Ofgem Consultation on framework for consumer standards and policy options to address priority customer service issues

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Consultation response from the

Centre for Competition Policy

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We focus our research based evidence on two aspects of Ofgem's consultation:
reputational incentives; and the costs to consumers (and its importance) of spending (and expecting to spend) more time on supplier contact.
We have responded to other issues where relevant, using Ofgem's questions as guidance.
Our response is based in part on surveys of consumer preferences which related to searching and switching, extracting findings relevant to the current consumer standards debate.

> ***Question 1:*** *Do you agree with our assessment on what good looks like for the issues consumers are facing relating to the priority issues of contact ease and identification and support/advice for consumers struggling with their bills. Are there any issues missing?*

We broadly agree with Table2, p.26 in particular the bottom right-hand box, that customers need not only to be able contact suppliers, but also to receive appropriate resolution. Problems arise if intermediate goals, such as speed of answering telephones, is measured and rewarded, as was seen in the early days of privatisation, as regulators first introduced service quality standards[1], and where it was clear that political and reputational incentives were as important as financial motivations in shaping regulated industry actions. This research also illustrates how whatever gets measured (and rewarded) gets managed, and the existence of some potential tensions between economic and other regulations, including safety.

> ***Question 2:*** *Do you have any views on potential options to address priority issues and do you agree with the extra requirements we are proposing?*

The two options in table 3, p.28, present the difference between whether suppliers are able to distinguish consumers in vulnerable situations. Suppliers can identify some forms of potential distress through their interactions via energy supply and payment arrears, but not general financial distress or (often) *potential* payment difficulties in energy. Moreover, given the difficulty for suppliers to identify some aspects of vulnerability (for example illness or bereavement), we would emphasise that the only way to ensure that such consumers are treated appropriately is to offer the proposed standard of care required for those circumstances to all consumers.

Difficulties faced in energy are usually part of wider financial challenges, and are closely linked to other budgetary choices, as three recent papers relating energy issues to eating, housing and health issues show[2]. The underlying problem may be better addressed by other instruments and in other markets, requiring liaison with a variety of regulators and policy makers, particularly in the financial and social care sectors.

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[1] *Service Quality in Regulated Network Industries* by Waddams Price, Brigham and Fitzgerald, 2008
[2] *Pay (for it) as you go: Prepaid energy meters and the heat-or-eat dilemma*, by Burlinson, Davillas and Law, 2022; *Fuel poverty and financial distress* by Burlinson, Giulietti, Law and Liu, 2021; and *Getting warmer: Fuel poverty, objective and subjective health and well-being*, by Davillas, Andrew Burlinson and Liu, 2022.

The interaction between resilience in the energy market and more generally is shown in our concept of energy price resilience, showing the general concept of household energy affordability resilience in the context of energy price rises. Here the joint importance of maintaining thermal comfort, affordability and elements of financial security is related to wellbeing, in particular health aspects. These ideas are developed further in a mimeo[3] and forthcoming discussion paper.

Figure 1. *A conceptual framework of household energy price resilience.*

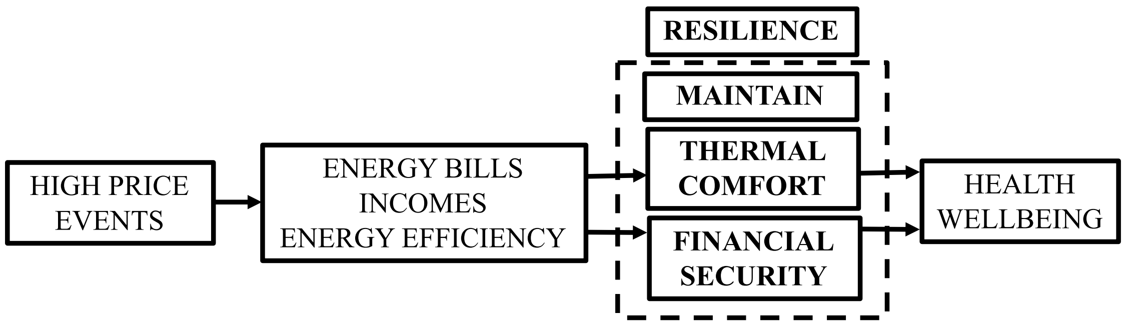

Figure 1 illustrates two aspects, each measured by two factors, which constitute energy price resilience. The first aspect captures thermal discomfort and energy affordability by two factors, namely that a household is:

1) unable to keep the accommodation warm enough during winter (because of affordability issues); and/or
2) spends more than 10% of their income on energy.

As for the thermal (dis)comfort channel, we rely on a combination of perception- and quasi objective measures to capture issues related to the second aspect, financial insecurity as particularly related to energy. We identify as Energy Insecure an individual who:

1) is currently and personally finding managing their finances at least quite difficult; and/or
2) is a member of a household which has fallen behind on at least some of their bills, including electricity, gas, and other utilities.

Whilst these measures of energy indebtedness are proxies, they have been found to be systematically associated with issues related to energy in previous research[4].

Question 4: *Do you agree with our proposed approach of introducing reputational incentives in our priority areas?*

[3] *A cause for concern: Household energy price resilience* by Burlinson, Davillas, Giulietti and Waddams Price, 2023

[4] *Fuel poverty and financial distress* by Burlinson, Giulietti, Law and Liu, 2021

Our research[5] indicates that reputational incentives are important, and often provide a link between surprising markets. For example, in the early days of privatisation, when companies were seeking overseas markets, they used their relative position in the regulator's relative measures of standards in the UK for marketing. Like any incentives, they may have unintended (and perhaps perverse) effects. Moreover, experience shows that privatised suppliers do not always respond to regulator imposed *financial* incentives in the ways that might be anticipated[6]. When price caps were first imposed, economic models predicted that their format would affect the structure of prices (eg fixed relative to commodity charge) and the relationship between prices charged to different groups of consumers, but Giulietti and Waddams Price found little evidence of such response.

Consumers reveal preferences about service quality and reputation in energy in their behaviour in choosing suppliers, when circumstances made such choice a feasible option. While financial gain has been a driver for choice of supplier (and we have seen the lack of offers and switching in the recent period of binding price caps), non-financial aspects have also affected behaviour. Consumers who were observed in their responses to supply choices in an auction showed that ethical and environmental grounds were an important factor in choosing whether to switch supplier[7]. If suppliers receive the same feedback from their own market research, this suggests that reputational incentives are likely to be influential for both consumers and suppliers.

> ***Question 5:*** *Do you agree with what we have set out in the assessment chapter? Please provide supporting evidence with your views. For evidence regarding additional costs, please provide quantitative data.*

While we are unable to provide quantitative data based on our research, we note that the costs to suppliers of improving consumer service may provide some corresponding insight into the costs incurred by consumers in contacting their suppliers. If a monetary value can be attached to customers' time spent communicating with suppliers (+ waiting times?) than it might be possible to estimate a monetary 'social cost' of addressing bill-related and other energy supply problems. The hours which employees spend responding to calls would provide a lower bound of hours of consumer time involved in contacting their supplier.

Our research shows a considerable heterogeneity between consumers within the energy market. In particular, expectations of how long it would take to switch varied considerably between consumers. Since switching requires contact with suppliers, there is likely to be similar variation in expected time taken to resolve issues of customer service[8]. Expected switching time was related to age, income, education and experience of searching and switching in the market. These variations suggest that a variety of policies will be needed to address the service quality concerns of different consumers in the market.

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[5] *Service Quality in Regulated Network Industries* by Waddams Price, Brigham and Fitzgerald, 2008

[6] *Incentive Regulation and Efficient Pricing* by Giulietti and Waddams Price, 2005.

[7] *Switching Energy Suppliers: It's not all about the money* by Deller, Giulietti, Loomes, Waddams Price, Moniche and Jeon, 2021

[8] *Empirical Evidence of Consumer Response In Regulated Markets* by Waddams Price and Zhu, 2016

Time pressures also featured as a deterrent in the switching decisions of consumers who had entered The Big Switch collective auction[9]. Participants who were worried about switching being very time consuming were more likely to accept the offer in the auction; while how busy they remembered the auction period as being had a strong influence on their acceptance of the offer made. This was true across the spectrum of responses to 'The Big Switch was at a particularly busy period'. Those who agreed (strongly or otherwise) were less likely to have accepted the offer and those who disagreed were more likely to have done so. Of course this may partially reflect resolution of cognitive dissonance, but given the very low barrier involved in accepting an offer, it suggests that any contact with suppliers is likely to be deterred by 'busyness', which is likely to be disproportionately experienced by consumers in vulnerable circumstances.

As well as the time involved, we note the additional stress of the process of contacting suppliers, recorded in Ofgem's own research[10].

What are the costs to Ofgem itself of the new of proposals?

In assessing the costs to suppliers of raising consumer service standards, it is important to explore and include any benefits which may accrue to companies from improved standards, including lower costs of debt management and collection.

Benefits from the proposals may extend beyond lower costs to consumers through transactions with suppliers, in particular through decisions which enable them to participate in the market more effectively, with pro-competitive effects between companies. On the other hand, giving vulnerable consumers an expectation that they will get the same support from all suppliers closes this off as an area of rivalry, and may weaken any competitive pressures in the market. This may well be an appropriate compromise for customers in vulnerable circumstances, many of whom are also less engaged in the market[11]. In general it would be expected that rapid and efficient debt management arrangements would benefit both suppliers and consumers, reducing the need to rely on third-party involvement.

Recovering any additional supplier and regulatory costs from consumers will also have distributional effects. If the main purpose is to support consumers in vulnerable circumstances, which extend beyond the energy market both in cause and effect, might they be appropriately recovered from general taxation rather than prices? If the costs are recovered through energy prices, then the balance between increasing standing charge or running rate is important. Higher standing charges disadvantage low income households on average (because they have lower consumption); but higher running rates will particularly affect consumers who are fuel poor because they have high

[9] *Switching Energy Suppliers: It's not all about the money* by Deller, Giulietti, Loomes, Waddams Price, Moniche and Jeon, 2021

[10] *Customer satisfaction with energy supplier complaints handling 2018*, Research Report Prepared for Ofgem June 2018
https://www.ofgem.gov.uk/sites/default/files/docs/2018/09/quadrangle_ofgemchs2018_researchreport.pdf

[11] *Energy Market Investigation* by Competition and Markets Authority, 2016.

consumption relative to their income[12]. In California, income related standing charges have been proposed to address these issues[13].

*1.6. **Question 6:** Using the list of prospective data items we present in the monitoring chapter as a guide, what other additional data items could we aim to collect and from what data sources? Do you consider there are any challenges you may face when collecting/providing these? If so, please provide any supporting evidence you have.*

One opportunity for further benefit from data collection will be making data (appropriately anonymised) available, so that academics and others can provide analysis in the longer term which is likely to inform and improve Ofgem's regulation. Such use often requires a simple request for permission when collecting data to make it available for further analysis.

We also suggest that data collected are as far as possible consistent with other data sources, collected both by Ofgem and other sources such as the ONS. This will facilitate more comprehensive analysis both within and beyond Ofgem.

While we have not had an opportunity to assess the relative costs and benefits of collecting these additional data, our suggestions include:

The number of tariffs available to vulnerable consumers, including PPM users;

Average fees for those in arrears;

The number of customers in arrears with debt sent to a debt collection agency by consumers with/without a repayment plan;

The proportion of arrears that is consumption-based and the proportion that is fee-based.

*1.7. **Question 7:** Do you have any comments on the factors that should be considered in determining whether to use principle-based or rule-based approach to setting standards?*

We agree with much of the analysis in Annex 3, in particular table 1. There is an interesting parallel between principles based and rule based standards, and ex post competition law and ex ante regulation. Since Ofgem has experience with both, this might yield some useful lessons for policy options in consumer standards. In paragraph 3.16 there is a suggestion of progressing from

[12] *Left out in the cold? New energy tariffs, low-income households and the fuel poor* by Bennett, Cooke and Waddams Price, 2002
[13] *Paying for Electricity in California: How Residential Rate Design Impacts Equity and Electrification* by Borenstein, Fowlie and Sallee, 2022

voluntary to mandatory standards; this may affect the incentives of companies to comply with/report on the voluntary standards, in anticipation of later enforcement of mandatory rules.

We agree with the practice and proposal in 3.22 of using a mixture of qualitative and quantitative methodologies, which we have found in our own research provides an understanding both of the depth and nature of consumer issues, and of their extent.

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