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To: - David Hunt, Ofgem Response by: - James Tallack, Which?

Consultation Response

Ofgem's Retail Market Review - Domestic Proposals

About Which?

Which? is an independent, not-for-profit consumer organisation with around one million members and is the largest consumer organisation in Europe. Which? is independent of Government and industry, and is funded through the sale of Which? consumer magazines, online services and books. Which?'s mission is to make individuals as powerful as the organisations they have to deal with in their daily lives by empowering them to make informed decisions and by campaigning to make people's lives fairer, simpler and safer.

Section 1: Summary and key positions

1. The liberalised energy market is not working for consumers and the case for reform is compelling. The cost of energy – which has risen by over 60% since 2000[1] – is the number one financial concern for consumers, with nine in ten saying they are worried about it. Yet, despite widespread awareness of their right to switch their supplier and/or tariff[2], this high level of concern does not translate into concerted action by consumers to reduce their bills. According to Ofgem's figures, six in ten consumers say they have never switched supplier, while around three quarters remain on their supplier's most expensive standard tariff. And despite an average discount of over £100 per year for paying by direct debit, 40% of consumers with a credit meter continue to pay on receipt of their bill. We have calculated that over the last four years consumers have overpaid by £16bn on their energy bills[4].

[1] DECC, 2011 (http://bit.ly/yNuDLu)
[2] Ipsos MORI, 2011 (http://bit.ly/oGeDnn)
[4] Analysis by Which?.

2. There are a number of reasons why consumers do not engage effectively with the energy market. We set these out in more detail in Section 2. Some relate to the essential nature of energy as a commodity and low interest area for consumers. These are beyond the scope of this consultation process. Others, such as the time it takes to switch supplier, are within the scope and should have been given greater consideration by Ofgem. Complex pricing, however, should be one of the easier challenges to overcome. The decision to focus the RMR on interventions that make tariffs more comparable is therefore appropriate. It is unacceptable that around 40% of consumers do not save money when they switch, despite this being the main reason to switch in the first place.

3. Fundamentally, we believe that the energy market should be made simple for all consumers. The benefits of a competitive market should not be limited to a segment of well-informed and well-resourced engaged consumers. In fact, the vulnerable and low-income consumers who have most to gain from lower prices are more likely to be uninformed and/or poorly resourced. For the vast majority of consumers, competition and choice in the energy market means one thing – getting the lowest price. In line with its duty to protect consumers by promoting competition, Ofgem should use the RMR reforms to make it far easier for consumers to understand prices and identify cheaper offers.

4. While we agree with many of the proposals in the RMR, we do not believe that the tariff reforms in the RMR go far enough in promoting this objective. We have explained in detail where we do and don’t agree with Ofgem’s proposals in our answers to the specific consultation questions in Sections 3-6 of this response. For clarity, we have provided a summary of our key positions in the boxes below.

5. We also urge Ofgem to be circumspect of claims regarding the costs of implementing our proposal for simple tariffs. As we have previously stated to Ofgem, private costs, incurred for example by a company introducing new systems or redesigning products to meet regulatory requirements, are invariably easier to quantify than the wider benefits to the economy as a whole from improving consumer access, choice and information. At present, these barriers impose an externality on consumers and the economy that results from the weakness in effective competition between energy retailers.

6. As always, we look forward to continuing our constructive relationship with Ofgem concerning these and other related issues. However, we do not see this relationship as the only route to simple and fair energy tariffs and will also look to Government to take action in this area if we feel it is necessary.

Where we agree with Ofgem’s proposals

- Although long overdue, Ofgem’s proposals to improve the simplicity and comparability of bills and other routine but essential communications from energy suppliers are welcome. These should be complemented with a ‘Red Tape Challenge’-type review of the regulatory information required on energy bills.
- The Tariff Information Label is a useful proposal that should help consumers understand and compare the non-price benefits of certain tariffs, such as loyalty points and boiler servicing.
- Formalising the Standards of Conduct into an enforceable licence condition is a positive move, although this largely vindicates our warning at the time of the Probe that the Standards lacked an obvious incentive for compliance.

- Ofgem is the appropriate body to take responsibility for monitoring and development of the Confidence Code for price comparison services. We believe that consumers would further benefit from the integration of Ofgem's tariff information remedies into the information provided by price comparison services. Ofgem should also consider a number of improvements to the way that prices are calculated, such as how to account for the impact of seasonal variation in consumption.
- We are pleased to see that Ofgem's complaints monitoring function has been given consideration in this consultation, as this vital role was conspicuously absent from the initial findings document. Our research has highlighted a number of problems with the way complaints are reported in the energy sector and we welcome Ofgem's recognition that this must improve.

Where we disagree with Ofgem's proposals

- We are concerned that some of the prohibited actions in the Standards of Conduct have been 'lost in transposition' to the licence condition. It is as important today as at the time the Standards were introduced that suppliers should not sell inappropriate products, not change anything about a product or service without providing the consumer with an explanation, prevent switching without good reason, or offer unnecessarily complex or confusing products. As such, these principles should be reinstated.
- We believe that Ofgem should follow the findings of its own research and extend a standardised simple format to cover all single-rate tariffs, and not just standard tariffs. This would mean that for the 85% of consumers on a single-rate tariff it would only be necessary to look at the unit price to identify the cheapest offer. Economy 7 and other time-of-use tariffs are inherently more complex and are likely to require a different approach.
- We question whether the simple format should include a standing charge at all. Ofgem's decision that the vast majority of network costs should be recovered not through the regulated standing charge but through the unit rate is welcome on the basis that this has been judged to be more cost-reflective. However, as our previous position was that only network costs should be included in the standing charge, the rationale for a standing charge now appears debatable. Furthermore, without a standing charge there would be no requirement for the problematic price comparison guide. Tariffs would also be more equitable as every consumer would pay the same price per unit irrespective of consumption.
- There is a risk that Ofgem's current tariff proposals will 'institutionalise' a two-tier market, in which suppliers continue 'business as usual' practices of targeting their most competitive offers at a small segment of energy 'prosumers' with the means and resources to engage effectively with the market.
- Ofgem claims that disengaged consumers on regulated standard tariffs will benefit from a 'ripple effect', but does not appear to consider that there are actually few downsides to suppliers making these tariffs the worst deal they offer. Prohibiting 'tracker' tariffs that are indexed to the standard tariff suggests that Ofgem recognises the risk that the standard tariff may not be competitive enough to constrain prices on these types of tariffs effectively.
- The price comparison guide is no silver bullet for the problem of tariff comparability. It depends on consumers knowing their consumption in order to make an effective choice; however, research strongly suggests that consumers have very poor awareness of how much energy they use. Furthermore, under current tariff structures, the price comparison guide will almost certainly show a picture of energy getting cheaper the

more you use – this risks sending entirely the wrong messages about fairness and energy efficiency.

- All discounts should be included in the unit price to bring an end to unfair discount structures. These can obscure the unit price and present significant opportunity costs to consumers that act as a brake on, rather than a driver of, competition. The implication of Ofgem's proposals for standard tariffs is that it should be entirely possible for suppliers to factor discounts into the unit rate.
- The main argument against wider standardisation of tariffs appears to be that it will hinder innovation. However, we do not believe that Ofgem has explicitly set out where innovation that has benefited consumers has resulted from not setting restrictions on the structure of current retail market tariffs.
- Smart technology, and time-of-use tariffs in particular, do represent an opportunity to deliver genuinely innovative and beneficial products that fundamentally change the relationship between consumers and the energy system as a whole. However, if standardisation will hamper the development of such tariffs they should be excluded from the simple format, rather than used to justify rejecting reform of the mainstream single-rate products that most consumers will continue to use well into in the smart meter era.

Section 2: Consumers, energy and engagement

7. We consider that in promoting engagement in the energy market, Ofgem must respond to a very particular set of challenges. Gas and electricity are entirely standard products. Quality and reliability of supply do not depend on the supplier but on the supply system, which is used by all suppliers in the market on a non-discriminatory regulated tariff. Furthermore, all suppliers are required to offer the same choice of payment methods. The dimensions of competition are therefore extremely limited, essentially coming down to service quality – the entirely routine processes of meter reading and billing, which offer little scope for differentiation – and, most significantly, price. Ofgem's own research bears this out: when asked their reasons for switching their energy supplier, over 80% of consumers say it was to save money, while just 7% say they were looking for better service. It is not clear whether those seeking better service were also hoping to save money, but our research suggests that they would have been – just one in ten say they would be willing to pay more for better service[5].

8. There are also a number of other barriers to engagement that are not present – or are at least not so pronounced – in other sectors. Consumers, on the whole, cannot be expected to find the purchase of an essential commodity particularly stimulating. The problem of low interest is exacerbated by a large and complex range of tariffs, which, although inherently similar in function, have forms and structures that render them virtually impossible to compare without using a price comparison service. In turn, using a price comparison service presents its own particular challenges[6], which are likely to contribute to the relatively low usage of these services (used by less than a quarter of switchers[7]), despite over three quarters of UK households being online[8]. Instead the majority of consumers who switch do so directly with an energy supplier – this denies them the

[5] Which? survey of 7,883 online panellists between 9th and 30th November 2009.

[6] In order to make a meaningful comparison between energy tariffs, consumers must go online to one of the 13 accredited price comparison sites and provide information from their bill or annual statement.

[7] Ipsos MORI, 2011 (http://bit.ly/oGeDnn)

[8] ONS, 2011 (http://bit.ly/yazWCu)

opportunity to objectively compare all tariffs in the market and will be a factor in why such a high proportion of consumers do not save money when they switch, despite this being the main reason to switch in the first place.

9. Consumers are also likely to be deterred from changing their energy supplier by a protracted switching process, which means that it takes between five and six weeks for the consumer to realise any material gain from switching. In the qualitative research we conducted, consumers were quick to contrast energy 'shopping' with shopping for other essentials, particularly groceries. While the impact on household budgets of a particularly expensive weekly food shop can be compensated for by choosing a cheaper supermarket and/or range of foods for subsequent purchases, this is not the case in the energy market. Instead, deprived of their main weapon to impose discipline on high-charging suppliers, consumers lack control and feel powerless.

10. We also found consumers to be acutely of the 'leader-follower' behaviour exhibited by energy suppliers in their pricing strategies. There is an expectation that the financial benefits of switching from a supplier who has increased their prices to one that has not are likely to be wiped out (by an increase in the 'cheaper' supplier's prices) in the near future. This further weakens the incentive to switch. While smart metering should, in theory, make switching quicker and easier in future, we believe that Ofgem should have given further consideration in the RMR to what impact a significant reduction the time-to-switch would have on engagement under current market conditions and metering technology.

11. We have heard the claim that the number and variety of available energy tariffs presents a less bewildering choice to consumers than other markets. Mobile phones are commonly cited as an example. Although this may be true, there are clear differences between buying a commodity and buying a mobile phone. In the case of the latter, consumers may be more prepared to invest more time and effort searching a market where the products and services on offer – handsets with attractive features and designs, bundles of inclusive minutes, text messages and data, and so on – are intrinsically more interesting and far easier to relate to than an intangible derived demand.

12. More fundamentally, it is in markets where there is ultimately a choice *not* to consume (because consumers can do without the product or service in question, or because there are substitutes available that provide a comparable service), or where choice itself is intrinsically more complex (because price is not the only differential) that it should be considered appropriate to reserve the best offers for a minority of prosumers with the means to understand and navigate the options that market has to offer. We do not recognise that the energy market has any of these features.

13. Intervention does not have to result in higher rates of switching by consumers. In fact, for consumers the best outcome may be a market where completely transparent pricing and the ability (whether exercised or not) to switch quickly and easily obliges all suppliers to match the best prices on offer. This would eliminate the requirement for consumers to continuously monitor the price of an essentially uninteresting product from a range of essentially indistinguishable suppliers.

Section 3: Improving tariff comparability
- Price comparison guide
- Discounts
- Implementation costs
- Innovation
- Dual fuel
- Smart metering and time-of-use tariffs
- Standardised element
- Information remedies
- Proposed exceptions

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

14. While, RMR Core is ostensibly a positive response by Ofgem to the problem of tariff complexity, we have identified a number of risks and other flaws that mean it may not achieve its objective. As such, we are opposed to its introduction.

15. RMR Core is designed to make it easier for largely price-driven consumers to identify the lowest-priced offers within a very limited range of standard tariffs[14] and, in doing so, exert a competitive pressure on suppliers that is currently severely constrained by an almost total lack of comparability between tariffs (in addition to the other barriers to engagement discussed in Section 2). Under RMR Core, all standard tariffs will consist of a regulated daily standing charge (p/day) set by Ofgem at the same amount for every customer in a region (irrespective of payment method) and a 'competitive' unit rate (p/kWh) that will be set by suppliers. Central to this intervention is the welcome proposition that consumers should be able to compare tariffs "at a glance" on the basis of the unit rate alone (and, by implication, without having to use a price comparison service). For all other tariffs (referred to henceforth as 'non-standard tariffs') Ofgem proposes to set no restrictions on the number, type or structure of tariffs, other than that all must be fixed term, with a clear end date and clear switching windows. There is a further requirement that that consumers who do not expressly agree to extend their contract or enter into a new non-standard offer will default to the appropriate standard tariff for their payment method.

16. However, there are clear risks in a solution that in effect creates a 'regulated' and 'unregulated' tariff market. Suppliers are unlikely to acquiesce readily to regulatory interference in the design of their products, and may choose to focus their attention instead on the unregulated segment of the market, where they can compete on their own terms. As such, we concur with the view of the Centre for Competition Policy (CCP) that "there is almost no downside to firms of making the evergreen [standard] tariff the worst deal they offer; if consumers complain, the firm can always offer them a better deal [from its non-standard tariffs], and since the tariff is one which they can present as 'imposed by the regulator' it is not really their 'fault' that it is such a bad deal"[15]. As

[14] Ofgem proposes to allow suppliers to offer just one standard tariff per payment method per fuel.

[15] CCP, 2011, p7 (http://bit.ly/rHfIF4)

undesirable as this outcome is, it could be exacerbated by - as Ofgem itself acknowledges – any poor communication of proposals that gives an impression that Ofgem favours standard tariffs (due to the regulated standing charge) and, as a result, causes consumers to be drawn to them rather than non-standard tariffs.

17. In light of the above, we would also question Ofgem's logic in prohibiting variable-price non-standard tariffs that track increases in the supplier's standard tariff. If RMR Core will "increase competitive pressure on prices" in the standard segment of the market, there should, in theory, be even greater constraint on non-standard tariffs that are indexed to standard tariffs and this should benefit consumers. We would support the prohibition of variable-price tariffs with a 'capped' discount structure (eg 2% minimum below standard), given their potential to mislead consumers[16]; however, Ofgem's proposal to ban <u>all</u> tracker tariffs (including those with a fixed delta) in the non-standard segment is not consistent with the apparent belief that RMR Core will deliver competitive standard tariffs.

18. In principle, we see the main benefit of RMR Core as currently constructed (beyond promoting simpler standard tariffs and enabling easier comparisons between them) as providing a clear 'default' option or 'tariff of last resort' for consumers who have not actively engaged with the market following expiry of a fixed-term non-standard tariff. However, a clear option is not necessarily a good-value option – it simply means that there is clarity over what will happen. If it happens that suppliers do not price their standard tariffs competitively then the prohibition of automatic rollover contracts means that – and here we again repeat the concerns of the CCP – the standard tariff may "become the switch part of a dynamic bait-and-switch strategy where the regulator provides the credibility of the 'switch' part as a good deal" [17]. This would not be a desirable outcome.

19. In our response to the first stage of the RMR we proposed a solution that we believed would leverage the advantages of RMR Core but minimise the risks described above. By extending the simple format proposed for standard tariffs to cover all single-rate tariffs (we propose an exception for Economy 7 and derivatives and smart time-of-use tariffs, below) a range of benefits that are clearly supported by Ofgem's own research would be delivered to the 85% of households[18] that currently have a single-rate tariff.

20. When tested in consumer research, this tariff structure facilitates the easiest price comparison across the market without any requirement for consumers to know their consumption and be able to readily identify with the concepts of low, medium and high usage. As we discuss below, poor awareness of energy consumption presents a fundamental barrier to effective decision making. When presented with a number of tariffs with a fixed standing charge and a variable unit rate almost nine in ten consumers were able to correctly identify the cheapest tariff. This is a significant improvement on

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[16] Driven largely by a need for the respective tariff to achieve a prominent position in price comparison tables, these products offer a substantial discount at the time the tariff is launched but allow (fully within the terms and conditions of the tariff) the discount to be reduced to the minimum level during the contract period. However, we consider that tariffs with a guaranteed discount or fixed delta relative to the supplier's standard tariff (eg Online Energy from British Gas has 4% guaranteed discount against its standard tariff) are appropriate because the commercial risk of excessive price increases on the standard tariff should act as a constraint on the price of the tariff that it is linked to.

[17] CCP, 2011 (http://bit.ly/rHfIF4)

[18] According to DECC, 3.9m out of 26m electricity consumers have an Economy 7 (or variant) tariff. It may also be the case that many of these households may be better off with a single-rate tariff (eg because they do not use enough electricity at off-peak times).

the less-than-half of consumers that were able to perform this essential task for tariffs representative of those currently offered to consumers (ie no fixed standing charge).

21. Uniformity in tariff presentation will increase competitive pressure on prices to the benefit of consumers because they will have the ability to easily identify price differences between what are very similar products. This benefit will be enhanced by an increase in the range of media that will be able to report tariff information, as a single pricing system for all tariffs, where only the unit rate 'matters' can be easily and clearly presented. It should also follow that simpler products will reduce the scope for suppliers to mislead consumers in their marketing, improve billing clarity, and promote a better understanding of the relationship between cost and consumption among consumers and associated sustainability benefits.

Price comparison guide

22. Rather than regulating the format of non-standard tariffs, Ofgem proposes to facilitate comparisons between simple, uniformly-structured standard tariffs, and the potentially limitless variations of non-standard tariffs, by introducing a price comparison guide. With a nod to the APR metric found in financial services, it calls this the "Standard Equivalent Rate" (SER). The SER seeks to make it possible for consumers to make comparisons between all tariffs on the basis of the unit rate alone. However, any consumer using the SER to compare a non-standard tariff with a standard tariff or a non-standard tariff with another non-standard tariff will also be required to decide what their usage level is. Allowing suppliers to set both the fixed (eg standing charge or initial tier of higher-priced units) and variable elements of non-standard tariffs, means that the total annual cost must be calculated[19] before the regulated standing charge can be subtracted from it to produce the residual that forms the basis for the SER. Because it would be impractical to provide an SER for every level of consumption (even though total annual cost will differ with every kWh used), Ofgem proposes publishing an SER for a 'notional' low, medium and high consumer for each non-standard tariff.

23. The requirement for consumers to know their consumption in order to make effective use of the SER adds a significant layer of complexity to a process that already presents a number of serious challenges to engagement. Research by the European Commission found that only 36% of UK consumers have a reasonable level of awareness of their electricity consumption[20]. It is also important to note that the Commission measured awareness of consumption by asking consumers if they knew how much electricity they used in kWh – the research did not entail asking consumers to state their consumption and then independently verifying whether or not the amount stated was an accurate reflection of their actual usage. Similarly, Ofgem's own work with its Consumer First Panel found that "very few Panellists understood the concepts of low, medium and high users"[21], and its qualitative research on tariff comparability observed that "many consumers do not know how much energy they consume […] none of the participants had any idea how much energy they were consuming"[22].

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[19] Eg (daily standing charge*365)+(unit rate*annual consumption)

[20] ECME Consortium, 2010 (http://bit.ly/xzYQeq). EU average is 54% for consumption and 79% for amount paid.

[21] Ofgem, 2011 (http://bit.ly/xChPek)

[22] Ofgem, 2011 (http://bit.ly/xChPek)

24. We are also concerned about the message sent to consumers by an SER that decreases (ie becomes cheaper) as consumption rises. While this phenomenon is normal for tariffs with a standing charge, or 'falling block' tiered tariffs, under current tariff structures the average cost-per-unit differential between a typical low user and a typical high user can be a premium of as much as 23% and 15% on the low user's gas and electricity prices respectively[23]. An 'official' (ie Ofgem-approved) price comparison guide that communicates this information carries two clear risks:
    - confidence that pricing is fair for all users will be undermined; and
    - energy efficiency is presented as becoming less cost-effective the more energy you use.

Discounts

25. In order to develop a clear understanding of the relationship between cost and consumption that enables effective decision-making about switching and efficient usage of energy, consumers should be able to refer to a unit price that accurately reflects their consumption at any given time. This is even more important given the increasing prevalence of devices that communicate this information to consumers, such as clip-on energy monitors[24] and In-Home Display (IHD) units for smart meters.

26. We consider that tariffs with discounts that are only paid to consumers that remain on the tariff for a specified period of time (typically 12 months) obscure this crucial link between cost and consumption. For example, Npower's Sign Online 25 Electric tariff[25] has two different unit rates depending on whether or not the discount is included (which, in turn, depends on whether the consumer remains on the tariff for the full 12-months) – the 'published' rate of 10.33p/kWh and a '12-month effective' rate of 9.10p/kWh. On top of this, under RMR Core, there will be a third rate – the SER – which will be calculated on the basis of the residual cost of the tariff once the regulated standing charge has been subtracted.

27. Some discounts result from a particular consumer course of action that has a specific financial benefit for their supplier (eg paying by direct debit increases working capital and reduces bad debt risks). It is therefore difficult to justify the financial benefit being withheld from the consumer for periods of up to a year, and doubly difficult to justify allowing it to function as a de-facto cancellation charge. We maintain that a 'fair' discount would be deducted from the unit price 'at source'.

28. Indeed, by stipulating that there should be a separate standard tariff for each payment method, Ofgem strongly implies that it considers that it should be entirely possible for suppliers to factor their direct debit discount, which is generally the most substantial discount they offer, into their unit rate. Our analysis of price data published by Consumer Focus for a typical region[26] suggests that the average saving from switching from a

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[23] Analysis by Which?.

[24] A survey of 1,410 Which? Connect members in November 2011 found that about a quarter said that they now have an energy monitor and 63% said it had helped them to understand their electricity usage. In our most recent test of energy monitors (*Which?*, February 2012), our researchers advised readers that: "[Y]ou're unlikely to be able to use the costs provided by your energy monitor as an accurate estimate of your bill. Many tariffs are complex, featuring standing charges and tiered rates, plus quarterly or annual discounts. Energy monitors typically just allow you to enter your unit rate."

[25] Figures are for a consumer in the London area with medium consumption (3,300kWh/year).

[26] Consumer Focus price sheet for London Electricity Region, published 20 February 2012 (http://bit.ly/zVzw2E)

standard quarterly cash/cheque (QCC) tariff to a standard direct debit tariff is around £100. According to projected annual prices on currently available tariffs, a further £60 can apparently be saved by switching to an online direct debit tariff, although the actual saving over the lifetime of the tariff may be substantially lower due the use of 'capped' discount structures on certain fixed-term online tariffs (see above)[27].

Implementation costs

29. In the RMR Impact Assessment (IA) Ofgem correctly highlights the potentially "substantially greater implementation costs" of a single tariff structure for suppliers. However, as with the vast majority of observations in the IA, this is not underpinned by the rigorous cost-benefit analysis that we would expect from an economic regulator and is therefore difficult to accept at face value.

30. Additionally, as we have previously stated to Ofgem, private costs, incurred for example by a company introducing new systems or redesigning products to meet regulatory requirements, are invariably easier to quantify than the wider benefits to the economy as a whole from improving consumer access, choice and information. At present, these barriers impose an externality on consumers and the economy that results from the weakness in effective competition between energy retailers. Moreover, we believe these costs, as well as any disruption to consumers, could be minimised through the use of derogations, such as grandfather clauses. We note that as part of the Warm Homes Discount obligation this approach is being used to manage the phasing out of legacy social tariffs and the smooth migration of consumers on those products to alternative arrangements.

Innovation

31. Ofgem voices concern in the IA about the significantly greater restrictions that a single tariff structure would place on innovation, particularly the scope for suppliers to design tariffs that would attract consumers from their current supplier and sustain effective competition over time. There is, of course, an alternative view of effective competition, particularly relevant to a commodity market, that entails a level of price transparency that obliges companies to match the best prices on offer in order to retain enough customers to stay in business. However, in order to justify this particular position, Ofgem should set out explicitly where it believes that innovation has been promoted by not setting restrictions on tariff structure. Our reading of the IA suggests that Ofgem sees discounts and "additional features", such as loyalty points, boiler services and energy efficiency assessments, as examples of innovation that have already benefited competition and, therefore, consumers. Looking forward, Ofgem is also concerned that suppliers should retain the ability to offer innovative tariffs in response to "technological developments".

32. Regarding the development of tariff innovation under market competition thus far, we remain unconvinced about how much consumers have benefited from the examples of innovation cited by Ofgem in the IA. As we state above, discounts that are credited in arrears obscure the unit price and can present significant opportunity costs to consumers in some situations. For example, an excessive price increase or instance of bad customer

[27] The true value of promotional online discounts can only be calculated over the lifetime of the tariff – something that is not possible using the 'static' price data provided by Consumer Focus.

service may prompt a consumer to switch, but the prospect of 'losing' their discount may give cause to reconsider, potentially weakening their role in the competitive market. Furthermore, the use of different discount structures by different suppliers increases the complexity of price offers, enhancing the ability for suppliers to conduct misleading marketing campaigns and depressing the ability of consumers to identify the most competitive offers. Tellingly, Ofgem's own consumer research on tariff comparability found that the exercise that most closely reflected current, non-standardised tariff structures ('Option Z') was "notably less successful at helping consumers to identify the cheapest tariff available"[28].

33. Regarding the "additional features" of tariffs that are not directly related to the commodity product, it is not clear to us how the structure of a tariff would affect a supplier's ability to offer these products and services. The behaviour of suppliers in this regard reinforces this view. For example, the market leader, British Gas, offers two additional features – its EnergySmart energy monitoring service[29] and its EnergyExtra 50 home repair service[30] – as optional extras at the same price and with the same terms and conditions on all its tariffs. We believe that Ofgem's proposed Tariff Information Label will enhance the transparency and comparability of such offers.

Dual fuel tariffs

34. We understand that Ofgem is concerned about the effect that the uniform pricing structure we have proposed would have on suppliers' ability to offer dual fuel tariffs. Under Ofgem's proposals dual fuel tariffs would not be available on standard tariffs, due to a concern about dual fuel 'discounts' that involve the cross-subsidisation of the price of one fuel with revenues from another and "remove a consumer's ability to tell whether a supplier is offering both the cheapest electricity and cheapest gas in the market". If Ofgem does not believe that dual fuel 'discounts' are cost-reflective (and, by implication, may confer a benefit on dual fuel customers that is not available to electricity only customers[31]) then, in line with its requirement for cost-reflective pricing, then it would be logical to question whether such discounts should be allowed on non-standard tariffs.

35. While removing dual fuel discounts may frustrate consumers, it is worth pointing out that the average dual fuel 'discount'[32] for a typical direct debit and QCC customer on a standard tariff with one of the major suppliers is, respectively, just 1% (£13) and 0.7% (£9)[33]. As such, we believe that the loss of such a minimal dual fuel discount would be more than offset by improving the ability for consumers to identify the cheapest electricity and gas on the market, and we would expect suppliers to respond by competing to offer the best prices on both fuels. However, if suppliers are only able offer the best prices on both fuels to customers who take both fuels from them then our proposals would not stop them from making specific 'dual fuel-only' gas and electricity tariffs available. If

[28] Ipsos MORI, 2011 (http://bit.ly/ybTVAU)

[29] "EnergySmart™ - A free online service, it gives you accurate monthly bills and could help you cut your usage. Includes a free electricity monitor." (http://bit.ly/xVbRIw)

[30] "EnergyExtra 50 - Fixed-price (£99), one-off repairs for your home's gas central heating, plumbing, drains and electrical wiring - all for £3 a month." (http://bit.ly/xVbRIw)

[31] Ofgem's analysis indicates that on average the major suppliers earned significantly higher margins on their single fuel customers relating to their legacy business (ie gas in the case of Centrica, and electricity in the case of the others) than on either their dual fuel customers or on their single fuel customers relating to their non-legacy business.

[32] ie the difference between the average annual dual fuel bill and the sum of the corresponding annual single fuel bills

[33] Consumer Focus price sheet for London Electricity Region, published 20 February 2012 (http://bit.ly/zVzw2E)

suppliers wish to offer certain non-price benefits to encourage consumers to take more than one fuel from them then, again, our proposals would not prevent this. Indeed, this would be supported by Ofgem's proposed Tariff Information Label, which would help make such offers more transparent and comparable.

Smart metering and time-of-use tariffs

36. We see smart metering as the technological development that is most significant in terms of its potential to deliver innovative products, such as time-of-use (ToU) tariffs. If Ofgem considers that a single tariff structure is unworkable because it would hamper the development of such tariffs, further consideration should be given to the extent that ToU tariffs could be excluded from a single structure. Indeed, Ofgem has already stated that Economy 7 (and, by extension, other ToU tariffs) may require a different standing charge to single-rate tariffs, while the consumer research on Economy 7 has identified that multiple unit rate tariffs are inherently more complex and therefore demand a different, possibly more personalised, approach in terms of the presentation of price information.

37. One way of doing this could be to imagine the non-standard tariff market as three 'sub-markets' rather than one. One sub-market would offer fixed-term single-rate and E7 tariffs (eg fixed-price and online tariffs) with the same simple format as standard tariffs. Another would offer more complex ToU tariffs (including Economy 7 and variants), where suppliers set different unit rates depending on the time of day. A third sub-market would include 'tracker' tariffs, where variations to the price depend on fluctuations[34] in a published and transparent index that is not controlled by the supplier (eg the NBP for gas and N2EX for electricity). Suppliers could be required to inform consumers of the different types of tariff by adopting a common naming convention.

38. We maintain that for all single-rate tariffs, mandating a single tariff structure for each to improve understanding and comparability of offers would not be detrimental to innovation on this type of tariff. Suppliers could continue to offer the various permutations (online or offline, with a range of payment methods) of fixed- and variable-price tariff on a fixed-term basis that are offered in the current market. The proposed Tariff Information Label would support this by providing greater transparency on the value of any beyond-the-meter or non-energy services that suppliers may choose to integrate with their commodity product.

39. Most importantly, single-rate tariffs are likely to remain the choice of a substantial majority of the 85% of households who currently have one for many years to come. In its latest smart meter impact assessment, DECC assumes take-up of ToU tariffs to be just 24% of domestic consumers by 2030.

40. In summary, we support the development of innovative ToU and tracker tariffs and recognise the beneficial impact that harnessing demand response through such tariffs could have on meeting carbon, security of supply and economic objectives. However, we do not believe that rejecting fundamental reform of mainstream products and the demonstrable benefits that this will bring to consumers can be justified on the basis of preserving the ability for suppliers to innovate on what will remain a niche product segment in the medium-term.

[34] The frequency at which changes in the index (eg daily, monthly) were reflected in changes in the tariff price would depend on consumer preference.

Standardised element

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

41. We intend to respond to the standardised element consultation by the deadline of 2 April 2012. As there are a number of questions in that consultation that cover similar issues to Question 2 of this consultation, our full position on the standardised element and the cost elements that it should incorporate will be presented in our response to the standardised element consultation.

42. In its recently published consultation on the standardised element of standard tariff Ofgem has departed from its previously-held view that the vast majority of network costs are fixed costs and should, therefore, be recovered as a fixed 'per customer' amount through the standardised element. It now considers that all gas network costs and all but a small element of the electricity distribution charges should be recovered volumetrically through the unit charge.

43. Broadly speaking, we welcome the proposal that the majority of network costs should be recovered through the unit charge, on the basis that this has been judged to be more cost-reflective. We have previously expressed concerns about the impact that high standing charges can have on low users, who are more likely to be in lower-income groups[35]. We therefore believe that removing the bulk of network costs from the standing charge is a more progressive approach to cost recovery.

44. However, given our previous position that <u>only</u> network costs recovered on a per-customer basis should be included in any standardised element, the proposed exclusion of the vast majority of network charges from the standardised element leads us to question whether there should be any standing charge at all.

45. We remain firmly opposed to the inclusion of any 'contestable' costs – such as the costs of environmental and social policies, metering and other supplier operations - in the standardised element. This implies that they are non-contestable pass-through costs that are beyond the control of the supplier, when, in fact, this is not the case. By including these costs in a standardised element that would be the same for all suppliers, Ofgem is effectively attempting to allocate a non-contestable cost to a contestable cost driver. We are concerned about the distortions to consumer behaviour and supplier incentives that this could have.

46. Firstly, it has a behavioural effect on consumers by segmenting or justifying (and therefore legitimising) in the minds of the consumer that some costs – or, at least, the *level* of some costs - are simply inevitable.

47. Secondly, it introduces the idea of a nominal 'target spend' for supplier obligations that are actually output (eg carbon saved) rather than input measured and undermines the efficiency benefits to consumers of delivering these policies and services through competition.

[35] DECC, 2011 (http://bit.ly/zCM9RG)

48. On the proposed inclusion of environmental policy costs specifically, recovering these costs as a fixed amount through the standardised element is not consistent with the 'polluter pays' principle and, as such, is environmentally regressive. This is a position supported by the Fuel Poverty Advisory Group (FPAG) and the Association for the Conservation of Energy[36].

Information remedies

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

49. It may be something of a leap of faith to assume that making comparisons between tariffs easier will result in more effective engagement with the energy market. As we set out in Section 2, complex pricing is just one of several reasons that consumers are disengaged.

50. Nonetheless, compared to other barriers, we consider that resolving tariff complexity should be one of the easier challenges to overcome. As such, we believe that the decision to focus the RMR on complex pricing is appropriate. However, as stated in our response to Question 1, we think Ofgem could – and should - go further in its tariff reforms. By extending its proposed structure for standard tariffs to all tariffs, it could eliminate many – if not all – of the problems we have identified with the proposed price comparison guide as an information remedy, namely:
    - it is too dependent on consumers knowing how much energy they consume – something that is not evidenced by consumer research;
    - Ofgem's decision not to place any restrictions how suppliers structure discounts on their tariff could mean that the 'real' price of a tariff (as communicated by the SER) is obscured; and
    - it risks sending the wrong messages about fairness and energy efficiency.

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

51. As we have stated, we consider that poor awareness of energy demand among consumers will undermine the usefulness of the proposed price comparison guide. We believe that consumers should be able to make comparisons between competing products on the basis of the 'lowest common denominator', ie the unit price provided in p/kWh. While there is an argument that consumers will be indifferent to price differences expressed in pence and may need to see the value of switching demonstrated in pounds in order for it to be more tangible, consumer behaviour in other markets (eg supermarkets, petrol) would suggest that consumers do respond effectively to prices, or, more accurately, price differences, presented in pence terms. Moreover, given that unit rate comparisons should increase the range of media that will be able to report tariff information, and that the obvious way for these information providers to present tariffs to price-driven consumers will be as some kind of price ranking, we would expect consumers to rapidly become more aware of tariff prices and how to distinguish between them.

52. That said, in order that the benefits of switching are made as clear as possible to all consumers, we do not object in principle to the presentation of prices in £/month. However, we would suggest that Ofgem presents prices in such a way that pre-eminence is

[36] ACE, 2011 (http://bit.ly/zZBXYl)

given to the unit price due to our aforementioned concerns about consumers' awareness of their consumption and ability to correctly identify if they are a low, medium or high user. We also believe that Ofgem should assess through consumer research the presentation of prices as £/mWh as proposed by EDF Energy in its first-stage response to the RMR, as this would appear to retain the benefits of the unit price approach, with the additional advantage that prices – and therefore savings – would be 'inflated' and therefore be more tangible to those consumers who are indifferent to p/kWh pricing.

Proposed exceptions

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

53. We agree with the proposed exceptions for legacy and social tariffs.

54. It is difficult for us to comment on the proposed exceptions for extremely high users, given the lack of information about possible eligibility criteria and the proportion of consumers that would be affected under each of the criteria. Although suppliers may need to protect themselves from the greater risks associated with extremely high consumption customers, as a general position we are not concerned about energy suppliers' ability to make money on *every* customer. This does not happen in other sectors yet businesses continue to prosper (eg due to successful diversification into other products and markets).

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?

55. Yes. Research suggests that engagement in the energy market at an environmental level is extremely low, with very few consumers influenced by environmental factors in their choice of supplier and/or tariff[37]. As such, we do not believe that allowing suppliers to offer a green standard tariff and the further complexity that this could potentially introduce would be a proportionate response to the level of interest in this type of tariff.

56. As Ofgem has decided not to mandate a uniform structure across all tariffs, we see the main benefit of RMR Core (beyond promoting simpler standard tariffs and enabling easier comparisons between them) as providing a clear 'default' option or 'tariff of last resort' for consumers who have not actively engaged with the market following expiry of a fixed-term non-standard tariff. Accordingly, the number of tariffs in this segment of the market should be limited to one per payment method to ensure absolute clarity over which tariff consumers will be transferred to in the event of not choosing a new fixed-term non-standard offer. We concur with Ofgem in our expectation that suppliers currently focused on offering green/renewable tariffs will offer what is effectively a green standard tariff following implementation of RMR Core.

Price guarantee

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?

[37] Ipsos MORI, 2011 (http://bit.ly/oGeDnn). 1% of consumers cited 'to switch to a greener tariff' as the reason the last time they switched their supplier.

57. A price guarantee for consumers switching to a standard tariff has a number of attractions, and is something that we have asked Ofgem to implement in the past. However, with in the context of RMR Core, we are mindful that what would in effect be an individual price guarantee for every consumer could undermine the simplicity of the RMR Core proposal.

58. For example, under a price guarantee the unit price on *Supplier X's* standard tariff for *Consumer A*, who is benefiting from a price guarantee, may differ from the 'published' unit price on the same tariff being offered by *Supplier X* to prospective *Consumer B*. In this situation, if *Consumer A* were to make a compare *Supplier X* and *Supplier Y's* standard tariffs within the price guarantee period, in order to make an accurate comparison and informed decision they would require the unit rate at the time they signed up rather than the current unit rate. In 2009, our independent price comparison service, Which? Switch, reported one supplier to the Consumer Focus Confidence Code for its policy of not distinguishing between differently-priced versions of the same tariff in the tariff name[38]. Our view was that giving the same name to a tariff with a number of different rates would make price comparisons very difficult and could lead to poor switching decisions. We see clear parallels between this situation and what could happen were a price guarantee to be implemented for standard tariffs under RMR Core.

59. As Ofgem correctly notes, under SLC 23 consumers on variable-price tariffs are already protected by a 30-day price guarantee that takes effect following the announcement of a price increase. We would recommend that this protection is underpinned by making it incumbent on suppliers to be clear and upfront in their price increase notification communications about the consumer's right to switch and what the consumer should do in order to avoid having to pay the higher rates.

Section 4: Strengthen Probe remedies - domestic
Bills and annual statements
Price increase notifications
Confidence Code for price comparison services
Complaints

Bills and annual statements

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

60. Yes, but with qualifications. We have long maintained that bills and, by implication, the more recently introduced annual statements are functional documents and would benefit from increased standardisation across suppliers in terms of language and format used, and have been calling for the introduction of a summary box on bills since 2008. We therefore welcome Ofgem's recognition that "consistency between different customer communications allows consumers to become more familiar with such information and makes it easier for them to understand the details provided", although we would also question why it has taken the regulator so long to arrive at this position.

61. We therefore consider that Option 3 is an appropriate response to the problems caused by poorly designed bills and are pleased to see the depth of consumer research that has been

[38] Which?, 2009 (http://bit.ly/w8yvjb)

carried out by Ofgem to support this proposal. However, as with the information remedies proposed for RMR Core, better information will not necessarily translate into better engagement with the energy market. As Consumer Focus pointed out in its recent research on energy bills, there are a number of endemic and topical features of the energy market that at best act as barriers to engagement and at worst lead to a loss of confidence and disillusionment.

62. We are currently engaged in discussions with Consumer Focus, DECC and the ERA about reviewing the regulatory requirements on energy bills, with a view to exploring whether any of the current information could be safely removed (linked to the Red Tape Challenge). This is an area where we would like to work jointly with Ofgem to ensure any proposed changes to energy bills can be implemented at the same time as the wider RMR changes to bills and annual statements. Consumers consistently tell us that they do not understand bills, simplification is long overdue.

63. While simplification and standardisation of bills is likely to improve the consumer experience, an important point missed by Ofgem is that a key factor in the simplicity of a bill is the simplicity of the product that is being billed for. Our recent investigation into energy tariffs found that just one out of 36 numerate and literate consumers was able to correctly calculate the annual cost of one of the major supplier's tariffs[39]. This raises wider questions about consumers' understanding of the way that energy tariffs 'work' and therefore their ability to use their bills to check that they have been billed for the correct amount. On the other hand, significantly more consumers were able to calculate the annual cost of simpler tariffs from two of the smaller suppliers – indicating the difficulties that consumers have with complicated tariff structures that include features such as tiers, standing charges and discounts of the type described in our response to Question 1. As such, it should be a concern for Ofgem that its efforts to make billing simpler for consumers may be undermined by the complex and confusing tariff structures that suppliers will still be allowed to offer under RMR Core.

64. We welcome the inclusion of the commitment under Option 2 (which would apply to Option 3) to "outline how any premium or discount the consumer received relative to their supplier's standard direct debit tariff should be displayed". As Ofgem will be aware, last year, as part of the Billing Stakeholder Group chaired by John Baron MP, a majority of the members of the Group came to an agreement on how this information should be communicated to consumers on bills. The general consensus was that it should be prominently positioned, use standardised wording and provide a premium or discount figure that is personalised to the extent that it reflects the actual consumption (or the supplier's best estimate of consumption) of the individual to whom it is directed. Given its research findings and suppliers' apparent billing system constraints, the ERA maintained a preference for a more general savings message at the time.

65. We understand that Ofgem is currently minded to only include this information on consumers' annual statements. This appears to be because Ofgem intends to reduce the absolute amount of information on bills to increase engagement with them. Accordingly, adding a cheapest tariff message would detract from this objective as it is not essential information. While this position seems reasonable, we would make a number of points.

[39] Which?, 2011 (http://bit.ly/yehacv)

66. Firstly, annual statements have not been a resounding success in terms of their ability to increase consumer engagement. We hope that the proposed changes to annual statements, such as greater prescription of language and format and the requirement that they are sent out separately to bills, will increase the usefulness of this communication to consumers. Nonetheless, putting this information on annual statements means that there is just one opportunity per year to communicate it to consumers. If it were included on bills, this would increase to four (for most suppliers). If consumers continue to ignore annual statements then there is a risk that this initiative will fail.

67. Secondly, consumers' attitudes to bills (and therefore the rationale that this information should not be provided on bills) are a formed on the basis of bills as they currently are - poorly designed and cluttered with significant variation between suppliers.

68. Finally, if consumers say they want to receive this information (as Ofgem's Consumer First Panel report would suggest), we should look to see if the RMR proposal to include a standardised summary box on bills does increase engagement. This should be monitored by Ofgem should through the Consumer First Panel and other appropriate workstreams. If engagement does improve then Ofgem should re-examine whether cheapest tariff information should be included in the summary box.

Price increase notifications

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")?

69. Yes, but with qualifications. We strongly support the principle underpinning Ofgem's proposal that consumers should receive timely and unambiguous information about disadvantageous changes to their energy supply contract(s). While price increases by energy suppliers are a source of high media interest, the non-linear price structures used by virtually all suppliers mean that 'headline' price increases, which usually describe the increase to a the bill of a 'typical consumer', may give little indication of the actual impact on an individual customer's bill, unless that customer's consumption profile happens to fit that of a typical consumer. For example, a supplier that announces a price increase of 10% on a tariff but chooses to apply the majority (or even all) of that increase to its standing charge rather than its unit rate will increase the bills of lower users on that tariff more than the bills of higher users – an outcome that would not be communicated by a headline price increase. It is therefore essential that consumers receive a personalised statement of the true impact of a price increase on their own energy costs.

70. With regard to the proposal not to prescribe "a format for those variations that do not relate to unit rates or standing charges", Ofgem should consider that certain suppliers' practice of treating discounts as separate from the fixed or variable elements of their tariffs (a practice that would be eliminated under our proposals for tariff reform) means that any reduction in the amount of that discount (or a change to the way that discount is calculated that results in a reduction in its value) could have a considerable impact on the price paid by the consumer.

71. An increase from the current 15 working days to 30 working days is welcome. However, we would question why Ofgem intends to set any restriction at all on the amount of time it should take for the new supplier to contact the current supplier to inform them that

they are taking over a consumer's supply in order that that consumer will not be disadvantaged by a variation to their contract terms. Ultimately, as long as the consumer has agreed a contract with the new supplier before the date the variation takes effect they have fulfilled their obligation and should not be penalised as a result of poor or ineffective communication between suppliers that is outside of their control.

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.

72. Yes. We believe the format and content proposed for the standardised table is appropriate.

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

73. Yes. We support Ofgem's view that price increase notifications should not be treated as a marketing opportunity by suppliers.

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.

74. Regarding the requirement for "an explanation of the key reasons for the increase in charges", we are concerned about an increasingly common approach to explaining price increases that entails framing the increase in the context of a change to a supplier's underlying cost base (eg "wholesale market prices", "global commodity costs", "weak currencies" and environmental and social policy costs). Not only are these cost increases extremely difficult for consumers to validate and accept at face value, we also believe that this approach is unhelpful because it gives the impression that some costs are 'pass-through' and therefore unavoidable. This may lead disillusioned consumers to conclude that all suppliers in the market will be affected by the same cost increases, and that, ultimately, there is little point in switching. We illustrate this point with the following opening paragraphs from recent communications sent to customers of British Gas and Npower:

"You may have seen in the news recently, world oil and gas prices are rising – an issue facing all energy suppliers. This means that the cost of supplying gas and electricity to you home has increased in the last few months and may continue to rise. Unfortunately, as a result we have to increase our prices."[40]

"You may have heard that we're changing our prices, so we wanted to let you know how this affects you. With reduced quantities of North Sea gas, we now buy more energy on the global wholesale market. World events are pushing up these prices and distribution and network charges are also increasing. This is affecting all energy suppliers in the UK."[41]

[40] Letter from British Gas, "Good News – your prices won't be increasing", July 2011

[41] Letter from Npower, "Keeping you informed about your energy prices", 16 August 2011

75. Fundamentally, in a competitive market consumers should be concerned only with end user prices and the quality of the product or service provided. Costs, on the other hand, should be the preserve of the managers of firms. Ultimately, as a consumer organisation we are interested less in the excuses or justifications for price increases given by businesses and more with the impact upon consumers. It is clear that consumers do care – and, indeed, are worried about the increasing cost of energy; whether they feel empowered by the market to avoid these increasing costs is, on the other hand, highly debatable. As such, Ofgem should consider not only whether requiring suppliers to explain a price increase is necessary, but also whether it may inadvertently exacerbate consumer disillusionment and disengagement with the market.

76. The requirement for the price increase notification to contain a clear title that relates to the increase in charges is welcome. However, Ofgem should consider extending this requirement to ensure that this information is communicated clearly on the outside of envelopes and in the subject line of emails containing price increase notifications. This will reduce the risk (acknowledged by Ofgem) that consumers will discard or ignore the communication.

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

77. We have no further views on these issues.

Confidence Code for price comparison services

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.

78. We believe that Ofgem is the appropriate body to take over responsibility for the Confidence Code following the abolition of Consumer Focus in 2013. We agree that a number of strategic benefits would be leveraged by Ofgem taking on this function, and, in addition, note that Ofgem is well-placed to draw on best practice from other national markets through the work of its European association, the Council of European Energy Regulators (CEER), on price comparison services.

79. We also consider that consumers would benefit from the integration of Ofgem's tariff information remedies into price comparison services – the replacement of largely ad-hoc information provided by suppliers with the Tariff Information Label, for example - and that this objective would be best achieved through Ofgem having responsibility for the Code.

80. Ofgem should investigate ways to address the current low usage of price comparison services through the Code. Use of these services remains a minority activity - just a fifth of gas consumers and a quarter of electricity consumers said they used one last time they switched.[42]

81. Furthermore, while some price comparison services offer telephone access, they are generally directed at online consumers, thereby excluding almost one in four (largely

[42] Ipsos MORI, 2011 (http://bit.ly/oGeDnn]

lower-income) households.[43] We recognise that making telephone access a condition of accreditation to the Code would add substantial costs to businesses currently in this market, possibly making some of them unviable. However, one option may be to require this of providers above a certain turnover threshold to provide a minimum level of telephone access, if only on a call-back basis.

82. Ofgem should also look at raising awareness of the Code among consumers. While we would prefer to see market improvements delivered through self-regulation, in this case the Code, we are concerned about low levels of awareness. Research by Which? in 2009 found that the Code was recognised by just 2% of consumers[44]. If the instrument of self-regulation is not readily recognised by consumers then it immediately lacks the fundamentals of effective self-regulation, ie:
    - a clear incentive for a provider to seek accreditation in the first place; or
    - a clear incentive to comply with the instrument if accreditation is deemed worthwhile (ie the value of accreditation to companies rests largely on consumer recognition of that scheme and the reputational damage that could result from public sanction by the scheme or even expulsion).

83. More generally, the ability of price comparison services to provide an accurate estimate of the savings from switching supplier depends fundamentally on the consumer knowing the name of their current supplier and tariff and their annual consumption in kWh for each fuel. However, research by Consumer Focus suggests that 57% of electricity consumers[45] do not know which tariff they are on and how much they pay per unit[46], while research by the European Commission found that only 36% of UK consumers have a reasonable level of awareness of their electricity consumption (awareness of amount paid is higher at 65%)[47]. Similarly, Ofgem's own qualitative research on tariff comparability observed that "many consumers do not know how much energy they consume […] none of the participants had any idea how much energy they were consuming"[48]. These factors are likely to undermine the usefulness of information provided by price comparison services. Furthermore, the requirement for consumers to obtain copies of their bills or their annual statement before providing this information imposes a further search cost on consumers.

84. Through its development of the Code Ofgem should therefore look at ways to encourage providers to minimise these search costs, eg:
    - requiring accredited providers to offer simple consumption estimation calculators for consumers that do not have this information to hand and to require that these tools are underpinned by a common methodology to ensure consistency of quotations across providers; and
    - encouraging use of participation in midata/ 'no bill switch' projects so consumers can permit price comparison services to obtain annual consumption and tariff information held by their supplier.

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[43] ONS, 2011 (http://bit.ly/yazWCu). 77% of GB households had internet access in 2011.

[44] Which? survey of 7,883 online panellists between 9th and 30th November 2009.

[45] We anticipate that these findings would also be reflected in an equivalent sample of gas consumers.

[46] Consumer Focus, 2010; cited by Ofgem, 2011 (http://bit.ly/qWL1gz)

[47] ECME Consortium, 2010 (http://bit.ly/xzYQeq). EU average is 54% for consumption and 79% for amount paid.

[48] Ofgem, 2011 (http://bit.ly/xChPek)

85. A further issue is that the prices quoted by price comparison services for certain tariffs may not give an accurate representation of actual costs because they are based on a calculation that assumes that the consumer remains with the respective supplier for a 12 month period, throughout which their consumption will be evenly distributed. If any of these assumptions does not hold, the price actually paid by the consumer can be significantly different to that quoted by the price comparison service. As Consumer Focus has pointed out in a public letter to Ofgem, British Gas has a discount that cannot be realised by typical medium and high users due to the fact that their consumption will vary seasonally (a factor not accounted for by price comparison services)[50].

86. Consideration should also be given to how price comparison services account for other anomalies that result from the ways that some suppliers structure their tariffs. For example, a consumer leaving an Npower dual fuel direct debit tariff in the 11th month would pay an additional £92 for their energy due to the supplier's policy of withholding its £100 direct debit discount until the 12th month.

87. Finally, taking ownership of the Code should also be used by Ofgem as an opportunity to address how price comparison sites display prices for tariffs where the supplier has announced a price change but that price change is yet to take effect. In such situations consumers using price comparison services currently see the 'old' (pre-price change) rather than the 'new' (post-price change) price. Depending on the direction of the price change, a price comparison service will either under- (price decrease) or overstate (price increase) the savings available, and could therefore mislead prospective customers. Furthermore, depending on the size of the prospective supplier's increase, the saving calculated by the price comparison service may actually turn out to be negative.

Complaints

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

88. In our response to the first stage of this consultation we voiced our concern that the level of information available about energy complaints handling is insufficient to determine how well the mechanisms[52] introduced by Ofgem in October 2008 are functioning in practice. We are therefore pleased that this subject has been given consideration at this stage and have focused our response to this question on this subject.

[50] Consumer Focus, 2010 (http://bit.ly/x7vcjG). The discount in question is based on Tier 2 consumption and capped at a quarterly level. A typical user will vary their consumption throughout the year, using less in the summer. Based on typical customer usage patterns, the actual discount is less than the savings quoted by British Gas' savings calculator on its website. The company's terms and conditions stated that the discount was 'up to' a certain amount but this should be made clear upfront so that consumers can make an informed decision.

[52] The Consumers, Estate Agents and Redress (CEAR) Act 2007 led to Ofgem introducing The Gas and Electricity (Consumer Complaints Handling Standards) Regulations, which came into effect on 1st October 2008.

89. Reliable, robust, and timely information on consumer complaints is a very useful indicator of consumer detriment and provides authorities and consumer advocates, such as Which?, with a rich source of intelligence to detect market problems and develop remedies. Complaints data can also be made available to consumers in summary form – commonly as 'league tables' or star ratings, as in the Consumer Focus model – to enable objective assessments of competing providers in a market on the basis of indicators such as the volume of complaints they receive and how well they deal with them. Indeed, Ofgem has recently stated that it sees the "provision of information to consumers to enable them to compare performance and make decisions on their choice of supplier as key", and that "appropriate benchmarking information will also help to motivate companies to further improve performance"[53].

90. In our view, the GB domestic energy sector *appears* to have the features of an effective complaints handling landscape, including recourse to an independent, fair, accountable, and (increasingly) efficient alternative dispute resolution (ADR) scheme if the complaints handling process operated by a consumer's supplier fails to deliver an acceptable and timely resolution.

91. The Customer Complaints Handling Report (CCHR) that Ofgem requires suppliers to publish may not be fit for purpose. At present, the CCHR amounts to a requirement to report a single figure absent of any context (eg. size of customer base) once every 12 months, detailing the number of complaints suppliers were unable to resolve by close of business the day after the complaint was raised ('Day+1'). This seems a fairly minimal requirement for such a critical indicator of performance.

92. Only recording complaints outstanding after Day+1 says nothing about how long suppliers are actually taking to resolve these complaints (if at all), nor does it reveal anything about the subject of the complaint. Given the fundamental principle that there should be easy access to an ADR scheme, it is very concerning that the CCHR does not provide any way to systematically monitor how the number of unresolved direct complaints[55] relates to the number of complaints assessed by the Ombudsman. A significant 'drop-off' between the number of unresolved direct complaints and the number of complaints seen by the Ombudsman could inadequate signposting to the ADR scheme – a factor in the fines following Ofgem's recent investigations into British Gas[56] and Npower[57].

93. We recently sought to obtain better information from suppliers about their complaints handling performance as part of our research for an investigation into energy complaints that was published in February 2012's *Which?*. In November 2011 we sent requests to all six of the major energy suppliers asking them for the following information for the period 1 October 2010 to 30 September 2011 in addition to the Day+1 figure that they are already required to report:
    - total number of complaints received; and
    - number of complaints remaining unresolved after eight weeks; and
    - number of complaints for which a 'deadlock' letter was issued.

[53] Ofgem, 2010 (http://bit.ly/A5dV0I)
[55] Direct complaints are complaints addressed to the company concerned.
[56] Ofgem, 2011 (http://bit.ly/vqjyA5)
[57] Ofgem, 2011 (http://bit.ly/rH6yrj)

94. In our view, the responses we received from suppliers point to a number of problems that demand urgent attention from Ofgem. The most fundamental of these is the material inconsistency between different suppliers in the interpretation of the term 'expression of dissatisfaction', which is the definition of a complaint that underpins the Consumer Complaints Handling Standards Regulations. Although most suppliers responded positively to our request and provided the information we asked for, the majority requested that we did not publish the data. This was on the basis that inconsistencies in interpretation and, therefore, recording of complaints meant the figures would be non-comparable and would not only be unhelpful, but also likely to mislead consumers.

95. To be useful, effective analysis of complaints data requires that data is collected by market participants using consistent definitions. If those collecting the data use different definitions and/or classifications when recording a complaint, making meaningful comparisons between different datasets can be a significant challenge, if not impossible.

96. As such, we question whether the CCHR has any value whatsoever, and would suggest that Scottish Power's failure to publish its report on time for two successive years is perhaps indicative of the low status accorded to the complaints reporting process. While Consumer Focus has continued to develop the more robust complaints reporting model established by Energywatch, it has elected to exclude direct complaints from it due to the aforementioned inconsistencies surrounding the complaint definition. We consider that a model intended to illustrate suppliers' complaint handling performance that does not take into account the vast majority of complaints actually made by consumers is somewhat flawed.[58]

97. Largely as a result of our intensive campaigning and lobbying activities, the Financial Services Authority (FSA) publishes a greater range of quantitative indicators on complaints to allow consumers and other external stakeholders to better judge the performance of providers in that sector. Importantly, the FSA, uses a similar definition of a complaint to that used in the energy sector[59] and also requires companies to record all complaints that are not 'resolved to the customer's satisfaction by the close of the business day after the complaint was made'[60]. However, the published data also shows the proportion of complaints closed within eight weeks as well as the proportion of closed complaints that are upheld (i.e. found in favour of the consumer). These are also broken down by product area (e.g. banking). As of September 2010, the FSA publishes aggregate and firm-level complaints data every six months. The most recent firm-level release[61] contained data on 167 firms (including several large groups of firms). While some of the data could be presented in a more helpful format, for example contextualising figures by size of

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[58] A second significant issue with the Consumer Focus model is that complaint ratios (complaints per 100,000 customers) are presented using a 'five star' rating scheme. While this is helpful as an indicator of relative performance, the way parameters for the star system (which effectively translates the calculated ratio to a 'score' of between one and five stars) have been set gives the impression that those at the top are performing well by an objective standard when in fact it is somewhat arbitrary. It may be better to simply rank suppliers by the ratio alone.

[59] 'Any oral or written expression of dissatisfaction, whether justified or not, about the firm's provision of (or failure to provide) a financial service which alleges that the customer has suffered (or may suffer) financial loss, material distress or material inconvenience' (FSA) vs. 'Any expression of dissatisfaction made to an organisation, related to any one or more of its products, its services or the manner in which it has dealt with any such expression of dissatisfaction, where a response is either provided by or on behalf of that organisation at the point at which contact is made or a response is explicitly or implicitly required or expected to be provided thereafter' (Ofgem).

[60] http://www.fsa.gov.uk/pages/Library/Other_publications/commentary/index.shtml

[61] 1st July to 31st December 2010

customer base[62], the FSA's system demonstrate that it is possible to establish a standardised complaints reporting mechanism in a market with a far greater number of firms offering a greater variety of generally more complex products than the energy sector.

98. Our vision for effective complaints handling reporting entails the following:
- Companies publish an enhanced annual CCHR segmented using the same complaint categories used by the Energy Ombudsman and containing the following indicators:
  - number of complaints opened;
  - number of complaints closed;
  - proportion (%) of closed complaints upheld
  - proportion (%) of complaints closed by close of business the following day;
  - proportion (%) of complaints closed within 8 weeks;
  - number of complaints assessed by the Energy Ombudsman; and
  - outcome of complaints to the Energy Ombudsman.
- The Ombudsman publishes complaints figures at firm-level as well as aggregate data.
- In response to the significant discrepancy identified in Ofgem's research where two fifths of complaints considered resolved by suppliers are not considered as such by consumers[63], suppliers should implement systems to ensure that complaints are only 'closed' on the consumer's say-so, thereby ensuring genuine satisfaction with the resolution.[64]

99. More generally, Which? believes complaints handling could be improved through the following measures:
- Suppliers provide all of the following information in a prominent position on bills and all complaint-related documentation:
  - The consumer has a right to use the Energy Ombudsman if the supplier cannot resolve their complaint to their satisfaction within 8/12 weeks;
  - The Energy Ombudsman is a free-of-charge service;
  - The Energy Ombudsman is an independent body;
  - The Energy Ombudsman's decision is binding on the supplier, but not the consumer; and
  - There are a range of forms of redress available through the Energy Ombudsman, including financial compensation.
- Ofgem follows the example of the FSA and bans prohibit multiple-stage complaints processes due to their inherent potential for misuse.[65]

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[62] This is a recommendation but not compulsory.

[63] Harris Interactive, 2010 (http://bit.ly/yVfeVy)

[64] This could entail a complaint handling policy that stipulates that a complaint can only be considered resolved for reporting purposes under the following circumstances:
(a) The supplier has sent a final response letter or email; and
(b) The supplier has received written confirmation from the complainant that they accept the internal resolution they have been offered; or
(c) The complainant has failed to respond to the firm within eight weeks of the initial written response.

[65] This is because it effectively gives firms an incentive to deal with complaints to a lower than satisfactory standard at the first stage on the basis that only a relatively small number of consumers will take their complaint further and the firm then has further chances to rectify any shortcomings in the original complaint handling. Which? has successfully called for multiple-stage processes to be abolished in financial services and the FSA has stated that it has not been convinced of the case for retaining the two-stage process on the basis of any benefits for consumers, indeed that "the feedback received supports [its] concerns that consumers do not pursue complaints after the first stage, partly because they remain unclear about their right to refer their complaint to the ombudsman service" (FSA, 2011, p16-19 [http://bit.ly/xFKfL3].

- Ofgem continuing its systematic monitoring of complaints handling practices through:
  - Annual research with consumers (eg Customer Complaints Handling Research prepared by Harris Interactive); and
  - Regular audits of suppliers' complaint handling practices.

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.

100. We have no specific views on costs and other implications, only to reiterate our earlier point that Ofgem should consider that private costs, incurred in this instance by a company introducing new systems, are invariably easier to quantify than the wider benefits to the economy as a whole from improving consumer access, choice and information.

Section 5: Standards of Conduct

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

101. Yes, but with qualifications. In our response to the first stage of the RMR we repeated our view at the time of the Energy Supply Probe that there was "no clear process for enforcement of the Standards [of Conduct] and no clear incentive for why energy suppliers would comply with the Standards". This view has not changed and, accordingly, we welcome Ofgem's proposal to make the SOCs a legally binding obligation via an overarching licence condition.

102. It is disappointing – although, for the reasons set out in the following paragraph, not entirely unexpected - that energy suppliers have not voluntarily implemented a set of principles that broadly reflect our minimum expectations of how any company should treat its customers.

103. Our qualitative research with consumers has reinforced our awareness of a pervasive and – in terms of effective market functioning – potentially dangerous mindset among consumers that there is little difference between the major energy companies that dominate the market. This is also borne out by the findings of our most recent energy supplier survey which puts the mean customer satisfaction score for the six major suppliers at just 46%, with a range of scores between 41% and 51%. While all but one[66] of the smaller suppliers tend to perform better in our survey, they are – with one notable exception[67] - less competitive on price (at least in terms of their ability to offer market leading deals), or do not compete on price at all.

104. These consumer attitudes are underpinned by a number of other factors. Firstly, the vast majority of consumers are unable to substitute gas and electricity for other sources of energy and 'opt out' of the retail energy market altogether. Secondly, a protracted switching process makes a 'vote with your feet' strategy less immediately harmful to energy suppliers (and therefore less attractive to consumers) as it might be to companies in other sectors. Accordingly, we believe that the commercial risks of poor conduct to energy suppliers are, at best, rather minimal.

[66] First Utility (customer score 44%)

[67] Ovo Energy

105. While we would generally agree with the assessment that regulation should be a last resort, we consider that energy suppliers have had every opportunity to improve their conduct voluntarily and have either opted not to, or have been unable to do so. Furthermore, we do not feel that making the SOC principles enforceable through an overarching licence condition imposes undue rigidity or inflexibility upon suppliers and their ability to design products and services that appeal to consumers.

106. Regarding the draft version of new SLC 1A, we seek urgent clarification from Ofgem as to why the transposition of the SOCs has resulted in the apparent deletion of Standards 1-4. We believe that it is as important today as at the time the SOCs were introduced that suppliers should not sell inappropriate products[68], not change anything about a product or service without providing the consumer with an explanation, prevent switching without good reason, or offer unnecessarily complex or confusing products. As such, these principles should also be reflected in the new licence condition.

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

107. Yes.

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

108. Yes.

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

109. No.

Section 6: Vulnerable consumers

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

110. The impact of RMR Core will depend fundamentally on suppliers' response to this intervention. Our view is that there is a very real possibility that suppliers may respond to RMR Core by focusing their attention on the 'unregulated' non-standard segment of the market and possibly inflating the cost of standard tariffs. If this happens then Ofgem's faith that disengaged (either through choice or lacking the necessary cognitive skills to engage) vulnerable consumers on standard tariffs will benefit indirectly from a 'ripple effect' from increased switching between standard tariffs by more engaged consumers may prove to be misguided. In this situation, we believe that the outcome of RMR Core for vulnerable consumers will at best be little change; at worst their bills may increase substantially.

111. There are likely to be vulnerable consumers who would like to engage but who, possibly due to limited literacy or numeracy, find the market too complex and difficult to

[68] We consider that obligating suppliers to provide "information that relates to products or services which are appropriate to the Customer to whom it is directed" (§1A.4.) does not offer the same level of protection as preventing suppliers from selling an inappropriate product or service.

navigate. We believe that our proposal to mandate a uniform tariff format for all tariffs would vastly increase their ability to evaluate alternative offers in the non-standard segment of the market and identify cheaper tariffs that could save them money. Ofgem's own research on tariff comparability supports this view: when presented with a range of tariffs with a fixed standing charge and a variable unit rate, vulnerable consumers were only slightly less likely than average ('all consumers') to be able to select the lowest-priced offer[69].

112. However, being able to identify the cheapest tariff in a controlled exercise does not mean that vulnerable consumers will be able to obtain the best prices in the actual market. Rising commodity prices are clearly the biggest challenge to an affordable supply of energy for all consumers, but this situation is exacerbated in the case of vulnerable and fuel poor groups by a retail market that effectively excludes the most competitive offers from those who would benefit most from them.

113. The so-called 'poor pay more' problem is most pronounced in the high price differentials between the methods of payment used most by vulnerable and fuel poor consumers – prepayment and QCC – and direct debit. According to the DWP's Family Resources Survey, some 4% of households are excluded from direct debit entirely through not having access to a transactional bank account[70], while a substantial number of households who could pay by direct debit may choose not to due to a concern that their finances are not stable enough to commit to a direct debit arrangement. As set out earlier in our response, online direct debit tariffs offer further savings, but the requirement for an internet connection to sign up, receive bills and manage accounts means these are less likely to be an option for the vulnerable and fuel poor.

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

114. Our immediate reaction is that the fact that Ofgem is considering a 'backstop' tariff priced relative to a basket of other tariffs as an effective price restraint for vulnerable and fuel poor consumers appears to undermine the argument that these disengaged groups will benefit from the increased competitiveness of standard tariffs under RMR Core.

115. However, were such an intervention deemed necessary, it would appear to address many of the concerns about market access for certain groups that we discuss in our response to Question 21. Nonetheless, we have a number of immediate concerns about introducing a backstop tariff. Given that such a tariff is unlikely to be cost-reflective, it would seem necessary to limit access to the product in order to limit the cross-subsidy from other consumers. The well-documented problems with effective targeting notwithstanding, applying any income-, age- or health-related eligibility criteria to a tariff would appear to give such a tariff the status of a social tariff – an intervention that is now being phased out in favour of the Warm Home Discount fixed rebate scheme. We also note that DECC considers social tariffs to be "inconsistent with the principle of competitive markets", because the offering by suppliers of different benefits to different groups of consumers "can make it difficult for consumers to compare and switch energy supplier to ensure they are receiving the best deal, and difficult for Government to reconcile costs[71]

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[69] Ipsos MORI, 2011 (http://bit.ly/ybTVAU)

[70] DWP, 2011 (http://bit.ly/xHuxfv)

[71] ie financial support with energy bills to fuel poor and vulnerable low income households.

between suppliers as they will depend on a number of variables including the level of tariff and level of usage"[72].

116. It may be that support for vulnerable and fuel poor consumers is not best delivered through specific market products, such as a social backstop tariffs, but through changes to the structure of mainstream tariffs. We are aware of at least two ways in which vulnerable consumers are unfairly penalised by current tariff structures.

117. Firstly, it is assumed that the costs of social policy obligations such as the Warm Home Discount (WHD), the Carbon Emissions Reduction Target (CERT) and the Community Energy Support Programme (CESP)[73], which are sized according to the number of customers a supplier has, are recovered by suppliers as an equal per-customer amount. This means that all consumers make the same contribution (estimated to be £29 per fuel per year) regardless of their level of energy consumption. Were these costs to be recovered through the unit rate, as we have advocated, they would better reflect the difference between the social and private costs of energy use. The close correlation between energy consumption and income means this would also be more progressive from a redistributive perspective. However, Ofgem would have to be mindful of the impact on a significant minority of low-income high-consumption households[74], meaning that funding the costs of such programmes through the tax and benefits system is another option that should be considered. This approach would offer the clear advantage of being able to relate contributions directly to income, although we appreciate that Ofgem may be constrained to collect such charges from energy consumers.

118. Secondly, as high standing charges penalise low users, Ofgem could also reduce the impact on vulnerable consumers (who are more likely to be low users) by ensuring that one of its policy objectives is to ensure that any regulated standing charge is kept as low as possible.

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

119. We do not have any views on which groups of consumers should receive additional support.

[72] DECC, 2010 (http://bit.ly/wTonxP)

[73] We consider CERT and CESP to be social policies because of the Priority Group and Super Priority Group elements.

[74] FPAG's analysis (unpublished) suggests that 1.4 million out of 4.8m low income consumers (those in the lowest two income deciles) have higher than average energy consumption, although 0.4m of these are only slightly higher.