February 23rd, 2012

Louise van Rensburg
Retail Markets
Ofgem
9 Millbank
London
SW1P 3GE

Dear Louise,

Retail Market Review: Domestic Consultation

Please find First Utility's answers to the above consultation below. We would request that Ofgem treat the appendix to this response as commercially confidential.

First Utility's view is that the primary aim of the Retail Market Review should be to boost consumer engagement and encourage competition by removing barriers to entry and growth for smaller suppliers as well as obviating the advantage that the Big Six derive from their level of vertical integration and dominance of the domestic supply market.

However, we believe that the single variable rate tariff proposal will further constrain the ability of smaller suppliers to effectively compete. It is reasonable to assume that the implementation of this proposal will create a market where the large majority of consumers are supplied through fixed tariffs although it is far from proven that a similar proportion of domestic customers actually want this. We also feel that smaller suppliers will be disproportionately disadvantaged by this proposal as these companies, having a rapidly growing customer base rather than an already established one which does not generally vary greatly in size as is the case with the Big Six, face a much greater level of uncertainty around hedging demand for their customers.

Chapter Two

Question 1: Do stakeholders agree that we should introduce the RMR core proposal?

While we appreciate the work done by Ofgem in relation to making it easier for domestic customers to switch through simplification of information provided, First Utility has some concerns relating to possible unintended consequences of the core proposal and particularly as regards standard tariffs.

Firstly, this could be seen by the Big Six as an opportunity to move large numbers of standard tariff customers onto new "fixed" non standard tariffs in order to remove these as potential customers for independent suppliers, at least for the period of time for which the "fixed" period of the new tariff applies. Currently, any action like this by the Big Six could be described as collusion and might be less likely to occur. However, once the new proposals are enacted, the Big Six could simply describe these actions as seeking to be compliant with the new rules. If this proposal is implemented it is imperative that the Big Six be required to inform customers that they can switch as part of the transition process.

Secondly, we have some concerns over the proposed standing charge which is to be determined by Ofgem. All suppliers calculate and make amendments to their standing charges differently.

Removing this ability could remove a competitive advantage that some suppliers might have against other suppliers as a result of having lower overheads and thus a lower level of cost to serve. It will also remove the possibility of suppliers offering certain products which we feel would be likely to be of benefit to consumers which is likely to stifle innovation. This would be to the detriment of smaller suppliers who are often more innovative in their product offerings as they attempt to differentiate themselves from the Big Six. For example, we have recently been considering a tariff which would track our standard tariff with a price cap. However, this would not be allowed under Ofgem's proposals as a non standard tariff cannot track the standard tariff. We have provided Ofgem with further examples of tariffs in a confidential appendix which we would like to offer in the future and which we feel would benefit the consumer but which would not be allowed under Ofgem's current proposals.

Finally we do not believe that creating a rigid structure for standard tariffs will necessarily increase levels of consumer engagement, particularly as a significant amount of comparison information is already provided through bills, annual statements and switching sites. Prohibiting discount offers for standard tariffs will also be to the detriment of smaller players as this will leave them less able to compete on a cost basis. In addition, the proposals would also stop smaller suppliers from targeting certain market niches in order to tactically grow their businesses thus creating a further barrier to entry and growth.

Question 2: Which cost elements should be included in the standardised element of standard tariffs?

We have some concerns as to how the network charges will be calculated and how equitable these charges will be when representing a variety of different consumers. The risk of low users paying more each year for their energy bills as a result of standardised elements of their bill still appears to be a significant factor under Ofgem's proposed options.

In addition many fixed elements currently included in standing charges change more frequently than annually, yet Ofgem is only proposing to update the fixed standing charge once per year. Suppliers will be exposed to this risk and this is likely to force them to be more conservative in tariff setting, thus potentially pushing the extra cost on to consumers.

This is also a time of considerable change resulting from EMR and various elements of the proposals related to this such as a capacity obligation on suppliers and a CfD FiT driven obligation on suppliers are controlled by DECC rather than Ofgem. If these obligations were to be introduced intra year at a time when the current Ofgem set standing charge does not take them into account, the results could be material.

We also have some concerns as to how the smart metering element of customers' charges will be taken into account. Currently, not all suppliers make use of these but there is clearly an associated cost of sales which will need to be taken into account. We would request further detail from Ofgem as to how it proposes to deal with this issue.

In order for competition to be effective, the view of First Utility is that suppliers should be able to offer tariffs with their own blend of fixed and variable rates at their discretion. It may be that consumers have confused tariff complexity with tariff comparability. It is worth noting that the mortgage and insurance markets and mobile phone offerings work along these lines and customers appear to be able to compare these without too much difficulty.

We would propose that tariffs should have a fixed and variable rate, both set by the supplier, but that the supplier should be required to take those two numbers, along with the EAC and AQ for each relevant site, and calculate a single "effective unit rate" which would then be clearly stated for comparability purposes. All bills and annual statements should then show this effective unit rate and thus allow customers to easily find the important numbers for comparison with other tariffs. This would be a simple change but would not stifle innovation and disproportionately disadvantage smaller independent players.

Question 3: Do stakeholders agree that our information remedies would help consumers engage effectively? If not, what would be more appropriate remedies?

First Utility agrees that tariff comparability is a cause of consumer disengagement from the energy market, therefore, the information remedies proposed such as consistent/standardised terms and language and the introduction of a price comparison metric will help by offering a quick and easy to understand comparison at a glance; however, great care must be taken to ensure the accuracy of any standardisation.

Research appears to show that the phenomenon of "sticky customers" results from a poor understanding of how to compare tariffs as well as a general lack both of trust in energy suppliers and awareness as to how the market operates. In order for a customer to ascertain which tariff best suits their consumption, it is necessary for them to know how much they pay annually and what their annual consumption is. Hopefully the provision of this information through the Annual Statement will assist in achieving this aim.

When the methods currently available to compare tariffs on switching sites are taken into consideration, it can be argued that the proposal of a standardised element to tariffs may be unnecessary and that simply offering customers more details regarding their consumption and prices on their monthly bills would prove more useful. This simpler option would be less costly to the industry and address the concerns raised by consumers regarding tariff comparison.

We also feel that competition in the retail market cannot be fully established until effective measures are undertaken to increase liquidity in the wholesale market. The difficulties which smaller players experience in accessing non standard products in levels of granularity that meet their needs, as well as the barriers posed by credit requirements, significantly constrain their ability to manage the risks associated with customer supply. It is likely that action taken by the regulator to reduce these risks to a more manageable level would result in a significant uplift in the level of new entrants which would then pose a real challenge to the incumbent suppliers, increase consumer choice and ultimately drive prices downwards.

Question 4: Do stakeholders consider that the price comparison guide should be presented in a p/kWh figure, a £ per month figure or both?

We consider that the price comparison guide should include both p/kwh and a £ per month figure, thus ensuring a more tangible comparison for budgeting purposes. This format of information is already included in First Utility's literature and we would encourage the use of a similar format by all other domestic suppliers. Our proposal for an "effective unit rate" discussed in our answer to Question 2 may be of particular relevance here.

Question 5: Do stakeholders agree that the proposed exceptions for legacy social tariffs and extremely high consumption domestic consumers are appropriate?

Yes, these seem appropriate.

Question 6: Do stakeholders agree that we should not allow an exception for suppliers to offer a green standard tariff in addition to an "ordinary" standard tariff?

We feel that suppliers should be able to offer the tariffs they feel are suitable with an "effective unit rate" being provided. Please see our answer to Question 2.

Question 7: Do stakeholders believe it would be appropriate to introduce a six-month price guarantee for standard tariffs, or do you consider that this would undermine the simplicity of the RMR core proposal?

We do not agree that 6 months is an appropriate length of time as this may unduly impact smaller players who are more exposed to short term volatility in the wholesale market. First Utility currently offer a 3 month price guarantee upon registration, with the instruction that the chosen tariff will not be subject to any price increase that takes place until the defined date, or until any unilateral variation takes affect after the 3 month price guarantee, whichever comes first. We also offer this guarantee to any customer changing to a different tariff.

Chapter Three

Question 8: Do stakeholders agree with our recommended proposal of Option 3 ("Introduce more prescriptive rules") for bills and annual statements?

We agree with the proposals of option 3 as more clarity is needed in such literature to increase transparency. We believe that an easier to understand bill/annual statement being sent to consumers, offering a more tangible format for budgeting purposes, will increase engagement in the market and may encourage those customers less likely to engage in the market to become more involved.

Question 9: Do stakeholders agree with our recommended proposal for SLC 23 notifications including price increase notifications of option 3 ("Additional information plus prescribed format") and option 4 ("Tighten and clarify policy intent")?

Yes, these seem appropriate.

Question 10: We seek views from stakeholders on the additional requirements outlined in option 3 ("Additional information plus prescribed format") for SLC 23 notices including price increase notifications.

It is the view of First Utility that the lack of understanding of the terms and format used to deliver information to the consumer is a subject of major concern regarding the disengagement of the consumer in the energy market. Any improvement on this is to the advantage of the consumer and subsequently to the competitiveness of the industry.

Regarding the additional requirements outlined in option 3, these seem appropriate, easy to incorporate into existing suppliers' methods and necessary to ensure the best outcome of the policy's intent.

Question 11: We seek views on any proposals to restrict the inclusion of additional materials (e.g. marketing material) along with SLC 23 notifications.

It is First Utility's view that, as SLC 23 notifications are specifically designed to inform a consumer of changes to current terms that is to their disadvantage, they must be fit for purpose and as such should not include any marketing material that could distort the consumer's interpretation of the changes thus affecting their judgement when deciding whether or not to continue with their current supplier.

Question 12: We seek views along with any supporting data or evidence for our proposals for information signposted to consumers in option 4 ("Tighten and clarify policy intent") for SLC 23 notifications including price increase notifications.

These additional obligations would provide more clarity for the consumer and in particular, the extended "notice of transfer" window addresses the current risk of certain suppliers not meeting deadlines in time for the customer thus reducing customer dissatisfaction and promoting effective engagement.

Question 13: We seek views on any additional recommendations which stakeholders consider relevant for bills, annual statements and SLC 23 notifications.

First Utility recommends an addition to the annual statement consisting of a glossary explaining the terms used in the energy industry and for this information to be printed in a standardised language and format thus increasing energy literacy in the UK. Such an addition would provide consumers with the information that they have advised they are currently not aware of via the latest customer survey reports mentioned by Ofgem in this consultation and promote confidence within the consumer to engage in the market.

In addition, we would like to see more information to help customers compare tariffs on each bill. This information would include annual consumption and annual costs based on current tariff prices and historical consumption data. Such information being made available to customers on a more frequent basis would go some way to address the concerns consumers have when faced with comparison guides on switching sites as consumers have advised that they do not always have this information and some do not know how to obtain this information. Again, we feel that our proposal for an "effective unit rate" discussed in Question 2 is of particular relevance here.

Question 14: We intend to consult on the content of the Confidence Code separately if and when we take over the governance responsibility for it. However at this stage we welcome any early views on developing the Confidence Code.

We have no suggestions at this time.

Question 15: We welcome views from stakeholders on our proposals for enhanced monitoring.

As compliance with SLCs is an obligation, we agree that if the need for enhanced monitoring exists then this needs to come into effect to protect the consumer and ensure consistency.

Question 16: We invite specific views on costs and other implications if we were to introduce our proposals. Please provide details and cost estimates where appropriate broken down by each proposal.

We believe that the tariff proposals, if enacted, will disproportionately affect the ability of smaller suppliers to offer innovative products and grow their businesses. However, it would be difficult to estimate the potential cost of this at this time. We are happy to discuss further with Ofgem on a face to face basis if Ofgem feels that this would be appropriate.

Chapter Four

Question 17: Do you consider the revised SOCs will help achieve our objectives?

Yes, although we would appreciate further information as to how Ofgem will apply these and address any non compliance issues.

Question 18: Do you agree the revised SOCs should apply to all interactions between suppliers and consumers?

We agree that the Standards of Conduct should form part of the licence and be enforceable for them to be fully effective.

Question 19: Do you agree that the SOCs should be introduced as an overarching, enforceable licence condition?

Yes.

Question 20: Do you have information regarding potential costs this may impose on suppliers?

We do not believe that any significant additional costs will are likely to derive from the proposed Standards of Conduct becoming a licence agreement as we would expect that suppliers are already attempting to behave in this manner.

Chapter Five

Question 21: Do you agree with our analysis of the impact on vulnerable consumers?

We agree with the analysis, and support the intervention empowering the Vulnerable Consumer with the necessary knowledge and means to effectively compare their tariff/supplier therefore enhancing engagement. However, we remain concerned that a fixed standing charge set by Ofgem will disadvantage customers who use less energy and provide a benefit to higher users. It seems reasonable to assume that customers in fuel poverty will be disproportionately disadvantaged by these arrangements should they come into effect.

Question 22: What are your views on the need for further intervention?

We are firmly of the view that the potential predatory pricing practices of the Big Six, where loss making tariffs are offered to new customers with these being subsidised by sticky customers on standard tariffs, need to be addressed in order to remove this distortion from the market and allow smaller suppliers to compete on a level playing field. As these tariffs are almost exclusively online direct debit tariffs, it can be argued that vulnerable customers who may not be eligible for tariffs of this type are particularly disadvantaged by this. We would urge Ofgem to take steps to address this matter, which is of real detriment to both the consumer and competition, and enforce the associated licence conditions prohibiting this. We feel that this is also an area that would benefit from further consideration as part of the Retail Market Review.

Question 23: Who in particular should any additional support be targeted at?

Any additional support should be targeted at households in fuel poverty who are also in receipt of the appropriate means tested benefits.

Please do not hesitate to contact me if you have any questions or would like any further information.

Best regards,

Chris

Chris Hill

Regulation Manager

07740 252072

01926 328760