

## **Deemed Contracts – Final report from Duty to Supply, Contracts and Information workgroup**

This document summarises the views of the Duty to Supply, Contracts and Information workgroup on the requirement for deemed contracts to be regulated in the supply SLCs. It reviews the following SLC:

### **SLC 28 - Deemed Contracts**

#### **1. Background to deemed contracts**

Schedule 2B paragraph 8(1) of the Gas Act and Schedule 6 paragraph 3(1) of the Electricity Act, respectively, provide that where a supplier supplies gas or electricity to premises or a consumer otherwise than in pursuance of a contract, the supplier shall be deemed to have contracted with the consumer for the supply of gas or electricity from the time when he began to supply that gas or electricity. Typically a deemed contract will occur where a customer moves into a new property and has not agreed contractual terms with a supplier who is supplying energy to that property or where a fixed term contract expires and there are no explicit provisions for terms and conditions for the period immediately after expiry.

The group notes that deemed contracts play a vital role in the energy market. The nature of supply is such that it would be inefficient, given current metering technology, to disconnect premises when a customer had moved out and reconnect the premises upon application for a contract by a new occupant. In addition, suppliers may not always be aware of customer movements until a period of time has elapsed after the event. A deemed contract therefore seeks to provide a sound and binding basis upon which suppliers will supply customers where a contract has not been expressly agreed. It also provides suppliers with a clear basis upon which to charge for that supply.

As by definition the terms and conditions of a deemed contract have not been expressly agreed between suppliers and customers, it is appropriate for these terms and conditions to be subject to regulation. In particular the charges levied under deemed contracts should not be unduly onerous and customers being supplied under deemed contracts should be free to access the competitive market and transfer to the supplier of their choice. On this last point, domestic gas and electricity customers on deemed contracts can still be objected to on grounds of debt where this meets the criteria set out under SLC 46 or Clause 16 of the MRA respectively. In the non-domestic market customers on deemed contracts can not be objected to for debt or on grounds specified in the contract.

Finally, there is a strong link between deemed contracts and the operation of the Supplier of Last Resort (SoLR) Arrangements. Where a SoLR is appointed then they will supply those customers affected on deemed contract terms. The SoLR arrangements are being reviewed separately by the Section B issues (inc. SoLR) workgroup.

#### **2. Review of SLC 28 – Deemed Contracts**

##### 2.1 Deemed contract charges

SLC 28(2) and SLC 28(3) restrict the level of charges that suppliers can levy under deemed contracts. They provide that such charges should not be “unduly onerous”.

Terms shall be taken to be “unduly onerous” if the revenue derived from supplying gas or electricity to customers on those terms:

- (a) significantly exceeds the costs of supplying gas or electricity; and
- (b) exceeds such costs of supply by significantly more than the supplier’s revenue exceeds costs of supply in the case of the generality of its domestic customers or non-domestic customers, as appropriate (except where customers are supplied in accordance with SLC 29 (Supplier of Last Resort)).

Competition is unlikely to deliver value for customers in this area and the group considers that it would therefore be prudent to retain regulation of deemed contracts. In particular customers have not expressly chosen to be supplied by a particular supplier on deemed contact terms.

However, it is considered that the obligations under SLC 28(4) are overly specific (for example, SLC 28(4) requires that charges must exclude costs associated with the promotional, marketing and advertising activities of the licensee).

Summary: **Retain** the principle set out under SLC 28(2) and SLC 28(3) that deemed contract charges should not be unduly onerous and that “unduly onerous” should be defined in the licence. **Remove** the specific requirement set out in SLC 28(4) for charges to exclude costs associated with promotional, marketing and advertising activities.

## 2.2 Access to deemed contract terms and conditions

SLC 28(5) requires a supplier to send a copy of their deemed contracts and revisions to such contracts to the Authority. The group considers that this requirement could safely be removed. The provision of information on deemed contracts to the Authority, energywatch and customers would be safeguarded by the retention of the obligation under SLC 28(6) to supply a copy of their deemed contracts to any person that asked. Given the uncompetitive nature of deemed contracts, transparency and access to terms and conditions is considered to be necessary.

Summary: **Remove** the requirement set out under SLC 28(5) to send the Authority a copy of deemed contracts or revisions to deemed contracts. **Retain** the principle under SLC 28(6) that a supplier should provide copies of their deemed contract terms to any person that makes a request.

## 2.3 Requirement for deemed contract to include terms required by SLC29 (Supplier of Last Resort)

SLC 28(7) sets out a requirement for the licensee to ensure that their deemed contracts include provisions required under SLC 29 when in relation to deemed contract supply under a last resort direction. The group considers that this obligation is not required and duplicates obligations set out elsewhere in the licence.

Summary: **Remove** requirement set out under SLC 28(7) to included terms required under SLC29 for deemed contracts in place under a last resort direction.

## 2.4 Customer information

SLC 28(8) provides that where a supplier supplies a customer with gas or electricity under a deemed contract, it shall use its reasonable endeavours to provide them with:

- a) details of the principal terms of that deemed contract
- b) written notice that contracts on terms other than deemed contract terms may be available and as to how information can be obtained as to any such terms, and
- c) if the customer is a domestic customer, an accurate summary of the principal terms of domestic supply contracts available to them.

As the customer does not expressly enter into a deemed contract, the group considers that it is appropriate for the supplier to make reasonable endeavours to provide customers with details of the principal terms of the deemed contract.

In recognition that deemed contracts are unlikely to offer terms to customers that are better than those that could be achieved under domestic supply contracts, the group also considers that it would be appropriate to inform customers of the availability of contracts (other than deemed contracts) and how they may obtain information about such terms (SLC 28(8)(b)). It was also agreed that it would be helpful to retain the specific obligation to provide this information in writing for future reference by the customer.

The group does not consider that there should be a requirement in the licence for the supplier to provide deemed contract customers with a summary of the principal terms of their domestic supply contracts that they would be prepared to offer the customer. It is in a supplier's commercial interests to enter into a domestic supply contract with the customer.

SSE and npower do not agree with the above proposal to retain SLC 28(8)(a) and SLC 28(8)(b). Given the provision in both gas and electricity for a deemed contract to have effect in the event that a customer has not entered into an express contract and therefore the customer's security of supply is protected, coupled with the obligation above that a supplier will provide copies of their deemed contract terms to any person on request and the fact that it is in all suppliers' commercial interests to enter into an express contract with the customer, we do not believe that it is appropriate to directly regulate this area further by specifying additional information provision requirements. We therefore believe that SLC 28(8) could usefully be removed from the licence in its entirety.

Summary: **Retain** the requirement set out under SLC 28(8)(a) to make reasonable endeavours to provide customers on a deemed contract with the principal terms of that contract. **Retain** the requirement set out under SLC 28(8)(b) to make reasonable endeavours to provide written notice to deemed contract customers that contracts on terms other than deemed contract terms may be available and how information can be obtained as to any such terms. **Remove** the requirement set out under SLC 28(8)(c) to use reasonable endeavours to provide domestic customers on a

deemed contract with an accurate summary of the principal terms of domestic supply contracts available to them.

## 2.5 Deemed contract required terms

SLC 28(9) provides obligations for suppliers to include set terms within their deemed contracts. These obligations reflect requirements stated elsewhere on suppliers with respect to contracts that customers expressly enter into and deal with:

- security and emergency arrangements (gas only),
- contracts to be terminable on appointment of a SoLR,
- security deposits,
- termination where a customer ceases to own or occupy a premise, and
- deemed contracts to be terminable at the point where a supply is taken under contract from the incumbent or new supplier

The group considers that it is sensible for deemed contracts to include all of the terms currently required. This provides protection for customers in key areas.

An alternative view was held by SSE. SSE believes that this SLC could be streamlined and simplified by removing SLC 28(9) and simply including deemed contracts within the wider definition of contracts in the licence. This would avoid the need to duplicate these requirements within SLC 28. This view was not agreed by the group but would be considered at the drafting stage.

SLC 28(10) allows suppliers to include additional termination provisions that do not derogate from those required in SLC 28(9). The group agreed that, whilst the intention of this paragraph was to be helpful, it was not needed within the licence. Further, if it was to be retained then redrafting would be required. SLC 28(10) of the electricity licence makes reference to SLC 29(17) which is not present in SLC 29 and SLC 28(10) of the gas licence makes reference to SLC 29(16) which appears to be wrong. In both instances the reference should be to SLC 29(15) which sets out the circumstances under which a deemed contract enacted under a last resort supply direction shall terminate.

Further, the licence is silent on whether suppliers should be able to charge termination fees for customers who are being supplied under deemed contract terms. The group considers that customers on deemed contracts should be free (subject to separate debt objection questions) to enter into contract terms. In particular the customer has not expressly agreed to enter into a contract which allows termination fees and suppliers should have a reasonable expectation, reflected in their charges, that deemed contracts will be a temporary feature of their relationship with a customer.

An alternative view was held by SSE and npower. They agree that it would not be reasonable to charge termination fees to customers supplied on deemed contracts. However, as they are not aware of any suppliers currently attempting to do this they do not therefore support additional obligations being added to the licence as part of this review where there is no evidence to date of any consumer detriment being experienced

in this area. This would not be consistent with the principles of best regulatory practice i.e. to be proportionate and targeted only at cases in which action is needed.

Summary: **Retain** the requirements for deemed contracts to include the terms set out under SLC 28(9). **Remove** the provision from the licence under SLC 28(10) that allows suppliers to include additional termination provisions that do not derogate from those required in SLC 28(9). **Add** a further obligation to the electricity and gas standard licence conditions to prevent a supplier from charging termination fees for customers who exit a deemed contract.

## 2.6 Estimating consumption

SLC 28(11) places a requirement on the supplier to act in a reasonable manner including the use of any available consumption data for the premises and other relevant factors when determining the kWh of gas or electricity taken. The group considers that in many instances an accurate actual start read for the deemed contract may not be available. It would therefore appear sensible to retain an obligation on the supplier to act reasonably in this instance. This test of reasonableness is additional to the rights of suppliers provided by the Acts to estimate consumption (Schedule 2B paragraph 8(9) of the Gas Act and Schedule 6 paragraph 3(8) of the Electricity Act).

SSE and npower hold an alternative view. They do not agree that the above licence obligations in relation to estimating consumption should be retained. The rights of suppliers to estimate consumption is provided for in the Gas Act 1986 and Electricity Act 1989 respectively. Suppliers have a commercial incentive to act reasonably in estimating consumption to ensure billing accuracy, avoid complaints, etc. and indeed are in the process of developing Billing Codes of Practice. Moreover, where suppliers fail to act reasonably in estimating consumption, customers have recourse to complain to Energywatch and the Energy Ombudsman (who will have powers to require appropriate redress to be made by the supplier concerned) and ultimately, to switch supplier. This area is therefore adequately provided for through primary legislation and is backed up by the competitive market and a number of voluntary initiatives established by suppliers.

Summary: **Retain** the requirements on suppliers under SLC 28(11) to act in a reasonable manner including, the use of any available consumption data for the premises and other relevant factors, when determining the kWh of gas or electricity taken.

## 2.7 Deemed contract following last resort supply direction

The group considers that SLC 28(12) provides clarity that where a deemed contract is in place as a result of a last resort supply direction, requirements on the level of tariffs and provision of information on standard deemed contract terms to customers in SLC 28 are not applicable. SLC 29 sets its own obligations on tariff levels and customer information.

Summary: **Retain** the clarification provided by SLC 28(12) that certain requirements (currently those set out under SLC 28(2) to (4) and SLC 28(8)(b)) do not apply where a deemed contract is in place following a last resort supply direction.

Note: a proposal by the group to retain an SLC does not prevent that condition from being considered for different (and better) drafting treatment under the SLR process.

AGREED