

## A response to the Ofgem consultation on the Retail Market Review: Domestic Proposals – February 2012

### Introduction

Consumer Focus Wales is the statutory organisation campaigning for a fair deal for energy consumers. Part of Consumer Focus, our structure reflects the devolved nature of the UK. Consumer Focus Wales looks at issues that affect consumers in Wales, while at the same time feeding into and drawing on work done at a GB, UK and European level.

We are the voice of the consumer and work to secure a fair deal on their behalf. In advocating for consumers we aim to influence change and shape policy to better reflect the needs of consumers. We do this in an informed way owing to the evidence we gather through research and our unique knowledge of consumer issues. We have a particular focus on vulnerable consumers, those on low incomes, people with disabilities, people living in rural areas and older people. In addition, we also seek to identify where other consumers may be disproportionately disadvantaged by a particular consumer issue or policy.

We are particularly concerned about the impact rising energy prices are having on the ability of many consumers in Wales, particularly the most vulnerable, to keep warm at a price they can afford.

We welcome the opportunity to respond to this consultation on '*The Retail Market Review: Domestic Proposals*'. This response is **supplementary to the full response submitted by Consumer Focus** and highlights some of our concerns about the current core tariff proposals, as well as research undertaken by Consumer Focus Wales into the extent consumers in Wales are engaging with the energy market<sup>1</sup>. A summary report of these findings is attached as part of this response.

### Overview

Our research shows that currently consumer engagement with the energy market remains low in Wales. Compared to the situation across Great Britain far more consumers in Wales who have never switched show no inclination to do so in the future, indicating **the challenge of encouraging more consumers to engage in the energy market could be even greater in Wales.**

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<sup>1</sup> 'Switched off: consumer views on energy switching in Wales', Consumer Focus Wales (January 2012)

If managed effectively Ofgem's proposals to simplify the tariff structure should hopefully not only make it easier for consumers to compare deals across suppliers but also to compare tariffs with the same supplier. Supporting people to switch tariff without changing supplier could be an important first step in encouraging more active engagement in the wider energy market.

We support the implementation of the majority of the package of measures proposed by Ofgem.

We do however have a number of specific concerns on certain elements of the core tariff proposal and the potential impact this may have on the already static market in Wales.

Many of these reiterate the concerns expressed by Consumer Focus in their response.

- ***Risk of consumer backlash resulting from the ban on all existing discounts for standard tariffs (e.g. dual fuel; prompt payment; on-line account management)***

Our evidence shows that around 40 per cent of people in Wales who have switched reported doing this infrequently or only once. This has largely been the result of switching to dual fuel deals with one of the previous incumbent suppliers, most notably SSE and British Gas. Removing such discounts has the potential to lead to further consumer disillusionment with the energy market and only increase confusion. More research on consumer reaction to this proposal is needed.

- ***Risk of higher prices for sticky consumers***

The prevalence of sticky consumers in Wales is high. Our research shows that despite substantial increases in energy costs last year the vast majority of non-switchers (94%) say they are unlikely to switch supplier in the coming year. This is mainly because they are happy with their current supplier (59 per cent) or they believe it's too much hassle to change (19 per cent). This indicates that the majority of consumers in Wales are likely to remain on their supplier's standard tariff in the foreseeable future.

Ofgem expects that making it easier for consumers to compare standard tariffs will help stimulate engagement in the standard tariff market and hence result in more competitive prices. However we believe another potential outcome could be that the proposals will lead to little differences between standard tariff prices meaning consumers see less value in switching. With limited incentives for suppliers to compete for standard tariff customers, combined with the loss of all existing discounts on such tariffs, many consumers in Wales could end up paying even more for their energy as a consequence of the core tariff proposals.

- ***Level of choice available to consumers not paying by Direct Debit***

Reflecting the situation across Great Britain, our findings show 47 per cent of electricity customers and 45 per cent of gas customers in Wales use a payment method *other than* Direct Debit to pay their bills. These customers are also among the least active when it comes to switching.

This may partly be explained by the fact that a recent review of fixed term tariffs by Consumer Focus<sup>2</sup> found that generally the options and potential savings people gain from switching tariffs and/or supplier can be much more limited if you choose to pay your energy bills by quarterly bill or prepayment meter (PPM) as opposed to Direct Debit.

Not paying by Direct Debit is an *active choice* for some consumers, many of whom are likely to be either younger (in the case of PPMs) or older (in the case of those paying quarterly by cash/cheque), and living on a low or fixed income. Previous research by Consumer Focus Wales<sup>3</sup> found that for the majority of people who manage on a cash budget maintaining control over their finances is the critical factor. Many felt this control was lost when you paid for things using Direct Debit. The fear of payments going out unexpectedly and the potential of being charged for an unauthorised overdraft put many people off using them. This situation is likely to continue unless an alternative means of paying bills electronically, more suitable to the needs of those who manage their budgets weekly, is developed.

We believe Ofgem needs to do further work to assess the impact the proposals will have on choices in the non standard market for those *not* paying by Direct Debit.

- ***Protection for vulnerable consumers***

For the reasons stated above we are concerned that the current core tariff proposals will do little to stimulate vulnerable consumers to engage more frequently in the energy market. As a result many of those living in fuel poverty, including the most vulnerable, may remain on less competitive, more expensive standard tariffs. If implementation of the proposals goes ahead we believe careful monitoring will be required to assess the specific impacts on this group of consumers.

Switching alone is unlikely to be enough to help some of the most vulnerable consumer groups afford to heat their homes adequately. We believe further intervention is needed to protect fuel poor and vulnerable consumers from the market forces that operate within the energy supply sector.

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<sup>2</sup> See Consumer Focus consultation response for details

<sup>3</sup> 'Cost of cash', Consumer Focus Wales (November 2009)

Over the coming years consumers will see an increase in non-consumption costs being added to their energy bills. For example, to recover UK Government environment and social levies and costs associated with updating our ageing energy infrastructure. As such people living on lower incomes, who generally spend a higher proportion of their income on energy, will be paying disproportionately more towards these costs. Alternative approaches should therefore be investigated, including basing the recovery of such costs on consumption rather than a fixed level for all.

We believe the UK Government should also take steps to extend current data matching powers to help energy suppliers identify low income and vulnerable households and target assistance at those consumers most in need. This should include extending Pension Act 2008 powers to other priority groups e.g. to the Super Priority Group (i.e. households eligible for Cold Weather Payments and those in receipt of Child Tax Credits with an income under £16,190).

These steps would help reduce considerably the wasteful administration costs companies face in trying to identify consumers who need help, a cost currently estimated by industry at £120 per priority group customer.

**Viv Sugar**  
**Chair**

**February 2012**

## Switched off: consumer views on energy switching in Wales

### Summary report

#### Introduction

This short summary report provides an overview of the key findings from research commissioned by Consumer Focus Wales in November 2011 on the extent to which consumers in Wales are engaging with the energy market<sup>4</sup>. It is submitted as evidence in response to the Ofgem consultation *'The Retail Market Review: Domestic Proposals'*.

A full copy of the report, *'Switched off: consumer views on energy switching in Wales'* can be found [here](#).

Our research included identifying the factors that are driving people to switch, or conversely identifying the factors that are preventing more consumers from engaging with the market. Both the Ofgem Energy Supply Probe in 2008 and the Retail Market Review (RMR) in 2011 have highlighted that the prevalence of so-called 'sticky consumers' ie consumers who don't switch, is higher in Wales and Scotland, particularly among electricity consumers in South Wales where loyalty to the SWALEC brand remains high<sup>5</sup>. Ofgem evidence also suggests that many sticky consumers are likely to be vulnerable consumers eg those on a low or fixed income<sup>6</sup>.

#### Overview

During these times of fluctuating energy prices, with the predicted long term trend being upwards, it is more critical than ever that people have a better understanding of how to get the best energy deal for their needs and circumstances. Equally it is critical that the market works well for consumers.

Since competition was opened up in the late 1990s Ofgem has stated that consumer switching is what drives a competitive energy market. Market structure and the number of new entrants play significant roles in effective competition. However, Ofgem argues that higher levels of consumer engagement – in terms of the proportion of people engaging with the market and the frequency with which they do so – place greater competitive pressures on suppliers to retain existing customers and gain new ones by reducing costs or improving customer service. Low levels of engagement reduce that competitive pressure. Ofgem's

<sup>4</sup> A total of 1,008 face-to-face interviews were completed with a representative sample of adults aged 16 and over, as part of the Beaufort Research Quarterly Wales Omnibus Survey. Fieldwork took place between 18 and 27 November 2011. Only those people solely/ jointly responsible for paying the household electricity and gas bills were interviewed giving a total of 823 interviews.

<sup>5</sup> The Retail Market Review – Findings and initial proposals: Supplementary appendices', p12, Ofgem (March 2011)

<sup>6</sup> The Retail Market Review – Findings and initial proposals: Supplementary appendices', p28, Ofgem (March 2011)

recent reviews of the energy market also found that suppliers generally make higher profits from consumers who don't switch.

Stimulating regular consumer engagement in the market is therefore seen as a key component for increasing competition between energy suppliers which should ultimately benefit consumers. As more and more people in Wales are struggling to pay their energy bills, we believe the focus should be on ensuring all consumers are getting the best energy deals for their circumstances. This may mean regularly changing their energy supplier, or it could also mean frequently moving to a different tariff or more appropriate tariff with the same supplier. This should be in addition to ensuring people are accessing any support they may be entitled to (including financial support for energy efficiency measures).

### *Frequency of switching*

Our research found that the proportion of consumers regularly engaging with the energy market remains low in Wales. Around two-fifths of consumers *have* switched (around 40 per cent) but haven't done so recently. Our evidence shows this has largely been the result of people consolidating their energy supplies by switching to dual fuel deals with one of the previous incumbent suppliers, most notably SSE (operating under the SWALEC brand in Wales) and British Gas. Both companies have actively encouraged existing electricity or gas customers to switch to a dual fuel contract. The two companies currently dominate the market in Wales. ScottishPower the incumbent electricity supplier in North Wales, appears to have been less successful in this approach.

Looking at each end of the scale, around one in eight consumers in Wales (12 per cent) describe themselves as regular switchers ie they switch supplier every year/two years. This is largely comparable with Ofgem's estimates for the rest of Great Britain (GB). Many of these proactive consumers are currently with suppliers other than the former incumbent suppliers and they tend to be in the middle age bands; on higher incomes; regularly use the internet; and predominantly research the market using price comparison sites. Most people who've switched after using this approach said the expected savings on their energy bills had been realised. They are also more likely to switch in the future.

Not surprisingly saving money is the main reason why people have switched suppliers. Consumers who've switched in reaction to face-to-face sales or telesales processes especially those who've switched on the doorstep, are less likely to have realised savings. This is likely to be due to people feeling pressured to buy without having all the relevant information available. Suppliers' best deals are also not often available on the doorstep. Following a recent campaign by Consumer Focus five of the 'Big Six' suppliers have now stopped this type of marketing activity. Only E.ON's position remains unchanged.

### *Disengaged consumers*

One of the key findings of our research was the high proportion of consumers in Wales who have never switched their energy supplier (46 per cent). **The majority of whom (94%) show no inclination to do so in the future i.e. they are 'permanently disengaged' from the market.**

These consumers tend to be younger, on lower incomes, and never use the internet. The two main reasons for never switching are because they are happy with their current supplier (59 per cent) or they believe it's too much hassle to switch (19 per cent).

These results are notably different from Ofgem's estimations for the whole of GB<sup>7</sup>. The proportions of those who have never switched are fairly comparable – the GB average is estimated to be around 40-60 per cent. However, a far lower proportion of disengaged consumers in Wales were likely to switch in the future (just 3 per cent compared to a British average of 20-30 per cent). **This indicates that encouraging more consumers in Wales to engage with the energy market could be an even greater challenge.**

### *Factors that impact on switching levels*

Supporting the findings of recent Ofgem research<sup>8</sup> we found a strong correlation between internet use and the frequency of energy switching. Regular internet users are much more likely to be regular switchers. Programmes to encourage internet take-up among some groups of consumers, most notably those on lower incomes, may therefore help to encourage more active engagement in the energy market.

There is also a strong correlation between the likelihood of switching in the next 12 months and the extent to which people had switched previously.

Saving money is the predominant reason why people have switched supplier however a whole range of factors can determine why people remain with the same supplier. These include customer knowledge and awareness of the market; the perceived value in switching suppliers and ease/confidence in doing so; levels of customer service/company performance; ability to access and understand information on prices/tariffs in order to make an informed choice; and brand/company loyalty (a particular factor in Wales and Scotland).

Low engagement levels will need to be tackled if more consumers are going to benefit from competition in the energy supply sector. Improving consumers understanding of the market will no doubt help, but information alone will not necessarily result in greater action. There are also likely to be a range of other social, cognitive and behavioural factors which influence consumers' decision making processes and engagement.

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<sup>7</sup> 'The Retail Market Review – Findings and initial proposals', Ofgem (March 2011), p29

<sup>8</sup> Customer Engagement with the Energy Market – Tracking Survey: Report prepared for Ofgem', Ipsos Mori (January 2011)

Behavioural economics theory can therefore go some way to gaining a better understanding of consumer behaviour in the energy market and is being increasingly considered by Ofgem and the UK Government. We would urge further exploration of these issues when designing switching campaigns.

#### *Protection for vulnerable consumers*

Ultimately encouraging consumers to engage more frequently in the energy market should lead to many more people being able to find the best deal for their energy needs. However, over the coming years as energy costs continue to fluctuate, and additional non-consumption costs are added to consumer bills (eg the recovery of costs associated with environmental and social obligations), **switching alone is unlikely to be enough to help some of the most vulnerable consumers afford to heat their homes adequately. Equally important is ensuring energy companies, as well as the Welsh and UK Governments are providing the right support for the most vulnerable.**

### **Recommendations**

In addition to the specific issues raised in the letter that accompanies this summary report regarding the RMR Domestic Proposals we make the following recommendations to Ofgem and others.

#### ***Ofgem, Citizens Advice Cymru and energy suppliers should:***

explore different ways of encouraging non-internet users to engage with the energy market as part of the Energy Best Deal Campaign. This could include:

- providing more hands-on support in switching tariff or energy provider, talking someone through the process
- formalising the use of peer educators who regularly switch provider to encourage others to turn the knowledge they have gained into action.

target support available under the Energy Best Deal scheme to off-gas communities as electricity-only customers are currently less likely to switch than those connected to the mains gas network

ensure future evaluations of the Energy Best Deal scheme include separate analysis for England, Wales and Scotland to allow more meaningful comparisons across nations

undertake more follow-up evaluation of impact, for example six months after people have taken part in an Energy Best Deal session, to see if people have become more engaged in the energy market as a consequence



***Ofgem, suppliers & UK Government should:***

consider the application of behavioural economics when designing and implementing switching campaigns, particularly among vulnerable groups.

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