, evidence shows that the design of the current DTC, despite recent positive changes, has overall led to unreasonable and unmanageable risks for suppliers, which in turn damaged the stability of the retail market, increased costs for consumers, and continues to risk undermining the progress that is required to reach Net Zero.

The DTC flaws were clearly exposed through the pandemic and subsequent energy crisis, which resulted in many complex, difficult and hurriedly introduced amendments to the methodology being made in order to address where the cap materially diverged from suppliers' efficient costs. Constant changes to the cap and cost recovery uncertainties damage the stability of the market and are not in the best interests of consumers or suppliers. It is important that we learn from this and work towards overhauling the current approach to price regulation to replace it with one that ensures suppliers are investable by making a fair margin, whilst supporting customers through increased competition in a market which supports a variety of business models.

Q2. Do you believe that the growing diversity of electricity consumption patterns will make it challenging to retain a flat, universal and stringent price cap? How quickly do you think this will materialise and with what impacts? What evidence can you provide to support your view?

We do not currently believe the time is correct to consider dynamic ToU based approaches to price regulation. The benefits of dynamic ToU tariffs will only be achieved with the active engagement and behaviours by consumers. Such tariffs are best left to the market to innovate and deliver value to engaged consumers. Such tariffs only present a very small share of the market currently, and this is not expected to change quickly, therefore the key risk is that regulation acts as a barrier to customer adoption.

It must be recognised that it is difficult to accurately predict how the market will evolve and how, and in what timeframe, consumers will become more actively engaged in responding to price signals and varying their consumption patterns. It is therefore important that Ofgem does not attempt to prejudge what will happen and set price protection measures for that expected outcome. Ofgem should ensure that in any future price protection approach innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can

be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

However, maintaining a flat, universal and stringent price cap is unlikely to meet the needs of all consumers in an evolving retail market. Furthermore, retention of the DTC in its current form is likely to result in picking winners from both suppliers and customers. This would be contrary to broader energy policy which is focussed on supporting the development of services and products which suit individual customers own characteristics and preferences. The DTC requires reform to reflect the changing market, and adequately support fairness for domestic customers on default tariffs as a greater proportion of customers move to static TOU tariffs.

As MHHS is fully implemented, suppliers will deploy more innovative tariff structures, including time of use options, to support commercial opportunities and in response to customer demand. A significant proportion of benefits from MHHS, in terms of the domestic market, will be realised with static time of use tariffs. While it should be acknowledged that dynamic pricing may become more prevalent via innovative tariff offerings as the market develops, we note the benefits of encouraging greater flexibility in the time of electricity usage may also be delivered via alternate means to the tariff offering. It is, therefore, important Ofgem ensure that in any future approach innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

Q3. What plans do suppliers have to launch ToU tariffs and to incentivise customers to shift their electricity consumption once MHHS is implemented?

Suppliers are already planning for MHHS and also undertaking small scale trials through elective HHS. On this basis it is important that Ofgem ensure that there are no regulatory barriers to innovation in this space.

We expect that the significant proportion of benefits from MHHS, in terms of the domestic market, will be realised with static time of use tariffs. While it should be acknowledged that dynamic pricing will become more prevalent via innovative tariff offerings as the market develops, we note the benefits of encouraging greater flexibility in the time of electricity usage may also well be delivered via alternate means to the tariff offering. For example, flexible offerings could support rebates or other types of rewards. It is, therefore, important Ofgem ensure innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

Q4. How quickly and at what scale do you expect customers, especially those with large flexible loads such as EV and solar / battery users, to take up ToU tariffs once MHHS is implemented?

We expect as MHHS is fully implemented, suppliers will deploy more innovative tariff structures, including time of use options, to support commercial opportunities and in response to customer demand. We note that as the smart meter rollout continues, more consumers, electric vehicle drivers or otherwise, will have smart meters installed at their property. We would welcome Ofgem having a greater focus on increasing demand on the installation of working smart meters for those who want them. For example, by ensuring price regulated smart offerings are the best on offer in the market.

However, it should be recognised that much of the benefit of adopting smarter use of electricity by customers may be delivered not solely via the tariff structure but rather via additional offerings. For example, digital offerings such as interactive mobile phone applications that could support rebates, or other reward mechanisms. Such incentives will be more effective at engaging those customers with the greatest opportunity, e.g. those with electricity heat or transport products, who will most gain from engaging with the market. Maximising this level of engagement will be more impactful than the price regulation outlined in this document for such customers.

Q5. In addition to the factors set out in this chapter, are there any other important changes that might affect the ability of the current default tariff cap to achieve its objectives?

Evidence shows that the design of the current DTC, despite recent positive changes, has overall led to unreasonable and unmanageable risks for suppliers, which in turn damaged the stability of the retail market, increased costs for consumers, and continues to risk undermining the progress that is required to reach Net Zero.

These flaws were clearly exposed through the pandemic and subsequent energy crisis, which resulted in many complex, difficult and timely amendments to the methodology being made in order to address where the cap materially diverged from supplier's efficient costs. Many of these changes have resulted in either a delay or failure in cost recovery, the risks of this continuing will increase as the market 'reopens' and customers move off the DTC.

Ofgem must work to continue to improve the DTC for as long as it remains in place. However, it must carefully prioritise those areas of reform which will have the greatest beneficial impact and can be carried out in a timely manner. We have recently submitted a response to Ofgem regarding its proposed price cap programme of work where we have highlighted the key work areas that Ofgem should undertake, including on operating cost and wholesale reviews and CfD allowance.

Key is to prioritise making the current price cap more stable and resilient to wider system shocks. On this basis, we would recommend the following are duly considered:

- Move methodology away from 'most efficient' costs to 'fair costs' to prevent excessive charging. A methodology focussed on average supplier costs rather than lowest quartile, including the current operating costs review.
- The design of notional supplier should be updated to ensure it better reflects actual market conditions e.g., takes account of fixed offerings too.
- Headroom should be amended to cover a greater range of scenarios.
- Move to a true back stop tariff i.e. only available to disengaged (no product choice for 3 years or the like).
- The introduction of a Debt Levy to ensure the costs associated with bad debt can be recovered fairly from all customers (whether on price regulated tariffs or not) whilst retaining an incentive for suppliers to minimise debt levels.
- In the absence of wider reform, the methodology must be updated to work with broader market reform such as MHHS and REMA.
- Above is supported by Ban on Acquisition-Only Tariffs (BAT) being made permanent and strongly enforced by Ofgem.

Q6. Do you agree that we need to retain some form of price protection in the retail market?

We acknowledge that some form of price protection measures is likely to be needed to ensure that disengaged consumers are suitably protected. However, as a precursor to the discussion on the form and scope of these, there is a need to reassess, determine and clearly communicate a clear set of priorities and objectives. Only by being clear on what issues price regulation is trying to mitigate and what market outcomes are being targeted can Ofgem and Government determine what price protection mechanism(s) are needed. The current DTC is, for example, flat, universal and stringent, because of the objectives set for it by Government. To now understand to what extent each of these categories remains important depends on what the forward-looking objectives are.

We note that the current DTC was implemented initially on the expectation that it would be a temporary intervention which could be extended annually up to the end of 2023. The retail market today, and how it is expected to transition in the future, is not the same as it was at the time the legislation for the DTC was introduced. Given this, any consideration of the future role of price protection should not be constrained by the existing objectives or the matters that Ofgem must have regard to (as set out in the Default Tariff Cap Act 2018).

There is a clear need to ensure that any policy and regulation is delivered agilely so that it can evolve to react to different external pressures and developments. Rigid, overly complex regulatory solutions cannot achieve this. We recognise that there may be tensions between varying objectives at any time, however, by focusing on pursuing solutions that are simple, least intrusive and most flexible, Ofgem can best balance competing objectives and best

protect the long-term future of the retail energy market. This should include consideration of how engagement can be increased, which includes the role that price regulation plays in reducing this. For example, where default tariffs are the cheapest option in the market due to regulatory drivers e.g. being able to recover their efficient costs, this allows a low-risk option for all customers not just the disengaged at times of price spikes or other external pressures.

Q7. Do you have views on which of the three key parameters - the cap being flat, universal and stringent - should be relaxed when considering future price protection options?

It is our view that a continuation of a universal, flat and stringent price cap is neither possible nor desirable for an evolving retail market. All three of these parameters should be reconsidered, depending on the objectives and agreed scope of future price protection. EDF considers that an overhaul of the whole approach to price regulation is needed to ensure that suppliers are investable by making a fair margin, whilst supporting customers through increased competition in a market which supports a variety of business models.

Flat

As MHHS is implemented there will be a growth of static TOU tariffs which will also be incentivised by electricity becoming a larger proportion of householders' costs through the electrification of heat and transport. Therefore, it is essential that work progresses in a timely manner to ensure price protection does not act as a barrier to evolving the sector and allowing for innovation in product and service offerings.

We expect that the significant proportion of benefits from MHHS, in terms of the domestic market, will be realised with static time of use tariffs. While it should be acknowledged that dynamic pricing may become more prevalent via innovative tariff offerings as the market develops, we note the benefits of encouraging greater flexibility in the time of electricity usage may also be delivered via alternate means to the tariff offering. It is, therefore, important Ofgem ensure that in any future approach that innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

Given the above, we do not currently believe the time is correct to consider dynamic ToU based approaches to price regulation. The benefits of dynamic ToU tariffs will only be achieved with the active engagement and behaviours by consumers. Such tariffs are best left to the market to innovate and deliver value to engaged consumers. Such tariffs only present a very small share of the market currently, and this is not expected to change quickly, therefore the key risk is that regulation acts as a barrier to customer adoption.

Universal

A key objective of price regulation and energy policy more widely should also be to support customer engagement with energy suppliers who can provide support and help achieve

ambitious net zero pathways through tailored products and services. In considering how to increase engagement Ofgem should consider whether a universal cap is acting as a barrier to this given that universal protection reduces the incentive for customers, who would otherwise be able and would benefit from, engaging with the market. Universal protection therefore acts as a barrier to engagement as such customers are aware that they will receive a 'fair price' even where they do not actively engage.

Despite how it is often perceived and wrongly presented, the affordability of energy has never been an objective for the current DTC. Affordability is best dealt with as a matter for social policy that requires action from Government to introduce meaningful change that can effectively better support households with their energy needs.

The best way to support such customers is via a targeted social tariff, or similar targeted support. It is vital Government urgently follows through on its previous commitment to introduce a meaningful social tariff, which we continue to consider would ideally be government funded rather than by other energy consumers. Therefore, Ofgem must continue to make the case to Government for such a targeted intervention to support customers who cannot afford to pay their energy bills.

Importantly, however, there is a need to ensure that any interventions to support vulnerable customers do not result in such consumers being excluded from accessing the benefits which can be achieved by engaging with the market, including smarter tariff options, where these are appropriate for their needs. This should be a key consideration when developing any additional support for vulnerable customers.

Stringent

A key focus for EDF is ever increased efficiency in how we deliver support and products to customers. This has always been a concerted area of focus for us and we are proud of the progress we have made. However, drives for greater efficiency must not be at the expense of services that customers expect and deserve, such as would be achieved through reducing customer service levels by for example reducing contact centre opening times.

Ofgem has described the current DTC as stringent because it is calculated using a bottom-up approach based on a notional efficient supplier. This design was primary as a result of concerns at the time around supplier efficiencies and its impact on the costs consumers faced.

Ofgem must, however, recognise that the market has evolved since the DTC was established and this must be considered in any revised approach to price protection. It is not clear that there is a need for regulatory interventions to drive efficiency over and above that which the market and competition brings.

Ofgem must be mindful of the risks of continuously incentivising cost reductions from suppliers whilst ensuring that high levels of customer service and Net Zero innovation are also brought forward by the retail market. Any options that overly focus on efficiency, for example

by constantly favouring a lower quartile cost benchmark in different areas, will make it challenging for suppliers to deliver the improvements in levels of customer service standards that customers expect, and which want suppliers want to be able to deliver. It is also welcome that Ofgem itself recognised this in a recent workshop that differences in cost to serve between suppliers can be attributed to differences in customer bases and business models rather than efficiency levels per se.

It is vital that any future price protection provides sufficient financial scope to allow all efficient and resilient suppliers, including small suppliers and those with innovative business models, to stay solvent, deliver high qualities of customer service and innovate for Net Zero. On this basis, in the absence of more significant broader price protection reform, Ofgem should also move away from using lower quartile approaches in the current DTC and instead adopt average benchmark approaches. Ofgem has already adopted such an approach under the price cap for other allowances such as smart metering, COVID-19 and additional support credit (ASC) bad debt costs. This would allow suppliers to have greater freedom to differentiate how they serve and create value for customers, leading to more choice, innovation and an active market.

Q8. What are your views on options discussed? Do you have any preferred options or combination of options?

As a precursor to the discussion on the potential benefits of each of the options, there is a need to reassess, determine and clearly communicate a clear set of priorities and objectives of any future price protection mechanism(s). Only by being clear on what issues price regulation is trying to mitigate and what market outcomes are being targeted can Ofgem and Government determine what mechanism(s) are needed. The current DTC is, for example, flat, universal and stringent, because of the objectives set for it by Government. To now understand to what extent each of these categories remains important depends on what the forward-looking objectives are.

We are currently minded that the most sensible approach to future of price protection will in fact be a combination of solutions, addressing different issues and delivering different objectives, in a manner no single solution is likely to be able to do simply without unintended consequences. In terms of options presented in the paper, we have at this stage the following high-level observations:

Options that move away from a flat cap

In terms of static ToU, we agree that greater flexibility could be accommodated, including under the current cap. As MHHS is implemented there will be a growth of static TOU tariffs which will also be incentivised by electricity becoming a larger proportion of householders' costs through the electrification of heat and transport. Therefore, it is essential that work progresses in a timely manner to ensure price protection does not act as a barrier to evolving the sector and allowing for innovation in product and service offerings.

We expect that the significant proportion of benefits from MHHS, in terms of the domestic market, will be realised with static time of use tariffs. While it should be acknowledged that dynamic pricing may become more prevalent via innovative tariff offerings as the market develops, we note the benefits of encouraging greater flexibility in the time of electricity usage may also be delivered via alternate means to the tariff offering. It is, therefore, important Ofgem ensure that in any future approach that innovation is not inappropriately constrained by unnecessarily prescriptive regulation and can be appropriately deployed in consumers' interests to reward engagement with smarter consumption and options for automation.

Given the above, we do not currently believe the time is correct to consider dynamic ToU based approaches to price regulation. The benefits of dynamic ToU tariffs will only be achieved with the active engagement and behaviours by consumers. Such tariffs are best left to the market to innovate and deliver value to engaged consumers.

Options that move away from a universal cap

As we have set above, the current DTC is not a tool that addresses affordability issues. It is also a challenge that all the options presented in the Ofgem paper are fundamentally ill-suited to address. Affordability is best dealt with as a matter for social policy that requires action from Government to introduce meaningful changes that can effectively better support households with their energy needs. The best way to support such customers is via a targeted social tariff, or similar targeted support. It is vital Government urgently follows through on its previous commitment to introduce a meaningful social tariff, which ideally would be government funded. Therefore, Ofgem must continue to make the case to Government for such a targeted intervention to support customers who cannot afford to pay their energy bills.

Importantly, however, there is a need to ensure that any interventions to support vulnerable customers do not result in such consumers being excluded from accessing the benefits which can be achieved by engaging with the market, including smarter tariff options, where these are appropriate for their needs. This should be a key consideration when developing any additional support for vulnerable customers.

An understanding the objectives and market outcomes of any future price protection needs to be established. This should include a reconsideration of the universal nature of the current cap and determination on what customer segment(s) need continued support. For instance, should it be limited to those who have been disengaged for more than a defined period of time (i.e. three years or the like), or should all customers be able to select a regulated tariff even where they are not disengaged.

A key objective of price regulation and energy policy more widely should also be to support customer engagement with energy suppliers who can provide support and help achieve ambitious net zero pathways through tailored products and services. In considering how to increase engagement Ofgem should consider whether a universal cap is acting as a barrier to

this. This is due to the fact that universal protection reduces the incentive for customers, who would otherwise be able and would benefit from, engaging with the market. Universal protection therefore acts as a barrier to engagement as such customers are aware that they will receive a 'fair price' even where they do not act on their own behalf.

Options that move away from a stringent cap

Relative Caps:

Both the market basket cap and the supplier relative cap are aimed at limiting default tariff prices based on comparisons to either average tariffs in the competitive market or to each individual supplier's cheapest tariffs. However, both, particularly as means of addressing any perceived loyalty penalty risk (compared to alternatives), would be very complex to implement and open to gaming, especially in a future retail market (e.g. MHHS). Ofgem would also be required to set an arbitrary differential between tariffs.

All relative caps would achieve is limiting the variance between what new and existing customers pay, rather than ensuring all are able to benefit from the same range of choices. We do not think that the relative cap options merit further investigation at this stage.

BAT:

EDF remains supportive of the BAT being an enduring feature of the market as this would involve the simplest option to mitigate the key risks of loyalty penalties. EDF consider a BAT is an essential protection, even with the current DTC, for loyal customers, who currently make up a majority of the market, against unfair and unsustainable pricing practices which mean they are forced to switch supplier if they want to access the cheapest deals. It also ensures that suppliers are encouraged to focus on supporting all of their customers, including their existing customer base, by for example investing in high customer service levels and innovative offerings.

A further advantage of the BAT is that it would mitigate the risk of the reintroduction of unsustainable and irresponsible business models and pricing practices and, ultimately, unnecessary instability into the market. As the history of this market demonstrates, this presents real risks to end consumers who will ultimately be asked to foot the costs of a destabilised market.

Margin Cap:

In the event that there are remaining concerns around the levels of profits being made in the sector, EDF would support further consideration of a margin cap and how it could be designed to meet the objectives and market outcomes being sought. However, careful consideration is needed to ensure that such a form of financial regulation can encourage greater levels of investment in service levels and net zero solutions (e.g. the need to also establish a 'reinvestment mandate').

It will also be essential to ensure that retail suppliers can make fair returns, even where there are systematic issues which impact costs, for example, at times of unexpected prices due to external factors. This would require a cap which extends beyond a single year and reflects losses or gains in any particular year.

Other areas to be considered would also be that such a cap may well prevent unfair pricing across all customers, but some customer segments may still be negatively impacted; and the extent to which such a cap would be a disincentive to a supplier to become more efficient.

Q9. In particular, which options or combination of options do you think would best protect vulnerable customers?

As set out in our response to Question 7, the best way to support such customers is via a targeted social tariff, or similar targeted support. It is vital Government urgently follows through on its previous commitment to introduce a meaningful social tariff, which ideally would be government funded.

Further support and protection could be delivered by combining the above with a continuation of the BAT, which would ensure that supplier offerings are available to all.

Q10. How should consumers with large flexible loads, mainly EV and solar / battery users, be treated with regards to future price protection?

Please see our response to Question 7.

Q11. Are there any additional options that we haven't, but should be considering?

EDF is not aware of any other additional options at this time. However, it is noted that all the options presented are described at a very high level and there will be variances in how the detail on some or all of them could be further developed. This would include, for example, how a margin cap approach would work in practice, specifically over what time period and how it would accommodate losses/gains between years.

In terms of moving forward, we would recommend the following:

- ensure that the future of domestic price protection is not considered in isolation, but rather within the context of the wider objectives and working of the retail market.
- reassess, determine and clearly communicate a clear set of priorities and objectives of any future price protection mechanism(s). Only by being clear on what issues price regulation is trying to mitigate and what market outcomes are being targeted can Ofgem and Government determine what mechanism(s) are needed;
- discontinue further development of options that will not deliver on these, or which add undue complexity; and

- work with stakeholders and experts, including suppliers and consumer groups, to further develop the design of remaining options, with a focus on operability and potential unintended consequences.

EDF
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