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Prepayment review: understanding supplier charging practices and barriers to switching

Report

Reference:	Prepayment review	**Contact:**	Karen Miller
Publication date:	23 June 2015	**Team:**	Consumer Vulnerability
		Tel:	0141 331 6046
		Email:	Karen.Miller@ofgem.gov.uk

Overview:

This review was prompted by concerns that prepayment customers can face particular barriers when trying to access competitively priced deals; notably fewer tariff choices, charges for installing and removing a prepayment meter, and upfront security deposits. Our social obligations monitoring indicates that prepayment customers have very low switching rates from prepayment to credit.

To better understand the issues in this area, and to ensure that that costs do not fall disproportionately on those least able to afford them, in February 2015 we issued an information request on prepayment to all domestic gas and electricity suppliers. This report is based on information provided by the suppliers who offer prepayment tariffs plus our own market analysis. The report outlines the key findings and proposed next steps of our review.

Context

Ofgem is the Office of Gas and Electricity Markets. We are the independent regulator of the electricity and gas system in Great Britain. Our principal objective is to protect the interests of existing and future energy customers. We have particular duties to safeguard consumers in vulnerable situations.

Our Corporate Strategy recognises that energy is an essential service for health and participation in society, which requires a regulatory approach that reflects this importance. This review helps to deliver three of our strategic outcomes for customers – better social outcomes, quality of service, and lower bills and costs than would otherwise be the case.

Our Consumer Vulnerability Strategy (CVS) was published in July 2013. Its overarching aims are to protect and empower customers in vulnerable situations, so as to reduce the likelihood and impact of vulnerability and ensure all customers can access market benefits. In 2014 we identified prepayment as a priority area for our CVS.

This review was prompted by concerns shared by consumer representatives and other stakeholders that prepayment customers can face particular barriers when trying to access competitively priced deals: fewer tariff choices, charges for installing and removing a prepayment meter, and upfront security deposits. It marks the next phase of work to support prepayment customers and follows on from our recent work with DECC to improve the take-up of energy bill rebates by prepayment customers, and improvements to the Debt Assignment Protocol (DAP) which will make switching easier for prepayment customers with an energy debt of up to £500 per fuel.

The findings of this report also relate to our work on supplier objections, faster switching and smart metering.

Associated documents

Decision document - Debt Assignment Protocol
https://www.ofgem.gov.uk/publications-and-updates/decision-make-modifications-gas-and-electricity-supply-licences-reform-switching-process-indebted-prepayment-meter-customers-debt-assignment-protocol

Decision to make a market investigation reference in respect of the supply and acquisition of energy in Great Britain
https://www.ofgem.gov.uk/ofgem-publications/88435/stateofthemarket-decisiondocumentinofgemtemplate.pdf

Payment differentials roundtable report
https://www.ofgem.gov.uk/ofgem-publications/94274/energydebate-topublish-pdf

Supplier objections – call for evidence
https://www.ofgem.gov.uk/publications-and-updates/supplier-objections-call-evidence-0

Supplier performance on social obligations
https://www.ofgem.gov.uk/about-us/how-we-work/working-customers/supplier-performance-social-obligations

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Executive summary

More consumers than ever are using prepayment to pay for their energy bills (15%)[1]. Although not all prepayment customers are financially vulnerable, they are disproportionately on low incomes[2] with more than 60% of prepayment meters installed due to debt[3]. One estimate suggests that more than a third of households with prepayment meters have one or more individuals with a long-term physical or mental health condition or disability[4].

It is important that prepayment customers can access competitively-priced deals and are treated fairly. It is worth noting that, while the majority of prepayment meters are installed due to debt, around just 7% of electricity prepayment customers and 10% of gas prepayment gas customers are currently in debt to their energy supplier[5]. We want to ensure that prepayment customers can not only switch to another prepayment deal, but where appropriate, to another payment method to access better deals.

Key findings
Our review identified:

- There are substantial savings available for prepayment customers who are able to switch. Customers on a standard variable tariff (SVT) (the most common tariff) can save up to £300 a year if they switch to the cheapest direct debit (DD) tariff and up to £66 a year if they switch to the cheapest prepayment tariff in the market – this includes fixed tariffs[6].

- Prepayment meter customers are now switching supplier at comparable rates to direct debit customers. However, the proportion of prepayment customers who have never switched supplier remains lower than for DD customers[7] and there are still very low rates of switching from prepayment to standard credit (SC) and DD[8].

- More suppliers than ever before (18) are offering tariffs for prepayment customers.

[1] Based on information provided by domestic suppliers on the number of customer accounts held by payment type in each month between January 2012 and March 2015.
[2] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/429873/Fuel_Poverty_Annual_Report_2015.pdf
[3] Ofgem Social Obligations reporting 2014
[4] Consumer Focus, 2010 http://www.consumerfocus.org.uk/assets/1/files/2010/02/Cutting-back-cutting-down-cutting-off.pdf
[5] Ofgem Social Obligations reporting 2014
[6] In this document we use the terms 'market' and 'markets' to refer to different segments of the energy sector. For the avoidance of doubt, these terms are not intended to describe or otherwise suggest the approach that may be taken by us for the purposes of market definition, for example in competition law investigations.
[7] https://www.ofgem.gov.uk/publications-and-updates/customer-engagement-energy-market-tracking-survey-2014 - 2015 findings of our customer engagement tracking survey to be published
[8] Ofgem Social Obligations reporting 2014

- There is a small but growing number of innovative prepayment deals including social tariffs for customers in vulnerable situations, competitively-priced collective switching offers and smart tariffs. However there remain fewer tariff choices overall for prepayment customers (20 gas and 22 electricity SVTs) compared to for DD customers (28 gas and 27 electricity SVTs). In particular there are very few fixed tariffs available to prepayment customers (just four compared to 27 for DD). These tend to be the cheaper tariffs.

- Suppliers cited three main reasons for this lack of tariff choice:
    - Commercial: prepayment customers can be relatively low energy users with higher costs to serve, making offering prepayment tariffs commercially less attractive for suppliers
    - Technical: limited availability of prepayment tariff codes to offer multiple tariffs
    - Regulatory: restrictions on the number of tariffs a supplier can offer introduced as part of the Retail Market Review (RMR) reforms.

  Competition seems weaker in this segment of the market. This is an issue that predates the RMR reforms, and is why we asked the Competition and Markets Authority (CMA) to look into it in more detail. We will consider further to what extent, if at all, the RMR exacerbates issues in this area in light of the CMA findings and our own RMR evaluation work. We can see the potential for smart metering to reduce the relative costs of prepayment and facilitate greater innovation and choice of prepay tariffs. This will go some way to mitigating commercial and technical barriers cited by suppliers.

- In terms of charging, we identified a range of practices by suppliers which appear to be good practice. The majority of suppliers (10 out of 18) do not charge for prepayment meter installations in any circumstances, and 95% of meter removals were carried out for free. Almost half of suppliers (8 out of 18) also do not require upfront security deposits when a customer wishes to pay by SC or DD. This means that those who can't afford a security deposit are not prevented from switching.

- The range of charges for a prepayment meter installation when not under warrant is £46.84 - £160.00. The range of charges for a prepayment meter installed under warrant is £69.00 - £179.96. The range of removal charges is £46.84 - £160.00.

- However the majority of suppliers charge customers warrant-related costs (16 out of 18) such as court costs, warrant application costs, for dog handlers and locksmiths. These costs range from £75.00-£566.00, and can be considerably more than the original debt owed by the customer.

- We are also concerned about the appropriateness of some charges identified. This includes the level of some charges, how charges are applied, and the types of charges applied. For example, two suppliers required a security deposit regardless of credit history; one requested a security deposit of £1,364 from someone that was bankrupt, while another charged £5,000 in the case of a property with a very high tenant turnover rate. Some companies charged more for a meter when installed under warrant than not. Charges varied significantly between suppliers for the same activity, eg between £2.50-£17.00 for a letter.

- The overwhelming majority of suppliers (16 out of 18) retain the right to refuse to remove a prepayment meter in certain circumstances. We have some concerns about the fairness of some practices by suppliers. For example, one supplier refused to remove a prepayment meter because the property in which the customer lived was a rented property with a high turnover of tenants, another because the prepayment meter was originally installed under warrant – even though the customer may have a good payment history.

Next steps

- There appears to be a lot of good practice by suppliers in relation to charging practices. We will consult on further identifying good practice and take steps to strengthen protections in this area. In particular, we will seek views on ending charges for installing and removing prepayment meters and ending use of security deposits in all or some cases.

- We will follow up with the suppliers who have given us cause for concern about the appropriateness of types of charges, levels of charges, and how they are applied. This includes examining their compliance with existing rules.

- We want to see more competively priced tariff options available for prepayment consumers. We have started a review to further understand the potential shortage of prepayment tariff codes and whether this is limiting competition. We note the interactions with the CMA investigation and will take its findings into consideration in the next stage of this work.

- We will continue to work with government and energy companies to ensure smart metering delivers benefits to all consumers including those on prepayment. This includes our work on faster switching and consumer empowerment and protection.

These next steps are designed to facilitate switching for prepayment meter customers, and enable them to access the best deals for them. This includes customers who want to stay on prepayment, and those who wish to change payment method. Our aim is also to ensure that customers are treated fairly and that costs do not fall on those least able to afford them.

1. Introduction

More consumers than ever before are using prepayment to pay their energy bills. Numbers flattened out in 2014, but a significant proportion (15%) of all energy consumers are currently using prepayment[9]. Customers using prepayment generally value the control this payment method offers as it enables them to budget more easily without the worry of an unexpectedly large energy bill[10]. However, they can can also face particular problems in the energy market. From a supplier's perspective, prepayment reduces debt risk and advanced payment has a financial benefit.

While not all prepayment customers are financially vulnerable, they are more likely to be on low incomes than those on credit payment methods. In 2013 around 21% of gas and 22% of electricity prepayment customers were fuel poor. This is higher than for customers paying by SC (16% of gas and 15% of electricity customers) or DD (6% of gas and 7% of electricity customers)[11]. It is important that these customers can access competitively priced deals and are treated fairly.

Background to the review

This review was prompted by concerns that prepayment customers face unique barriers when trying to access competitively-priced deals in the energy market – relatively high energy costs and fewer tariff choices when compared to DD customers; charges for installing and removing a prepayment meter; and upfront security deposits. There were also concerns that charges are falling disproportionately on financially vulnerable customers who are least able to afford them. Furthermore, that in some cases, charges to install a prepayment meter under warrant can be considerably more than the original debt owed by a customer:

- Our Social Obligations reporting indicated that in 2014, nearly 17,000 electricity prepayment customer accounts and 17,000 gas prepayment customer accounts *without a debt* were refused to switch to credit meters (approximately 11% and 14% of those who attempted to switch to credit)[12].

- Some of our Customer First panel participants using prepayment meters reported that the cost of changing their prepayment meter to a credit meter was a barrier when they had considered switching supplier or tariff[13,14].

[9] Based on information provided by domestic suppliers on the number of customer accounts held by payment type in each month between January 2012 and March 2015.
[10] http://www.consumerfocus.org.uk/files/2013/03/Smart-Metering-Prepayment-in-Great-Britain.pdf
[11] England figures only. There are no figures available for Scotland and Wales. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/429873/Fuel_Poverty_Annual_Report_2015.pdf
[12] Ofgem, Social Obligations reporting 2014
[13] https://www.ofgem.gov.uk/ofgem-publications/94017/panel3reportv5-pdf https://www.ofgem.gov.uk/ofgem-publications/90913/panel2reportoctober2014rmrfinal.pdf
[14] The Customer First Panel consists of everyday domestic customers recruited from four locations across GB. The Panel meets regularly to discuss issues impacting on their participation in the energy market.

- Our retail market monitoring identified concerns about the relatively limited choice of tariffs available to prepayment customers when compared to SC and DD customers.

- Research by the Children's Society[15], Citizens Advice[16], Church Action on Poverty[17] and the All-Party Parliamentary Inquiry into Hunger[18] all raised concerns that charges for security deposits, and meter installations and removals, act as a barrier to customers accessing a better deal, with costs falling unfairly on those who can least afford them.

Our wider work to support prepayment customers

This is the latest phase in our work to support prepayment customers. In 2014, we:

- Raised concerns with the Competition and Markets Authority (CMA) that competition may not be working as well as it should for customers.

- Reviewed and made improvements to the Debt Assignment Protocol which will make switching easier for prepayment customers with an energy debt up to £500 per fuel.

- Supported Citizens Advice in securing a £6m voluntary commitment from energy suppliers to use unallocated payments to help customers in vulnerable situations. Following our recommendations, improvements have also been made by industry to the current processes.

- Worked with suppliers to ensure their delivery plans took into account good practice so as to increase uptake of the £12 Government Electricity Rebate by prepayment customers from 50% to 73% since December 2014. This is estimated to have benefitted more than one million prepayment customers.

- Completed an investigation of price differentials between prepayment, SC and DD payment methods. While we found no evidence of overcharging, we recognised that prepayment customers face higher charges for their energy than those paying by DD[19] and undertook further action to address this.

- Held an industry workshop with Citizens Advice to discuss self-disconnection, in particular to identify how prepayment customers struggling to afford their energy could be best supported.

- Hosted a roundtable with industry, consumer groups and parliamentarians to explore what else we could do to support prepayment customers. This review takes forward suggested actions from the roundtable[20].

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[15] http://www.childrenssociety.org.uk/sites/default/files/Show_some_warmth_full_report_1.pdf
[16] https://www.citizensadvice.org.uk/about-us/campaigns/current_campaigns/fair-play-for-prepay-campaign/fair-play-for-prepay/
[17] http://www.church-poverty.org.uk/switch/report/letthemswitch
[18] https://foodpovertyinquiry.files.wordpress.com/2014/12/food-poverty-appg-evidence-review-final.pdf
[19] https://www.ofgem.gov.uk/ofgem-publications/94274/energydebate-topublish-pdf
[20] *ibid*

Scope of the review

In February 2015, we issued an information request on prepayment to all domestic gas and electricity suppliers. This report outlines the key findings and proposed next steps of our review. It is based on the information provided by the 18 suppliers who offer prepayment in the energy market plus our own market analysis. It covers:

- the availability of tariffs for prepayment customers, including the reasons for comparative lack of tariff choice and potential switching savings
- energy suppliers' policies in relation to security deposits
- energy suppliers' charges for the installation and removal of prepayment meters and
- company compliance with regulation related to the above areas.

There are interdependencies between this work and our wider activity on smart prepayment, faster switching and supplier objections.

2. Tariff choice

Chapter background

It is important that prepayment customers can access competitively-priced tariffs that meet their needs. As part of our retail market monitoring, we identified concerns about the relatively limited choice of tariffs available to prepayment customers when compared to SC and DD customers.

In particular, we found a very low number of short, fixed tariffs which, while not always the case, tend to be among the cheapest in the market. We highlighted this issue as an area for investigation in our submission to the Competition and Markets Authority (CMA) in July 2014. This issue was also raised at our payment differentials roundtable in October 2014 where it was recommended that we conduct a wider review into reasons for the lack of tariff choice for prepayment customers.

As well as presenting the range of reasons identified by suppliers for this comparative lack of prepayment choice, this chapter updates our analysis of the number of tariffs and potential cost savings to customers.

Relevant regulation

Requirement to offer prepayment

Energy suppliers must offer their domestic customers a wide choice of payment methods if they have over 50,000 customers[21] (Supply Licence Conditions (SLC) 27.1-27.2). These methods must include payment by cash and in advance through a prepayment meter.

Retail Market Review rules

The objective of RMR policies is to protect consumers' interests by making the retail energy market simpler, clearer and fairer. RMR policies were designed to promote consumer engagement, increase competitive pressure on suppliers and improve quality of service. In the absence of a derogation, suppliers (and, where applicable, their representatives) are required to comply with all RMR rules.

Under the Retail Market Review (RMR) reforms, suppliers can offer a maximum of four core tariffs to customers in a particular region and per metering category (eg single unit rate, Economy 7 and other time of use rates) (SLC 22B.2). This rule is aimed at helping customers to compare and choose the best energy tariffs for their needs.

Suppliers are able to make all of their core tariffs available to prepayment customers as well as customers paying by SC and DD. SLC 22B.7 outlines restrictions on how the core tariffs can differ. This includes that price differences between payment methods:

- must be no more than cost-reflective
- must be the same across all open tariffs and
- must be the same across GB.

[21] Or such other number as may from time to time be directed by the Authority.

In practice, we recognise that some suppliers cross subsidise prepayment so that customers pay less than the cost to serve. We are permissive of this practice and therefore do not intend to pursue discrepancies in pricing of payment types which result in lower charges for prepayment customers[22].

Collective switching is a relatively new and growing activity in GB markets. Some schemes, typically led by local authorities, are specifically aimed at disengaged, vulnerable and fuel-poor customers. Many recent collective switching schemes have included competitive offers for prepayment customers[23]. We recognise that collective switching schemes have demonstrated they can raise consumer engagement, particularly amongst vulnerable and disengaged groups[24]. To facilitate collective switching we included an exemption from the tariff cap for tariffs that are bid into collective switching schemes which meet certain criteria specified in the licence (SLC 22B.38).

To make the case for a derogation, suppliers must demonstrate that compliance with one or more RMR rules would result in outcomes that are inconsistent with RMR objectives or would have unintended adverse consequences for consumers. Derogation requests are considered on a case-by-case basis, taking into account our principal objective to protect the interests of existing and future consumers, as well as our statutory duties. For example, social tariffs and pilot schemes for innovative products linked to smart metering are areas where derogations from RMR rules may be appropriate. In granted derogations, we have considered schemes specifically targeted towards vulnerable customers and innovations which promote energy efficiency and sustainable development. This has included derogations to allow additional prepayment tariffs targeted towards specific social groups.

We encourage interested suppliers to contact the derogation team at Derogations@ofgem.gov.uk to seek advice on the process.

[22] Guidelines on Cost Reflectivity between Payment Methods and the Prohibition of Undue Discrimination in Domestic Gas and Electricity Supply Contracts https://www.ofgem.gov.uk/ofgem-publications/85032/2-19-guidelinesoncostreflectivityandunduediscriminationinsupply.pdf
[23] https://www.ofgem.gov.uk/publications-and-updates/collective-switching
[24] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/253862/Helping_Customers_Switch_Collective_Switching_and_Beyond_final__2_.pdf

Key findings

Prepayment switching rates

Our 2015 Tracking Survey[25] indicates that, in 2014, prepayment customers were switching supplier at comparable levels to DD customers and to the population as a whole[26]. The proportion of customers switching supplier was the same for prepayment and DD customers (13% switched their gas supplier and 15% switched their electricity supplier).

However prepayment customers remain more likely to have never switched supplier. Only 34% have ever switched gas (compared to 48% DD) and only 33% have ever switched electricity (compared to 44% DD) [27].

Prepayment customers are also unlikely to switch from prepayment to credit meters. In 2013, only 3% of all electricity prepayment customers and 3% of all gas prepayment customers switched to a credit meter[28].

Tariff availability: snapshot as at 30 March 2015[29]

- More suppliers than ever before (18) are offering tariffs for prepayment customers.
- Five suppliers below the threshold of 50,000 customers are voluntarily offering tariffs for prepayment customers. This indicates commercial opportunities in the prepayment market for these suppliers.
- Prepayment customers have access to 20 gas and 22 electricity standard variable tariffs[30] (SVTs). This is approximately three quarters of the number of gas and electricity SVTs that are open to DD customers (28 and 27 tariffs respectively).
- There is a comparable level of choice of SVTs for Economy 7 prepayment customers (20) as there is for prepayment customers with standard meters.
- There is significantly less choice of fixed tariffs for gas and electricity prepayment customers (4 tariffs offered by 4 suppliers). This is around one seventh of the number of fixed tariffs that are open to DD customers (27 gas and electricity). Suppliers have suggested the reasons for this include a range of commercial, technical and regulatory factors. These are explained below in more detail.

[25] Not yet published
[26] We do not know how many customers switched supplier and payment method at the same time.
[27] Customer engagement with the energy market tracking survey 2015 – to be published
[28] Social Obligations reporting 2014
[29] We are currently analysing trends in tariff numbers from 2012 to 2015.
[30] A 'Standard Variable Tariff' refers to the standard evergreen supply contract offered by a supplier (ie a contract which is for a period of an indefinite length and which does not contain a fixed term period that applies to any of the terms and conditions). SVT rates can be varied at any time, subject to giving customers advance notice where the change may significantly disadvantage the customer. SVTs do not require online account management.

- Only three suppliers offer fixed tariffs for prepayment customers with Economy 7 meters (3). Fixed tariffs deals tend to be the cheapest on the market.
- However, a small but growing number of suppliers are offering innovative tariffs to prepayment customers. This includes tailored social tariffs for customers in vulnerable situations.

Figure 1: Number of fixed and standard gas tariffs available by payment method

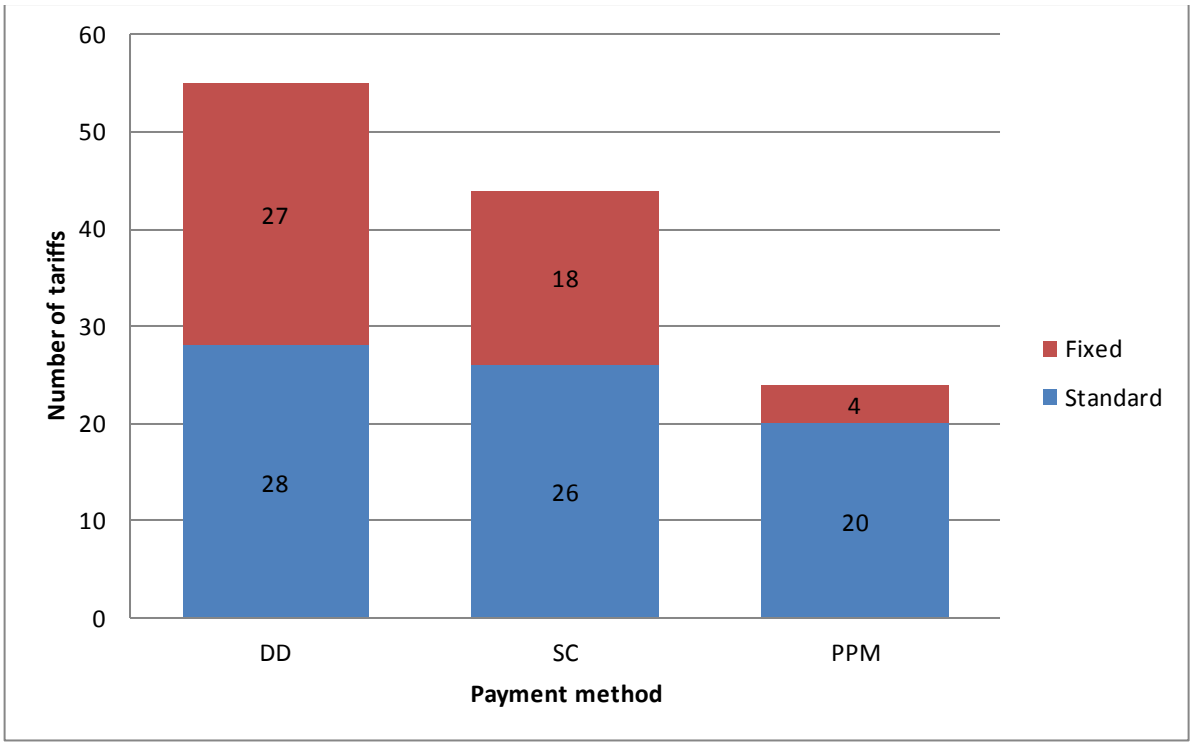


Figure 2: Number of fixed and standard electricity tariffs available by payment method

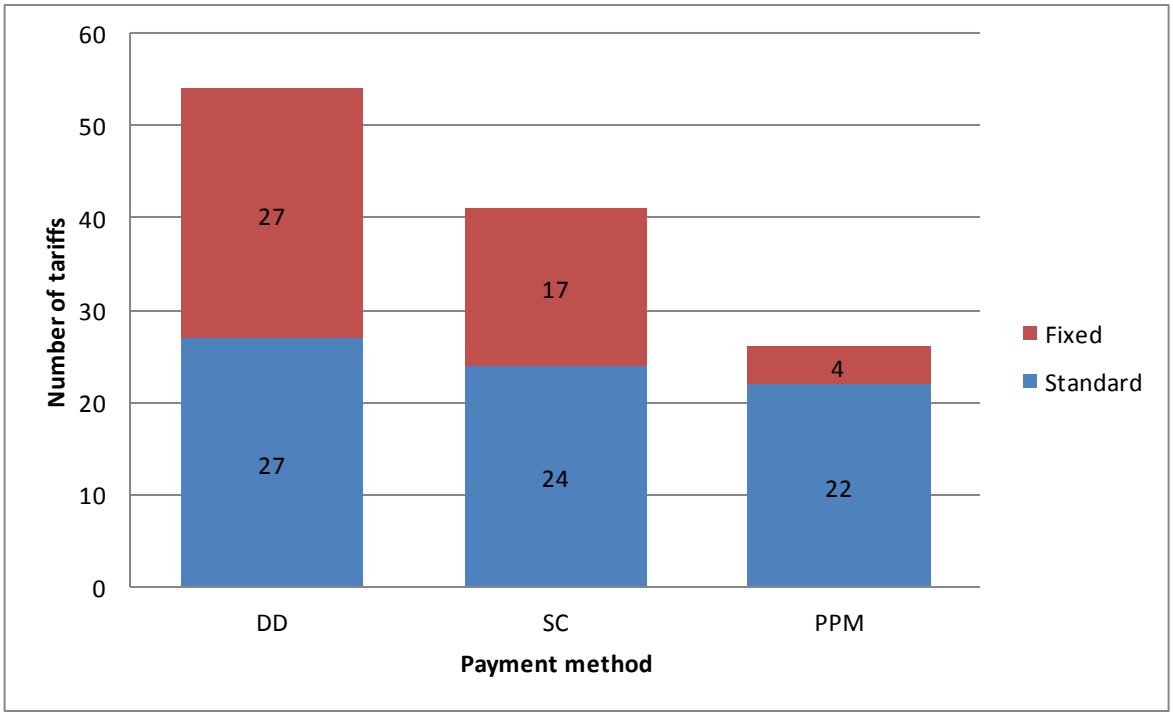
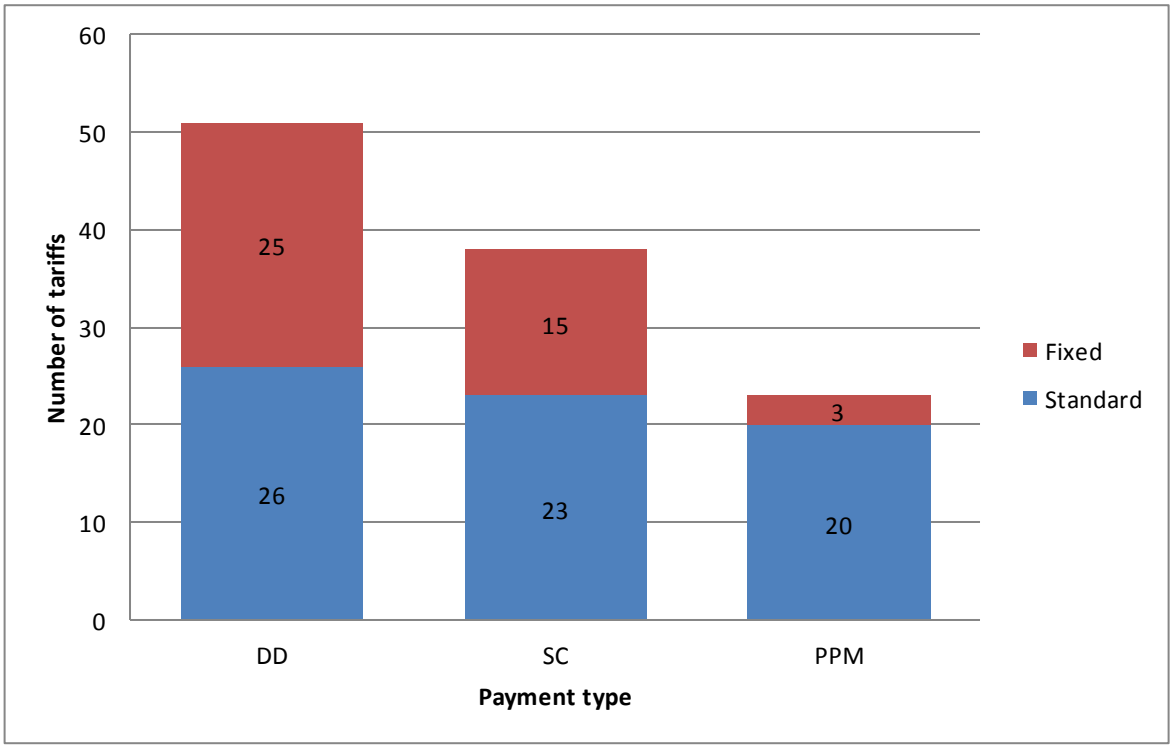


Figure 3: Number of fixed and standard Economy 7 tariffs available by payment method



Potential switching savings for prepayment customers

The average combined gas and electricity bill for a prepayment customer in 2014 was £1,266, while it was £1,267 for a customer paying by SC and £1,188 for a customer paying by DD[31].

By switching, a dual fuel prepayment customer on a SVT with a larger supplier can save:

- by moving to the cheapest fixed tariffs in the market and paying by direct debit, up to £300 per year[32]
- by moving to the cheapest prepayment tariff in the market, including fixed prepayment tariffs, around £66/year
- around £36/year by moving to a cheaper prepayment tariff with the same supplier, where available[33]

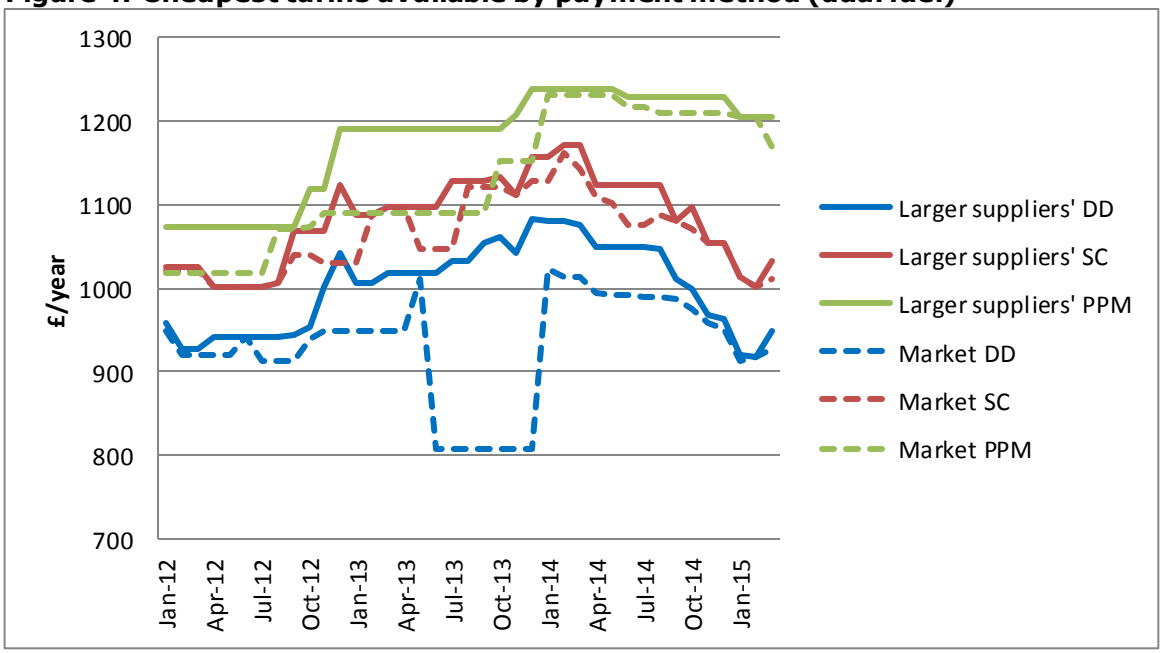
In recent years, the cheapest fixed tariffs have tended to be priced significantly below other tariffs available[34].

Looking across the cheapest tariffs (including fixed tariffs) offered by all suppliers between 2012 and 2015, our monitoring shows that DD customers were offered the cheapest deals over the period, while prepayment customers paid more than SC customers (see Figure 4). The differential between DD and SC prices is fairly static over this period with the cheapest SC tariff on offer typically between 5 and 10% higher than DD. Up until 2014, the cheapest tariff available to prepayment customers was typically between 5 and 10% higher than SC customers.

However, from early 2014 suppliers started offering cheaper fixed tariffs for DD and SC but not for prepayment, causing the size of this differential to increase. Prepayment customers do not appear to have benefited from price cuts made by suppliers to fixed tariffs in the last year[35].

[31] Ofgem analysis of Energylinx data. Bills are calculated based on typical domestic consumption values of 13,500kWh year for gas and 3,200kWh per year for electricity, and looking at SVTs as the starting point.
[32] We assume inactive customers who have not switched recently or have never switched are on a larger suppliers' standard variable tariff (SVT). These savings include fixed tariffs and SVTs. The figures are quoted in £/year and assume no change in standard variable tariffs in the next year.
[33] This applies where a supplier offers more than one prepayment tariff. Nine suppliers currently offer more than one prepayment tariff.
[34] Ofgem analysis of Energylinx data
[35] We are currently analysing recent data on trends in the number of customers on different types of tariffs and using different payment types and will publish this later in 2015.

Figure 4: Cheapest tariffs available by payment method (dual fuel)[36]



Source: Ofgem analysis of Energylinx data, 2015

Innovation in the prepay market

Social tariffs and derogations

A small but growing number of suppliers are offering innovative tariffs to prepayment customers. This includes tailored social tariffs for customers in vulnerable situations.

We strongly encourage any supplier that wishes to offer an additional prepayment tariff with environmental or social benefit, including for customers in a vulnerable situation, to consider applying for an exemption from RMR[37].

We granted suppliers a total of 10 exemptions from our RMR rules between January 2014 and May 2015. Of these, five were open to prepayment customers:

i. Spark offers a tariff designed specifically for social housing tenants. This is a standard variable prepayment tariff which has a zero standing charge and is designed for low to medium energy users. Customers can save up to £137 per

[36] Typical domestic consumption values, which are 13,500kWh year for gas and 3,200 per year for electricity.
[37] https://www.ofgem.gov.uk/ofgem-publications/95429/guidanceforderogationrequestsfromdomesticretailmarketreviewlicenceconditionsversion2-pdf

year[38]. Around 7000 customers are expected to benefit in the first year of the scheme[39].

ii. British Gas has introduced a standing charge rebate of £95 for vulnerable low and zero gas users. This helps prepayment customers who, over summer months do not top-up and can build-up debt. In the first year of the scheme, British Gas will write to customers whom it believes are eligible for the rebate, asking them to confirm their eligibility. They will pay the rebate to their existing customers who are considered financially vulnerable and have consumed less than 1,500 kWh of gas over the previous 12 months[40].

iii. Green Energy offers a shares scheme in which the first 50,000 customers who enter into a contract with the supplier are offered 400 free shares each. The company expects this to result in consumer and community benefits. The company will ultimately be 50 per cent owned by its customers, who through their share rights will be actively involved in the company's business and its objectives[41].

iv. Ovo and EDF offer community energy schemes:
   - Ovo's scheme allows the company's community partners to offer four additional tariffs within a given region and to directly supply energy to their residents and local population. The scheme aims to facilitate the transition to a distributed renewable energy network and promote energy efficiency by facilitating and promoting the diverse activities and projects undertaken by its members[42].
   - EDF Energy offers a district heating scheme which offers residents on the heat network access to a zero standing charge tariff with a unit rate 20% cheaper than the average rate charged by other comparable suppliers in the same region[43].

It is also worth noting that one supplier offers a social tariff as one of its four core tariffs. This tariff allows customers in receipt of disability living allowance, including those paying using a prepayment meter, to receive 10% off the unit rates of any of the suppliers' tariffs.

[38] Based on dual fuel user in London using 9,000kWh gas and 20,00kWh electricity. The tariff is designed for low use social housing tenants and therefore medium and high comparisons are not appropriate.
[39] https://www.ofgem.gov.uk/publications-and-updates/decision-grant-spark-energy-supply-limited-temporary-derogation-certain-standard-conditions-their-gas-and-electricity-supply-licences-respect-affordable-social-housing-prepayment-tariff
[40] https://www.ofgem.gov.uk/publications-and-updates/decision-british-gas-trading-limited-request-temporary-derogation-certain-standard-licence-conditions-its-gas-supply-licence-respect-its-standing-charge-rebate
[41] https://www.ofgem.gov.uk/publications-and-updates/decision-green-energy-uk-plc-request-derogation-certain-standard-licence-conditions-its-electricity-supply-licence-respect-green-energy-share-scheme
[42] https://www.ofgem.gov.uk/publications-and-updates/decision-grant-ovo-energy-limited-temporary-derogation-sub-paragraph-22b.2b-slc-22b-their-respective-gas-and-electricity-supply-licences-respect-community-energy-south-tariffs
[43] https://www.ofgem.gov.uk/publications-and-updates/decision-edf-energy-customer-plc%E2%80%99s-request-formal-derogation-paragraph-2b-slc-22b-respect-barkantine-tariff Note that this is based on the lowest decile of average unit rates.

Smart meters

Smart meters have the potential to revolutionise the prepayment market, reducing the relative costs of prepayment and improving customer service[44]. The overwhelming majority of suppliers (13/18) stated that they expect smart meters to make it simpler and cheaper to serve prepayment customers (for example, by overcoming the need to employ a prepayment meter infrastructure provider and overcoming the restrictions on tariff codes).

A number of suppliers are starting to pilot competitively-priced smart prepay offers. E.ON, OVO and Utilita are among those have smart prepay offerings in the marketplace.

- Utilita has been offering customers smart prepayment services since 2008. All of Utilita's prepayment customers are offered smart pre-pay, and smart meters if they do not have them. 85% of Utilita's customers currently have smart meters installed. Utilita has two smart prepayment tariffs, one with a zero standing charge. Customers are automatically switched to the cheapest tariff and they are offered the same prices as DD customers. Customers can top up in a number of ways including payment by cash at any PayPoint outlet, online, by SMS/smart phone app, phone and pre-pay credit or debit card online. Additional functionality includes £10 emergency credit per meter, and friendly credit periods which prevent disconnection during evenings, over weekends and on public holidays.

- OVO introduced Smart PAYG+, the UK's first full-service smart pay as you go energy platform, in March 2014. OVO's Smart PAYG+ offers customers some of the most competitive market rates along with the ability to top up via smartphone app, text or online, removing the need to top up at the shop with the traditional key or card. Additional functionality includes a credit count down that updates every 24 hours, with optional alerts and auto top ups so customers can manage all of their energy needs on one platform at any time and anywhere.

- E.ON has just launched a Smart Pay As You Go pilot which is available to prepayment and credit customers[45]. Under the pilot scheme, E.ON's prepayment customers are being offered the same prices as DD customers potentially saving them up to £104 per year[46]. Smart Pay As You Go customers will be offered the choice of all E.ON's tariffs and access to the same prices previously offered only to customers who choose to pay by DD. Smart Pay As You Go customers are able to top-up their meter(s) by credit or debit card using a smartphone app, online or by phone. Customers can also move funds between meters if they are running low on

[44] Smart Energy GB http://www.smartenergygb.org/sites/default/files/Attitudes%20around%20buying%20gas%20and%20electricity%20with%20smart%20pay-as-you-go%20-%20FINAL.pptx
[45] http://www.eonenergy.com/for-your-home/saving-energy/smart-meters/smart-pay-as-you-go
[46] £104 is the amount a typical dual fuel prepayment meter customer could save per year if switching from E.ON's EnergyPlan standard tariff to its cheapest one year fixed price tariff (E.ON Energy Fixed 1 Year V16). This amount includes payment method discounts of £70 per year (£35 per fuel through a reduction in standing charge), which is the equivalent amount received by customers who pay by fixed monthly Direct Debit. Prices valid as of 20 May 2015.

credit. During the 2015 pilot phase, Smart Pay As You Go is being made available to 30,000 eligible E.ON customers. It will be more widely available for new and existing customers from 2016.

It is important to highlight that suppliers can only charge differently for genuinely different payment methods. Suppliers are able to make adjustments to tariffs to reflect the costs of genuine differences between payment methods provided they comply with relevant licence conditions including, but not limited to, SLC 22B and SLC 27[47]. We consider that smart metering can transform the experience of prepayment consumers, in terms of both service and cost, and are supportive of appropriate innovations in this area. At the same time, we want to avoid unintended consequences for traditional prepayment consumers who do not yet have access to a smart meter, and expect suppliers to think about what is right for all consumers as they structure their tariffs. We will consider this topic further in our upcoming consultation on smart prepayment[48].

Reasons for comparative lack of tariff choice

Suppliers cited three main reasons for the relative lack of choice for prepayment customers:

i. **Technical**
Some suppliers stated that the nature of competition for prepayment customers is materially different from credit customers as a result of technical limitations in the prepayment meter infrastructure. The technical limitations relate to the number of 'tariff codes' which the prepayment infrastructure can accommodate. The view from some suppliers is that there are insufficient codes available in the system to support multiple suppliers offering multiple tariffs for prepayment customers.

Suppliers report that a different tariff code is needed for each supplier, region and (in the case of electricity) meter type. There may be additional complexities when a supplier wishes to refresh its fixed prepayment products. In this case, a supplier needs a separate tariff code for each version of the product which is 'live' at any given time, not just the version that happens to be on sale. The view from some suppliers is that there are insufficient codes available in the system to support multiple suppliers offering multiple tariffs for prepayment customers.

ii. **Commercial**
A number of suppliers stated that prepayment customers use low amounts of energy and have a higher cost to serve. This higher cost to serve includes the cost of employing a prepayment meter infrastructure provider, using paypoint equipment and the cost of meter exchanges. This makes prepayment customers less financially attractive from a commercial perspective and means that the competitive drivers are lower. Some suppliers stated that they do not wish to grow their prepayment

[47] Guidelines on Cost Reflectivity between Payment Methods, August 2009, Ofgem https://www.ofgem.gov.uk/ofgem-publications/85032/2-19-guidelinesoncostreflectivityandunduediscriminationinsupply.pdf
[48] https://www.ofgem.gov.uk/publications-and-updates/smart-prepayment-proposals

customer base and that they offer prepayment only as a way to re-pay debt.

iii. **Regulatory**
Some suppliers argued that the core tariff cap introduced as part of the RMR reforms restricts their ability to meet the needs of a diverse customer base because it limits the number of tariffs that they can offer. For example, some suppliers stated that they have chosen to remove zero standing charge tariffs for commercial reasons because the number of customers on the tariffs was limited (typically low or zero gas users). A number of suppliers also requested that prepayment should be treated as a separate meter type with four distinct tariffs available for prepay customers.

Commentary and next steps

- **Smart metering:** smart meters have the potential to revolutionise the prepayment market, reducing the relative costs of prepayment and facilitating greater innovation and choice of tariffs. This can positively impact the commercial realities of this market segment and therefore benefit competition. As part of our wider programme of work on Customer Empowerment and Protection, we are proposing to monitor use of key functionalities which will benefit smart prepayment consumers.

- **Review of technical barriers:** we are reviewing whether there is a shortage of prepayment tariff codes and if this is limiting competition. We will explore whether there is a need to address any problems in advance of the smart meter rollout.

- **Regulatory barriers:** Competition seems weaker in this segment of the market. This is an issue that pre-dates the RMR reforms, and is why we asked the CMA to look into it in more detail. Under the RMR, all core tariffs can be open to prepayment meter customers and most suppliers do not use this flexibility. Suppliers are also allowed additional prepayment collective switching tariffs. Finally, there is also the possibility of suppliers applying for derogations from the RMR to offer additional products or services to this segment[49]. We will however consider further to what extent, if at all, the RMR exacerbates issues in this area in light of the CMA findings and our own RMR evaluation work.

- **Compliance:** we will continue to routinely monitor suppliers' compliance with SLC 27.1-27.2 - the requirement to offer a choice of payment methods including prepayment. We will also consider whether the SLC remains fit-for-purpose in light of the smart metering roll-out and developments in competition in this segment of the market.

[49] Guidance for derogation requests from domestic Retail Market Review (RMR) licence Conditions https://www.ofgem.gov.uk/ofgem-publications/95429/guidanceforderogationrequestsfromdomesticretailmarketreviewlicenceconditionsversion2-pdf

3. Security deposits

Chapter background

Prepayment customers can make significant savings by moving from prepayment to the cheapest credit tariff in the market. It is therefore essential that any customer capable of managing their energy bills in arrears is able to switch easily.

The electricity and gas supply licences define a security deposit as "a deposit of money as security for paying electricity and gas charges". There are different circumstances in which suppliers require customers to pay security deposits. Suppliers typically require security deposits from customers wishing to pay by SC, and in some cases by DD, in the event that a credit check suggests they have a high propensity to fall into debt. Some suppliers request security deposits when a prepayment customer wishes to switch from prepayment to credit meter. Suppliers say they use security deposits as a credit management tool to control bad debt which potentially lowers bills for all customers.

While a prepayment customer can save up to £300 a year by moving to the cheapest DD tariffs in the market[50], depending on the charges applied, these initial savings can be eroded or wiped out by the need to pay a security deposit and where applicable prepayment meter removal charges. Not all customers are able to pay upfront lump sums when payment is required in this way. From the individual prepayment customer's point of view, security deposits can potentially:

- be an additional barrier to switching, without necessarily causing financial hardship but nevertheless discouraging them from attempting a switch to credit
- result in financial detriment for low-income customers.

As part of our review, we investigated:

- the circumstances in which suppliers charge security deposits
- the values of security deposits being charged
- whether suppliers were compliant with existing regulation
- examples of good practice, especially instances of preferential treatment for customers in vulnerable situations.

[50] Figure from Ofgem Retail Market Monitoring, May 2015.

Relevant regulation

Reasonableness of application and levels of security deposits

SLC 27.3 of the gas and electricity supply licences explains what we require of suppliers with regard to security deposits:

"A licensee must not require a customer to pay a security deposit in relation to the supply of gas or electricity or, where the premises are Green Deal Premises, in relation to Green Deal Charges:

(a) if that customer agrees that the premises may be supplied through a Prepayment Meter and it is safe and reasonably practicable in all the circumstances of the case for the premises to be so supplied; or

(b) if it is unreasonable in all the circumstances of the case to require that customer to pay a Security Deposit."

SLC 27.4 states that a security deposit must not exceed a reasonable amount. The 2007 supply licence guidance[51] further clarifies SLC 27.3 and SLC 27.4. The guidance suggests that it may be unreasonable in all the circumstances of the case to require a domestic customer to pay a security deposit, for example, if that customer has a payment history showing regular prompt payment of charges for the supply of gas (or electricity) or where the customer has demonstrated a reasonable credit history. We recognise that it may not be easy for a prepayment customer to demonstrate regular prompt payment of charges and will consider how the guidance may be updated to reflect this.

The guidance also defines that in most cases a security deposit is not expected to exceed one-and-a-half times the value of the average quarterly consumption of gas (electricity) reasonably expected at the relevant premises. There may be circumstances in which that amount may be lower and circumstances in which it may be higher.

[51] https://www.ofgem.gov.uk/ofgem-publications/38821/appendix-10-slr-supplementary-document-electricity-final.pdf; https://www.ofgem.gov.uk/ofgem-publications/38822/appendix-11-slr-supplementary-document-gas-final.pdf

Standards of Conduct

We introduced the Standards of Conduct (SLC 25C) in 2013 as part of our Retail Market Review reforms. The Standards require suppliers to treat customers fairly. Customers should be able to expect all their dealings with energy suppliers to be carried out in an honest, transparent and clear way.

SLC 25C.4 states that:

"(a) the licensee and any representative behave and carry out any actions in a fair, honest, transparent, appropriate and professional manner;

(b) the licensee and any representative provide information (whether in writing or orally) to each domestic consumer which:

(i) is complete, accurate and not misleading (in terms of the information provided or omitted);

(ii) is communicated (and, if provided in writing, drafted) in plain and intelligible language;

(iii) relates to products or services which are appropriate to the domestic consumer to whom it is directed; and

(iv) is otherwise fair both in terms of its content and in terms of how it is presented (with more important information being given appropriate prominence)."

We consider that the Standards of Conduct require suppliers to ensure that all charges, including security deposits and prepayment meter installation and removal charges, are clearly communicated to customers and that the situations in which charges are applied are fair.

Key findings

- 8 out of 18 suppliers do not require security deposits when a customer wishes to pay by SC or DD. Of the larger suppliers, this includes EDF Energy (see Appendix 2).

- The other 10 out of 18 suppliers do require security deposits. Of these, suppliers generally charge customers wishing to pay by SC, and in some cases they charge customers wishing to pay by DD[52]. Suppliers tend to do this at the point of acquisition of a new customer, in the event that a credit check suggests that the customer has a high propensity to fall into debt[53].

- 5 out of 18 suppliers, including two of the six largest suppliers, do require security deposits when prepayment customer wishes to switch to a credit meter[54]. Two suppliers appear to request security deposits without regard to customers' credit history. We are following up with these suppliers.

- The average value of security deposits across suppliers in 2014 was about £211[55,56]. The range of typical values is £150 - £300, although some suppliers charge more than this. Suppliers use different approaches to calculate the value of security deposits, usually based on the customer's annual or quarterly consumption. One supplier also takes into account the customer's credit risk - in addition to consumption levels - when calculating the value of security deposits.

- Some suppliers requested high deposits in particular circumstances, eg one supplier requested a deposit of £1,364 in the case of customer bankruptcy, while another supplier requested a deposit of £5,000 where a property had a very high tenant turnover rate. Another supplier requested a maximum value of £1,250. We would like to draw suppliers' attention to our 2007 guidance when setting security deposit values to ensure that the amounts are reasonable.

- In 2014, 4,800 customers (0.1% of all SC customers) paid approximately £1m in security deposits.

[52] Out of the 10 suppliers who require security deposits, three do not do so for customers wishing to pay by DD.
[53] One supplier takes into account the availability and nature of the previous payment history between them and the customer, in addition to the results of a credit check. The same supplier requires different deposit values in the case of high credit risk and in the case of customer insolvency or bankruptcy. Two suppliers requested a security deposit from a customer who was disconnected due to non-payment of charges before reconnection could take place.
[54] Two suppliers indicated that they did so when a credit check indicated that the customer has a high propensity to fall into debt.
[55] These values are in line with our guidance on what constitutes a reasonable value for a security deposit, ie 1.5 times the value of average quarterly consumption (see 2007 supply licence guidance). The average quarterly consumption is currently ca. £220 for electricity and £270 for gas, based on current gas and electricity bill values. Calculations based on DECC Quarterly Energy Prices data.
[56] The majority of suppliers who request security deposits (7) do so for each fuel separately, while 3 suppliers request security deposits per customer.

- The time given by suppliers to customers to pay security deposits varies[57]. One large supplier indicated that they give customers 42 days to pay security deposits. Two other large suppliers give their customers only 14 days. One of these suppliers allows this period to be extended based on each customer's personal circumstances and their ability to pay. It is good practice for suppliers to consider customers' ability to pay when determining the time given for a customer to pay security deposits, especially where there are signs of vulnerability.

- Suppliers have different policies with respect to return of security deposits to customers. Some suppliers return deposits after 12 months of continuous payments, whole others do so after 6 months. One supplier holds on to security deposits while the customer is on live supply.

- Although we did not explicitly request information on the treatment of customers in vulnerable situations, of those suppliers that request security deposits, only two provided evidence of differential treatment for this customer group. In this instance, these customers were not charged a security deposit and the meter exchange was carried out free of charge. We consider this good practice.

Impact of security deposits on switching payment methods

Security deposits may act as a barrier to switching. This is particularly the case where, in addition to a security deposit, a customer may be asked to pay for a meter exchange (see Chapter 4 for more information on prepayment meter removal charges).

Not all suppliers were able to provide information on the number of customers who did not pay a security deposit when asked to do so. However, some suppliers did provide this information. It showed that around 75-85% of customers who requested to pay using SC and were asked to pay a security deposit did not end up paying a security deposit and were not able to complete the transfer.

Suppliers have different policies regarding the time period they give customers to pay the security deposits. The time period may be an additional factor affecting a customer's decision whether to pay the security deposit.

[57] Only four suppliers responded with information about the time given to pay security deposits.

Commentary and next steps

Compliance:

- **Reasonableness of security deposit application**
  We identified two suppliers who applied a blanket policy to require security deposits from all customers wishing to pay by SC, without having regard to all their circumstances eg payment history (SLC 27.3). As this does not take into account customers' circumstances or their credit history, we consider this this may be unreasonable. We are following this up with the suppliers concerned.

- **Reasonableness of security deposit values**
  We also identified three suppliers potentially requiring more than a 'reasonable' amount for security deposits (SLC 27.4 and our 2007 guidance). While the guidance states that there may be circumstances in which that amount may be lower and circumstances in which it may be higher that the recommended 1.5 times the value of average quarterly consumption, it was not clear how the value of the security deposits in these instances was derived. In these cases, it appears that suppliers might have required values that were well above the recommended threshold of 1.5 times the value of average quarterly consumption. We are considering whether these companies have complied with current protections. When assessing compliance with SLC 27.4, we will have regard to those matters set out in the 2007 guidance.

Consultation on use of security deposits:

- We are concerned about the effect of security deposits on a customer's ability to switch payment methods, as well as how appropriate some of the current approaches are. In particular:
  - the high values of some security deposits
  - the need to pay deposits upfront within short timeframes
  - the lack of transparency with respect to policies in relation to security deposits, including how security deposit values are calculated
  - some suppliers' security deposit retention policies
  - not considering customer vulnerability when applying security deposits.

We have decided to consult on strengthening protections in this area, including ending use of security deposits in some or all cases. We recognise that security deposits are only one of a range of tools used by suppliers to manage debt. We will consider this as part of our wider work on supplier objections.

4. Charges for installing and removing prepayment meters

Chapter background
Charging for installing and removing prepayment meters can act as a barrier to switching, particularly for customers on low incomes. These charges, especially installation costs and costs associated with installing prepayment meters under warrant, can further disadvantage customers already struggling to afford their bills. In some cases, these costs can be considerably more than the original debt owed by the customer.

In 2014, around 60% of newly-installed prepayment meters were installed due to debt, and around 16% of these were installed under warrant[58]. This chapter examines the range of supplier policies and charges applied to customers for installing and removing prepayment meters.

Relevant regulation

The standard licence conditions have a number of requirements that relate to setting and applying installation and removal charges - as well as conditions when prepayment meters must be removed.

Installation and removal charges – cost reflectivity

SLC 27.2A requires "Any difference in terms and conditions as between payment methods for paying Charges for the Supply of Electricity shall reflect the costs to the supplier of the different payment methods". Charges for the Supply of Electricity or Gas includes any charges made for the provision of an electricity or gas meter. We consider that the requirements of SLC 27.2A includes costs and charges relating to the installation and removal of a prepayment meter.

A customer should not be penalised because of their choice of payment method. We permit suppliers to charge less than the actual cost or to waive the charge of installing or removing a prepayment meter where these can benefit customers in vulnerable situations, including those on low incomes.

[58] Ofgem, Social Obligations reporting 2014

Standards of Conduct

We introduced the Standards of Conduct (SLC 25C) in 2013 as part of our Retail Market Review reforms. The Standards require suppliers to treat customers fairly. Customers should be able to expect all their dealings with energy suppliers to be carried out in an honest, transparent and clear way (refer to Chapter 3: Security deposits for full details).

We consider that the Standards of Conduct require suppliers to ensure that all charges, including prepayment meter installation and removal charges, are clearly communicated to customers and that the situations in which charges are applied are fair.

Ability to Pay

SLC 27.8 (b) requires suppliers to take "all reasonable steps" to ascertain a customer's ability to pay and must take this into account when calculating repayment installations, considering the value of all charges that are to be paid through a prepayment meter.

Regulation 3 of the Electricity (Prepayment Meter) Regulations 2006 and Gas (Prepayment Meter) Regulations 2006[59] states that prepayment meters may be used to recover sums owed for the supply of gas and 'for the provision of a gas/electricity meter'. The Gas and Electricity Act also states that "the sums that regulations under this paragraph may permit the recovery of through a pre-payment meter include — (c) sums owed in respect of matters other than the supply of gas" (paragraph 6A(3)(c) of Schedule 2B to the Gas Act/paragraph 12 (4)(c) to the Electricity Act).

Regulation 4 of the Electricity (Prepayment Meter) Regulations 2006 and Gas (Prepayment Meter) Regulations 2006 provides that in order to recover such sums via the prepayment meter, suppliers must enter into an agreement with the customer to recover sums via a prepayment meter. The agreement must include written terms that state that the repayment rate and amount has been calculated by the supplier to take into account the customer's ability to pay the total charges to be recovered through the prepayment meter, and that the customer has agreed to the repayment amount.

The effect of the above is that suppliers must take into account a customer's ability to pay installation and removal charges if they are to recover such charges via a prepayment meter. We consider that this includes the total amount of charges, as well as repayment rates.

[59] Or para 6A(1)(a) of Schedule 2B to the Gas Act and Electricity Act which contains similar provisions to Regulation 3.

Prepayment meter removal

SLC 28.1A requires suppliers to offer to replace or move a prepayment meter if they become aware that it is no longer safe and practical for a customer to use a prepayment meter. We have provided guidance which includes situations in which it is not safe nor practical for a customer to use a prepayment meter[60].

In our open letter on the treatment of low and zero customers of gas from June 2014[61], we outlined our expectation that customers in vulnerable situations should not have to pay for the removal of their meter.

SLC 25B.13 states that when a customer is switching, the gaining supplier needs to provide a replacement prepayment meter at no extra charge, when a customer with an advanced prepayment meter seeks a supplier change and the new supplier cannot support existing advanced prepayment meter.

National charging

Licence Condition S22B states that the licensee must ensure that all charges and fees for those matters in S22.B1 are of the same monetary amount across Great Britain[62]. This includes charges levied on particular occasions for (a) matters related to the licensee's statutory powers to disconnect premises, (b) the licensee's statutory powers for rights of entry to the premises and (c) removing, installing or re-installing a meter[63] and (d) making a connection between premises and the main of gas/electricity transporter. If, due to the nature of a particular service and the way it is performed, the charges for that service could not be of the same monetary amount throughout Great Britain, the licensee must use a methodology which is clear and easy to understand (SLC 22B.26 and 22B.27). ***We consider that suppliers must charge the same fees to all customers regardless of where they live in GB. If a supplier believes this is not possible they must have a clear, easy to understand methodology and policy to explain why.***

[60] https://www.ofgem.gov.uk/ofgem-publications/57343/modification-direction.pdf
[61] https://www.ofgem.gov.uk/ofgem-publications/88276/openletter-treatmentoflowandzerocustomersofgas.pdf
[62] Includes termination fees and other charges referred to in S22B.1, but excludes charges referred to in sub-paragraph S22B.1(p).
[63] Refer to S22B.1 (c).

Key findings

Prepayment meter installation: types of charges

Suppliers tend to install a prepayment meter as part of the debt recovery process or at the customer's request (this can be the landlord or the householder)[64]. Charges for installing a prepayment meter fall into three broad categories (Table 1).

Table 1: Types of charges relating to prepayment meter installation

Types of charge	Examples of specific charges
Prepayment meter installation charge	Meter exchanges (typically the time taken by an engineer or meter operator to exchange a credit meter for a prepayment meter) – this can be a prepayment meter installed under warrant or with the customer's consent
Charges when prepayment meter is installed under warrant (not including meter installation)	Warrant application, including court fees, warrant execution, dog handlers, locksmiths, missed appointments
Other charges	Administration fees, debt collection costs

Prepayment meter installation – charging policies

- The majority of suppliers (11 out of 18) do not charge a customer for installing a prepayment meter when the customer has requested a meter, or consented to repay their debt using a prepayment meter, or if the meter is outside of the property and does not need a warrant.

- Suppliers stated a number of reasons for installing a prepayment meter for free. These included:
  - the supplier derives benefit of reduced credit risk from the customer having a prepayment meter installed and therefore chooses to cover the cost of installation;
  - the supplier does not want to add extra debt burden on a customer who may already be in financial difficulty;
  - it creates an incentive for indebted customers to voluntarily agree to have a prepayment meter installed earlier in the debt path.

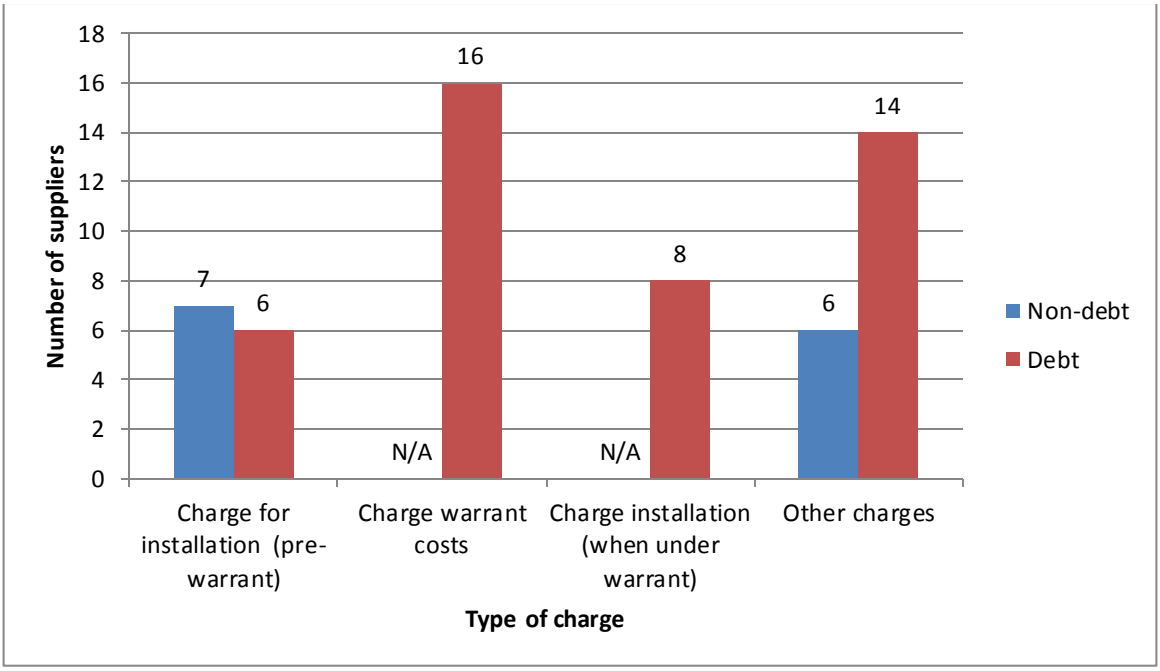
- Most suppliers (10 out of 18) do not charge for the physical meter installation, even when installed under warrant. Eight suppliers charge to install a prepayment

[64] Some suppliers indicated that they will charge a customer where there has been evidence of tampering with the meter or theft of energy, however our review does not focus on these types of charges.

meter under warrant. This includes two suppliers that would not charge if the meter was installed with customer's consent without a warrant.

- The most common reason that suppliers gave for charging customers was that it was reasonable for the individual customer to bear the cost of installation rather than passing the cost on to all customers. Some felt this was especially the case when the charges were a result of a specific request or because of the action, or inaction, of the customer.

Figure 5: Number of suppliers that charge for prepayment meter installation by charge type and reason for installation (debt and non-debt)



Prepayment meter installation charges: levels

- The range of charges for a prepayment meter installation not under warrant is £46.84 - £160.00. We will follow up with suppliers as appropriate to understand how these charges were calculated to ensure they are no more than cost-reflective.

- On average, installation charges appear to be higher when the meter is installed under warrant[65]. The range of charges for a prepayment meter installed under

[65] Two suppliers increased the charge they passed onto customers for the meter exchange, when the meter was installed under warrant.

warrant is £69.00-£179.96. We will take action to understand the reasons for the variation (both when the meter is and is not installed under warrant).

- We found evidence that three suppliers are charging consumers different fees for the same service depending on the meter operator used and the customer's location. This applies to meter installation and removal. We will take further action, as appropriate, if this variation in cost is not in line with our regulations.

Installations under warrant: charging policies

In 2014 around 60% of newly-installed prepayment meters were installed due to debt, and around 16% of these were installed under warrant (49,615 electricity prepayment meters and 47,876 gas prepayment meters)[66]. Installations under warrant should always be a last resort and, as with all prepayment meter installations, the supplier must ensure that prepayment is safe and practical for the customer to use.

- Most suppliers (10 out of 18) do not charge for the physical meter installation, even when installed under warrant.

- The overwhelming majority (16 out of 18) do however charge for warrant-related costs such as court costs, warrant application cost, dog handlers, and locksmiths. These costs range from £75.00-£566.00, which can be considerably more than the original debt owed by the customer.

- We identified a wide range of miscellaneous charges associated with the installation of a meter. We are concerned about the appropriateness of the types of some charges and the value of some charges, eg nine suppliers apply debt recovery charges including for issuing letters. Charges for the same activity can vary significantly, eg a range of £2.50-£17.00 for a letter. Some suppliers charge for pre-disconnection visits with charges of £17-£55.00, including for visits to check for vulnerability.

- Warrants and other charges accounted for the majority of costs levied against customers for the installation of a prepayment meter.

- Suppliers that charged felt that passing warrant-related costs on to individual customers was fair because the charges were a result of individual customer choices, eg the customer had not responded to communications and was not working with the supplier to manage their energy debt. Suppliers did not feel it was appropriate to pass these costs on to their broader customer base.

[66] Ofgem, Social Obligations reporting 2014

Table 2: Range of prepayment meter installation charges

Charge		Range (£)
Prepayment meter installation charges (home visit and cost of physical meter)	Consent	**£46.84** - **£160.00**
	Warrant	**£69.00 - £179.96**
Warrant costs (court costs and execution cost, eg dog handlers, locksmiths)		**£75.00 - £566.00**
Other charges (revenue protection, theft of energy charges, pre-installation debt charges, admin charges including home visits, letters)		**£7.00 – £175.50**

Prepayment meter removal charges – policies

- The policy of the majority of suppliers is to charge for removing prepayment meters under certain circumstances, including three of the larger suppliers. However in practice, 95% of meters that were removed in 2014 were removed for free (317,721 of 335,602 meters[67]).
- The most common reason cited (10 out of 18 suppliers) for waiving the removal fee, including by the six larger suppliers, was that it was no longer safe and practical for a customer to have a prepayment meter.
- Other reasons included if the customer was vulnerable or the supplier wanted to demonstrate good customer service.

Prepayment meter removal – charges

- The range of removal costs is between £46.84 and £160.00 per customer. This is comparable to the charge levied on customers for installing a prepayment meter, which is expected as it reflects the cost of the meter, travel time, and the time for an engineer to exchange the meter for another meter type[68]. As we have indicated regarding installation charges, we will take action to understand the reasons why

[67] Includes traditional and smart prepayment meters.
[68] However, in some instances a prepayment meter is removed with no replacement.

some suppliers charge removal fees that appear significantly larger than the industry average.

- A small number of suppliers have other charges relating to the removal of a prepayment meter. This includes charges for missed appointments and additional administrative fees.

- We estimate that total removal charges passed on to customers amounted to approximately £1 million in the 2014 calendar year, based on data provided by suppliers for this review.

Prepayment meter removal refusals

The overwhelming majority of suppliers (16 out of 18) retain the option to refuse the removal of a prepayment meter under certain circumstances. The reasons given were:

- the customer had outstanding debt on their prepayment meter (16)
- the customer had failed credit checks (3)
- there was a high turnover in rented properties (1)
- the prepayment meter was installed under warrant (1)
- the customer refused to pay a security deposit (2).

We are concerned about the fairness of any approach that penalises an individual customer due to where they live, their property or the reason for the original meter installation, especially if the current customer has a good payment or credit history.

Implications of smart meters on the prepayment market

Smart meters have the potential to revolutionise the prepayment market helping to reduce the relative cost of prepayment and improve customer service.

The overwhelming majority of suppliers (13 out of 18) stated that they expect smart meters to make it simpler and cheaper to serve prepayment customers (for example, by removing the need to employ a prepayment meter infrastructure provider and overcoming restrictions on tariff codes).

Smart meters will enable remote switching between prepay and credit modes (and vice versa) without needing an operator to physically exchange the meter. More than half of suppliers with prepayment (10) indicated that they do not intend to charge for a switch between smart credit and prepay modes in any circumstances due to the cost saving that will result from remote switching. We agree that suppliers should not charge customers for a remote switch.

A remote switch would also remove the need for installations under warrant. This represents costs that should no longer be passed onto customers already in debt. Suppliers will still have to follow the appropriate debt recovery process and ensure that it is safe and practical for the customer to operate the meter in prepay mode.

The ability to switch more easily between modes will also improve suppliers' ability to monitor and intervene early to prevent debt build-up. We expect suppliers to innovate and offer products that can help customers to better manage their budgets in credit mode.

Better access to data should also improve monitoring and enable suppliers to intervene earlier to prevent customers from building up debt.

Some suppliers indicated that they would retain other charges that were incurred by customers such as the debt collection visit. Suppliers indicated that their charging policy would be cost-reflective and that they would consider passing on costs to customers if a charge was incurred. We will consult further on this issue.

As the rollout completion date for smart metering is set for 2020, many traditional prepayment customers will be without smart meter functionality for some time leading up to this date. Suppliers are starting to introduce smart prepay services but these are not yet widespread[69]. We therefore think there is a strong case for addressing the issues outlined in this report for traditional prepayment users and we plan to do so as soon as possible.

Commentary and next steps

Potential compliance issues:
We are concerned about suppliers' practices in a number of areas. We will be following up with suppliers where appropriate.

- *National charging*
  Under SLC 22B, all permitted separate charges which are not incorporated in the unit rate(s) and standing charge should be the same across GB. Customers should not be charged more because of where they live[70]. We found three suppliers that charged different prices for the same activity across different regions. In some cases the difference in meter or installation cost was as much as £40.

- *Cost reflectivity*
  Suppliers apply a wide range of charges for activities associated with the installation of prepayment meters. We are concerned that some charges for prepayment meter installation appear to be higher if installed under warrant. Also, some suppliers charge higher than average costs for the same activity. We recognise that this may reflect higher operating costs particularly for smaller companies who do not have the same economies of scale, however we expect suppliers to keep these costs down as much as possible and we will require suppliers to justify their charges.

[69] Note that the smart metering technical specifications require smart meters to be able to remotely switch between modes.
[70] If, due to the nature of a particular service and the method by which it is performed, the charges for that service could not be of the same monetary amount throughout GB, the licensee must use a methodology which is clear and easy to understand.

- *Ability to pay*
  We saw evidence that suppliers considered the 'Ability to Pay' principles when it came to setting repayment amounts and schedules. However, it was not clear whether suppliers take into account a customer's ability to pay when agreeing the total amount of charges with that customer. We expect suppliers to take a customer's ability to pay into account regardless of whether the meter is installed under warrant. Similarly, we expect that suppliers should take account of a customer's ability to pay not only in relation to debt arrears, but also in applying charges for installing and removing a prepayment meter and associated costs where these costs are to be recovered through a prepayment meter. We will consider ways to improve compliance with the Ability to Pay Principles.

- *Transparency and fairness of charging*
  Suppliers must be transparent about the charges they apply, in line with our Standards of Conduct (SLC 25). We found some suppliers that were not clear about when their charges do and do not apply. We will pursue this with the suppliers concerned. We will also consider whether certain types of charges applied to customers were fair.

Consultation:
We will consult on further identifying good practice and extending this all suppliers. In particular, we will seek views on ending charges for installing and removing prepayment meters, both with standard and smart meters. We plan to host a pre-consultation workshop later in the year to explore the following options further.

Ending installation charges for all or some customers
Based on the current evidence, we believe there is a strong case for ending charges for installing a prepayment meter if it is not installed under warrant:

- more than 60% of prepayment meter installations are due to debt. Charging for installations further adds to customers' financial difficulties.
- suppliers benefit from reduced debt risk when a prepayment meter is installed.
- charging can deter customers from engaging with their supplier early in the debt path which can lead to higher costs for both the individual customer and the supplier.
- charges can also penalise customers who may not be in debt but who are proactive in requesting a prepayment meter to help them manage their energy use or to prevent debt build-up by a future tenant.
- charges can act as a barrier to switching and erode switching savings with the resultant negative impacts on competition and higher charges for all customers.
- the majority of suppliers do not charge for this kind of installation and this good practice should be extended.
- it may incentivise earlier rollout of smart prepayment.
- a common approach across all suppliers strengthens consumer rights in this area.

On balance we also plan to consult on ending all installation charges, including warrant-related charges. Though, we recognise that the case for this is less straightforward. Customers have a responsibility to get in touch with their supplier to pay any outstanding debt. Some customers may deliberately not pay their bills and actively choose not to engage with their supplier, while others may have had a prepayment meter installed

under warrant due to theft of energy. In these instances it could be seen as unfair that charges accrued are passed onto all customers including those on low incomes.

However, we are also mindful that in practice there are also some customers who end up at the warrant stage as they lack the capacity to engage, perhaps due to disability or illness. Whether the customer engages with their supplier also depends in part on how effectively the supplier communicates with them. In addition:

- charges applied when a meter is installed under warrant can be significantly higher than the customer's original debt, causing severe and ongoing financial hardship.
- ending charges would incentivise suppliers to keep costs as low as possible. In theory, competition should put pressure on charges, but the wide range of charges applied for the same activity by suppliers, including similarly-sized suppliers, suggests that passing on charges to those who are often sticky customers may not be providing adequate protection.
- smart metering will improve suppliers' ability to support customers in their energy management and monitor and intervene early to prevent debt build-up. Ending charging would arguably further incentivise innovation in this area.
- we are concerned about whether some of the charges are appropriate, and the seeming lack of consideration of vulnerability when applying installation. A blanket ban on charging can be simpler and more efficient than the cost involved in identifying particular groups of customers.

Ending removal charges in all circumstances

While the majority of meter installations are already carried out for free, we intend to also consult on ending prepayment meter *removal* charges in all circumstances. This is because:

- prepayment meter removal charges can act as a barrier to switching with negative impacts on competition and customers' bills.
- such a move would help ensure that all customers, regardless of their income, can access competitively-priced energy tariffs.
- with smart meters there will be no need for a meter exchange. This may incentivise making smart prepayment available to existing prepayment customers.
- it extends existing good practice and puts more downward pressure on costs where charges cannot be passed on to customers.
- it creates regulatory simplicity with the associated benefits in terms of communicating customer rights– there are already a number of exemptions to the current rules which require or encourage suppliers to remove prepayment meters for free – including for customers in vulnerable situations and with advanced meters.
- linked to above, ending removal charges would strengthen customer rights and send a clear message to prepayment customers that they are able to access competitively-priced deals.

Refusing to remove meters

Our review uncovered several reasons why suppliers may refuse to remove a prepayment meter, most commonly if a customer has outstanding debt on their prepayment meter or has failed a credit check and won't pay a security deposit. We have particular concerns that one supplier blocks customers from switching if the prepayment meter was installed under warrant, regardless of the customer's payment or credit history. We are encouraged that a number of suppliers allow prepayment customers to move onto another payment method if their account remains in credit for periods ranging from no fewer than two months to 12 months. We will consult on whether these approaches are right, and identify and seek to extend good practice as appropriate.

Interactions with the CMA's Energy Market Investigation

As outlined in this chapter, meter charges can represent a barrier to switching. We note the CMA's investigation is considering barriers to switching. It is due to publish its provisional findings shortly. We have kept the CMA informed of our review and will continue to do so. We will also take the CMA's findings into consideration in the next stage of our review.

Appendices

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Appendix 1 – Prepayment tariffs offered by suppliers

Supplier	Number of tariffs open to prepayment customers (available for gas, electricity and economy 7 unless otherwise stated)		
	Standard	Fixed	Social
Better Energy	1 (gas only)		
British Gas	1	1	
Co-operative Energy	1		
Economy Energy	1	1	
Ecotricity	1[71]		
EDF Energy	1	1	
E.ON	1		
Extra Energy	Did not support prepayment in March 2015 but as of May 2015 are offering prepayment		
First Utility	1		
Flow	Not required to offer prepayment and do not offer prepayment		
Good Energy	1		
Green Energy	3 (electricity and economy 7) 1 (gas)		1
Greenstar	Not required to offer prepayment and do not offer prepayment		
isupply	Not required to offer prepayment and do not offer prepayment		
LoCO2 Energy	1 (electricity and economy 7 only)		
Npower	1		
Ovo	1 (not economy 7)		
Scottish Power	1	1	
Spark	1		1
SSE	2		
Utilita	2		
Utility Warehouse	1		
Zog	Not required to offer prepayment and do not offer prepayment		

[71] There is a different rate for customers on Economy 7 ToU mode and standard mode.

Appendix 2 – Average and maximum security deposit values charged by supplier

Supplier	Security deposit (average value £)	Security deposit (maximum value £)
Better Energy	Do not charge	Do not charge
British Gas	£90	£125
Co-operative Energy	Do not charge	Do not charge
E.ON	£200	£1,000; £5,000
Economy Energy	£250	£250
Ecotricity	Do not charge	Do not charge
EDF Energy	Do not currently charge	Do not currently charge
Extra Energy	N/A	N/A
First Utility[72]	£300	£300
Flow	Do not offer prepayment – N/A	Do not offer prepayment – N/A
Good Energy	Do not charge	Do not charge
Green Energy	£250	£250
Greenstar Energy	Do not offer prepayment – N/A	Do not offer prepayment – N/A
isupply	Do not offer prepayment – N/A	Do not offer prepayment – N/A
LoCO2 Energy	Do not charge	Do not charge
Npower[73]	£125 (due to credit risk); £262-£400 (due to insolvency or bankruptcy)	£250 (due to credit risk); £806-£1,364 (due to insolvency or bankruptcy)
Ovo	£200	£218
Scottish Power	£150	£150
Spark	Do not charge	Do not charge
SSE[74]	£150	£150
Utilita	Do not charge	Do not charge

[72] The £300 security deposit is being reviewed at present and may change in the future.
[73] The larger of the figures relating to insolvency or bankruptcy is relevant where Npower is already supplying a customer who becomes insolvent or bankrupt, and Npower requests payment for future consumption upfront based on the individual customer's previous consumption. The security deposit figures at customer take-on are based on an estimate where Npower has had no historic dealings with a particular customer.
[74] SSE rarely requests customers to pay a security deposit. In 2014, only 26 customers paid security deposit, with the sum requested totalling £3,900. Security deposits were requested from customers changing supplier. SSE has recently removed the £52 charge for the removal of a prepayment meter to credit meter. In the light of this change, as well as due to recent changes to the Debt Assignment Protocol and the ongoing consultation on the review of the debt objections, SSE may review the use of security deposits in the future.

Supplier	Security deposit (average value £)	Security deposit (maximum value £)
Utility Warehouse	£173-£205	£950-£1,250[75]
Zog	Do not offer prepayment – N/A	Do not offer prepayment – N/A

Total value of security deposits paid in 2014

Total value of security deposits received in 2014 (£)	Number of customers who paid a security deposit during 2014	Average (£)
£1,013,998	4,796 (0.1% of SC customers)	£211

[75] Utility Warehouse calculates security deposits based on average energy consumption, in line with Ofgem's 2007 licence condition guidance. This means that on occasions the value of security deposits may be lower or higher than average. Utility Warehouse stated that it retains low average values for security deposits overall.

Appendix 3 – Prepayment meter installation and removal charges by supplier

Supplier	Installation charge (£)	Removal charge (£)
Better Energy	£100 (excl. VAT) - No charge when customer agrees to prepayment meter installation	£100 (excl. VAT)
British Gas[76]	Do not charge	Do not charge
Co-operative Energy[77]	Electricity - £66.15 - £108.15 Gas - £69.02	Electricity - £66.15 - £108.15 Gas - £69.02
Economy Energy	£69.00 - £87.60[78]	£69.00 - £87.60
Ecotricity[79]	Electricity - £46.84 -£82.26 (incl. VAT) Gas - £87.09 (incl. VAT)	Electricity - £46.84 -£82.26 (incl. VAT) Gas - £87.09 (incl. VAT)
EDF Energy[80]	Do not currently charge	Do not currently charge
E.ON[81]	Do not charge	Do not charge
Extra Energy	£160	£160[82]
First Utility	Do not charge	Do not charge
Flow	Do not offer prepayment – N/A	Do not offer prepayment – N/A
Good Energy	Do not charge	Do not charge
Green Energy	£56.88 (incl. VAT)	N/A
Greenstar Energy	Do not offer prepayment – N/A	Do not offer prepayment – N/A
isupply	Do not offer prepayment – N/A	Do not offer prepayment – N/A
LoCO2 Energy	£78 (incl. VAT)	£78 (incl. VAT)
Npower	Do not charge	£60 (non-vulnerable) Do not charge (vulnerable)
Ovo	Do not charge	Electricity - £51.72 +vat Gas - £69.20 + vat

[76] British Gas applies a charge for a meter installation/removal when there has been evidence of energy theft.
[77] Co-operative Energy provided a range of meter exchange costs. The min and max figure have been provided in this table.
[78] Prepayment installation costs for Revenue Protection & Credit to PP meter purposes vary by distributor.
[79] Ecotricity provided a range of meter exchange costs. The min and max figure have been provided in this table.
[80] EDF Energy may charge customers to reposition a meter, depending on circumstances.
[81] E.ON will charge customers for a prepayment meter disconnection where the meter is not replaced.
[82] Extra Energy previously charged an hourly rate.

Supplier	Installation charge (£)	Removal charge (£)
Scottish Power	Do not charge	Do not charge[83]
Spark[84]	Electricity - £65 Gas - £75	Electricity - £60 Gas - £75
SSE	Do not charge	Do not charge[85]
Utilita[86]	Do not charge	Do not charge[87]
Utility Warehouse	Electricity - £66 (incl. VAT) Gas - £103.20 (incl. VAT)[88]	Electricity - £66 (incl. VAT) Gas - £79.20 (incl. VAT)
Zog	Do not offer prepayment – N/A	Do not offer prepayment – N/A

[83] In the 2014 reporting period, Scottish Power did apply a removal charge in certain circumstances however Scottish Power has decided to remove this fee as of April 2015.
[84] Spark will not pass on the charge to vulnerable customers.
[85] In the 2014 reporting period, SSE did apply a removal charge in certain circumstances however SSE has decided to remove this fee as of April 2015. Installation and removal costs are fixed costs to the business and are therefore recovered through the standing charge and/or unit rate.
[86] Utilita do not install traditional prepayment meters. Utilita primarily offer a smart prepayment service. When a customer joins Utilita, they will install a smart prepayment meter for free as part of their service.
[87] Utilita only charges for meter removal where there is damage associated with revenue protection cases and then the costs would usually relate to smart prepayment meters not traditional prepayment meters, due to Utilita's installation of smart prepayment meters.
[88] Utility Warehouse only charge installation fees when there is no meter at the property.