

Friday 7 January 2022

Statutory consultation response: potential short-term interventions to address risks to consumers from market volatility

Retail Policy Interventions Team -

Response summary

The conclusions arrived at in the consultation document are considered and balanced. It's right that Ofgem has thought ahead to plan for the exceptional scenarios that could arise as wholesale gas prices adjust over the next price cap period, having sustained record levels over this winter.

In particular, the identified options correctly target what is the primary market risk: the risk that unsustainable business models and pricing, which have proved so damaging and costly, are allowed to return to the retail energy market. As the executive summary states: "we are now putting in place an enhanced regulatory approach to ensure energy suppliers pursue sustainable business models, minimising risks to customers and the market."

In short, we agree with Ofgem that there is insufficient justification to approve either option 2 (exit fees on standard variable tariffs) or option 3 (a new Market Stabilisation Charge). Either of these solutions would risk micromanaging what is a more fundamental issue at stake; and they would unduly distort normal competition and switching practices, which will yet return. We also agree that option 1 (requiring new tariffs to be available to existing customers) should be approved, as a sensible mitigation against the unsustainable practice of 'price walking'.

Should this be the outcome - the approval of option 1, and the rejection of both options 2 and 3 - there will be more to do to protect against the risk identified in this consultation; but we note that such further initiatives sit under other consultations which are open in parallel.

Regarding the price cap reform consultation, we expect that the responses Ofgem gets back will reflect what seems to be an emerging consensus: that some form of relative price cap should be put back on the agenda. We believe this could be made to work in conjunction with the absolute price cap.

Regarding the financial resilience workstream, while a substantial raising of standards is overdue and welcome, we think it would be much more effective and simpler to prohibit suppliers from taking advance payments, and so forcing customers into a credit position with them from the outset. Had this already been in place, much of the market instability and consumer detriment we are witnessing presently would likely have been avoided.

Question 1: Have we correctly identified and assessed the risks to consumers from continued wholesale market volatility?

Yes. In parallel to managing the wholesale price shock, the market will have to recover the costs accumulated by the failed suppliers, and this means allowing responsible suppliers a fair chance of being able to do so. There is a scenario whereby the suppliers robust enough

to still be in the market in 2022, and who will therefore be cleaning up the impact of this winter, have their own financial resilience undermined by the return of unsustainable, customer acquisition targeted pricing. This situation could in turn worsen market instability and so cost consumers even more in the long run.

Question 2: Do you believe that intervention is warranted in the interests of consumers?

Yes. It would be a false economy not to make interventions, as we now know unequivocally that a race to the bottom on acquisition pricing, whilst seeming to benefit the most engaged consumers, actually increases the total costs ultimately paid by all consumers.

Question 3: Which of these possible interventions, if any, would be most effective and proportionate in addressing the risks identified in consumers' interests?

Option 1 is a sensible intervention, as it mitigates against an indicator of unsustainable practice, which we refer to as 'price walking'. There will be a case later to make such a temporary change permanent.

Option 2 should be avoided as it would disrupt customers' normal engagement with the market, at a time when confidence in the market is already delicate.

Option 3 should be avoided for the potential downsides as laid out in the consultation. It is also notably complex and would create a whole 'cottage industry' set of processes, when simpler measures could be applied instead to mitigate what is as a broader risk: that unsustainable business models and pricing are allowed to return.

Question 4: For each option, are there particular benefits or risks for consumers, including those in vulnerable circumstances, that we have not identified?

The consultation is comprehensive.

Question 5: For each option, do you agree that we have identified the full range of expected impacts on suppliers, consumers and competition?

The consultation is comprehensive.

Question 6: Where applicable, do you agree that the draft Licence Condition text accurately implements the intervention as described?

Yes.

Question 7: Do you agree that the methodology outlined in Appendix 2 best delivers the charge described in this consultation document?

Yes.

Questions 8 - 10: ex-ante publication of the charge/weekly publication/payment mechanism

As covered above, this could be made a workable solution as outlined, but is notably complex overall, and would create a whole 'cottage industry' set of processes, when cleaner and simpler measures could be applied instead to mitigate against the risk of returning to unsustainable business models and pricing.