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Standing Charges: Call for Input UW response

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Utility Warehouse was one of the first ‘challenger’ brands when it entered the retail energy market over 20 years ago, and we have a unique perspective in that we operate across numerous regulated markets: energy, telecoms and insurance. Today we serve over 950,000 households.

UW overarching view

Given the relatively low positive impact of this proposal, the scope for inefficiency and market distortions, and the regressive outcomes it creates, we do not see how it is justified to pursue the case for policy intervention on standing charges. This is particularly true given we have a very clear proposal - with industry and consumer body support - for a new policy approach that truly addresses the issue of affordability ie. a targeted, progressive and government-funded social tariff, which would complement the existing price cap. Our key views are set out below:

- The price cap is the only mechanism that genuinely protects consumers from unfair pricing and that enables Ofgem to drive down standing charges through scrutiny of costs. We firmly believe the price cap is an effective tool at ensuring fair pricing and should be retained as a pillar of the future retail market, but it does not address the issue of affordability directly.
- A social tariff is the most appropriate mechanism to support customers in need of bill support. Unlike the proposed reforms on standing charges, a social tariff is progressive and avoids the negative impacts of regressive policy, which in the case of standing charge reform would mean that vulnerable and low income consumers would face even higher costs than they do today. It would also mean some affluent consumers could stand to benefit through the use of low carbon technologies - at the expense of other bill payers.
- Innovation is already happening and where suppliers have created innovative tariffs, they should be able to beat the cap to reduce standing charges for consumers.
- Cost recovery is an essential part of financeability and market stability; Ofgem should retain the cap to ensure fair pricing of standing charges for disengaged customers.
- The case for standing charge reform is weak. High standing charges have in part been driven by the cost of supplier failures, which we hope are largely a matter of history. Going forward, we would expect these costs will fall away and ease pressure on standing charges.
- Changes in standing charge structure cannot hide or offset changes in variable costs and the resulting impact on consumer bills. As explained in Ofgem’s TCR Decision, the changes made to industry cost structures will have removed the cost of network charges from (and therefore reduced) unit costs, however, the wholesale energy crisis means that the effect of this has not been obvious to consumers. This is a dynamic that will not change even if Ofgem re-models what costs are taken via the standing charge.

Consultation questions

Q1	What are the barriers to suppliers using the existing flexibility under the price cap?
	<p>Cost recovery is an essential part of financeability and market stability; Ofgem should retain the cap to ensure fair pricing of standing charges for disengaged customers</p> <ul style="list-style-type: none"> • The standing charges are cost-reflective, and suppliers are acting in a rational pricing manner, taking the least-risk approach to recovering their costs in an industry with very narrow margins. The cost-reflective nature of this charging is not driven by the price cap, but by the fixed costs incurred by the supplier. If the standing charges were not cost-reflective, this would expose suppliers to the risk of not recovering their costs. • Whether a tariff is capped or uncapped, suppliers still recover their costs in the same way i.e. p/day and p/KWh basis; the price cap doesn't change the opportunity for supplier innovation on standing charges. Further, even where zero standing charge tariffs exist, we believe that the cost-reflectivity is still driving the pricing structure whereby the first KWh recovers the standing charge. • We welcome the measures Ofgem has been putting in place to ensure market sustainability and believe that standing charge cost-reflective pricing is a key element in this. • From a customer perspective, the SVT is the tariff that vulnerable customers are likely to be on and needs to protect customers who are unable to reduce their consumption or benefit/understand the complex TOU tariffs. Hence keeping these costs in the Standing Charge - and ensuring these are cost-reflective - ensures those customers are paying a fair price. <p>Innovation is already happening and where suppliers have created innovative tariffs, they should be able to beat the cap to reduce standing charges for consumers</p> <ul style="list-style-type: none"> • In our view, the price cap does not create insurmountable barriers to tariff flexibility. Suppliers can and should differentiate themselves not solely on price, but through their service, e.g. offering better customer support, more innovative/greener products, or, in the case of Utility Warehouse, bundling together multiple utilities (energy, broadband, mobile and insurance) through one provider. • UW provides a multi-service offering to its customers via a single set of overheads and passes on the cost savings through a lower standing charge. Our energy products are therefore priced below the price cap and are regularly the best value in the market. UW has an innovative business model and therefore has consistently been able to set the standing charge of all our price-capped tariffs below the zero-consumption cap rate. • E.ON Next also offers a Pledge variable tariff that offers a fixed discount off the Price cap for 12 months¹. Octopus Energy offers a Tracker Variable tariff, this is a

¹ <https://www.moneysavingexpert.com/news/2023/12/e-on-next-opens-tracker-tariff-to-new-customers/>

	<p>smart variable tariff where the rates you pay change every day. In recent months, it's been cheaper than the Price Cap.²</p> <ul style="list-style-type: none"> • Innovation is also possible outside of the cap. For example, suppliers can target specific customer segments resulting in entirely different tariff constructs e.g based on time of day, or by block of consumption. These segment-level propositions operate outside of the default tariff (which is a backstop), and are rather a matter for customers to opt in to. We note such TOU tariffs beginning to emerge along these lines. <p>The price cap is the only mechanism that genuinely protects consumers from unfair pricing and that enables Ofgem to drive down standing charges through scrutiny of costs</p> <ul style="list-style-type: none"> • There are broadly two types of relevant costs: those that are 'per customer' (fixed) in nature and those that are 'per kwh' (variable) in nature and it is essential for market stability that suppliers are able to recover these costs, at a fair price to the consumer. The retail energy price cap is structured to ensure this is the case; it is reflective of both the fixed and variable costs of supplying energy to consumers, through the standing charge and unit rate, respectively. • Ofgem therefore already has at its disposal an effective mechanism to regularly scrutinise the underlying costs that drive the standing charges paid by consumers. This mechanism ensures fairness, accuracy, supplier financeability and market stability. It is a transparent, and technically robust mechanism that effectively delivers its policy intent - to ensure fair pricing. • It is our view that continuing to drive cost efficiency via the price cap mechanism is a better way to ensure fair and cost-reflective standing charges, than to try to engineer (with limited data to enable targeting) an arrangement so that some customers pay less (through cross subsidisation paid for by others). • We believe that to avoid unintended consequences, the price cap methodology must remain a bottom-up cost-reflective assessment of a notionally efficient operator; Ofgem should not introduce cross-subsidisation that could compromise the integrity of the methodology and result in unintended consequences. • Customers protected by the price cap include some of the UK's most vulnerable customers. This safety net is a key pillar in a future market that is financially resilient, transparent, and that protects consumers.
Q2	Why are suppliers not innovating on standing charges for tariffs not covered by the price cap?
	<ul style="list-style-type: none"> • Our response is the same as with Q1. Whether a tariff is capped or uncapped, suppliers still recover their costs in the same way i.e. p/day and p/KWh basis; the price cap doesn't change the opportunity for supplier innovation on standing charges. Even where zero standing charge tariffs exist, we believe that the cost-reflectivity is still driving the pricing structure whereby the first KWh recovers the standing charge.
Q3	What changes could Ofgem make to improve provision for lower standing charges under

² <https://www.moneysavingexpert.com/utilities/stick--switch-or-fix-your-energy-tariff---what-are-the-options-/>

	<p>the cap?</p> <ul style="list-style-type: none"> • <u>Retain the price cap:</u> This is the only policy that can genuinely protect consumers from unfair pricing; it ensures fair and cost-reflective standing charges and provides Ofgem with a mechanism that allows them to drive down standing charges through scrutiny of costs. Cost-reflectivity is an essential pillar of market stability and we caution Ofgem to avoid creating distortions that may decrease market stability or discourage new entrants. Please refer to our Q1 response. • <u>Develop new policy levers to drive up smart acceptance levels:</u> Tariff and standing charge innovation is already happening and should increase once Market Wide Half Hourly Settlement is in place. UW is a strong supporter of the move to MHHS and we have achieved over 70% smart coverage of our customer base. It is important now for Ofgem and DESNZ to seize new opportunities in policy-making that will increase customer uptake in this latter part of the smart rollout. This is the enabler for so much of a net zero retail market e.g. allowing pricing flexibility which will enable suppliers to create tariffs that meet their customers needs. • <u>Work with the Government to develop a progressive, treasury-funded social tariff to sit alongside the price cap:</u> Rather than intervening on standing charges, we believe a social tariff is the most appropriate mechanism to support customers in need of bill support. Where customers have a vulnerability which justifies price support beyond that which is cost justified it is a matter to be dealt with through a centrally funded mechanism - either through general taxation/benefits or through a Treasury-funded social tariff (but this should always be in addition to, rather than instead of, the price cap). • We support the views shared by Citizen's Advice in their recent blog³ on Standing Charges. Tackling the issue of affordability through a low impact - and distortive - intervention on standing charges risks distracting from the development of a more meaningful, long-term, targeted and progressive approach such as a government-funded social tariff. • Given the relatively low positive impact of this proposal, the scope for inefficiency and market distortions, and the regressive outcomes it creates, we do not see a strong justification for an intervention on standing charges.
Q4	<p>As a result of TCR and changes to the recovery of residual costs, domestic consumers with very low consumption now bear a share of fixed network costs which is more in line with the cost of maintaining access to gas and electricity networks. Is this fair? Should more be done to shield these customers from these costs?</p>
	<ul style="list-style-type: none"> • <u>Ofgem has already impact-assessed and decided upon the most equitable and lowest cost to the consumers of distributing fixed network costs.</u> The package of reforms introduced by Ofgem was intended to enable competition, innovation and decarbonisation at lowest cost, and to protect consumers in the transition to a smarter, more flexible and low carbon energy system. We would be concerned about the risk of compromising the integrity of that decision, and possible unintended consequences. <p><u>To shield customers from costs, Ofgem should:</u></p>

³ <https://wearecitizensadvice.org.uk/why-standing-charges-are-fairer-than-you-might-think-0af937499149>

	<ul style="list-style-type: none"> • <u>Develop with the Government a treasury-funded social tariff.</u> This is the most appropriate mechanism to support customers in need of bill support. Please refer to our Q3 response where we describe the benefits of a social tariff. • <u>Continue to use the price cap to protect consumers from unfair pricing.</u> Ofgem should use this to drive down standing charges through scrutiny of costs. Please refer to our Q1 response where we describe the importance of the price cap in keeping standing charges as low as possible. • <u>Maintain cost-reflectivity</u> to ensure market stability and fair pricing for all consumers, particularly those who cannot engage in switching. Please refer to our Q1 response on cost-reflectivity.
Q5	What are the reasons for regional variations in electricity standing charges?
	<ul style="list-style-type: none"> • TNUoS and DUoS charges vary by region, which is then passed through to the customer in order to be cost-reflective.
Q6	Can we learn from other sectors about how to improve suppliers' tariff offering in the UK energy market?
	<ul style="list-style-type: none"> • The water sector compulsory metering programme provides a practical example of how an opt-out metering programme could work. The UK's smart rollout programme could benefit from the learnings of the water industry as we approach the final stages of the rollout and as the need for MHHS increases i.e. as a way of enabling more innovation in standing charges, for example.
Q7	Why do so few suppliers offer multi-tier or zero standing charge tariffs to their customers?
	<ul style="list-style-type: none"> • The standing charges are cost-reflective, and <u>suppliers are acting in a rational pricing manner</u>, taking the least-risk approach to recovering their costs in an industry with very narrow margins. Please refer to our Q1 response where we set out our view that cost-reflectivity drives tariff structure.
Q8	Why are zero standing charge tariffs no longer offered in the market, with the exceptions cited in this paper?
	<ul style="list-style-type: none"> • Please refer to our Q1 response where we set out our view that <u>cost-reflectivity</u> drives tariff structure. • <u>Tariff and standing charge innovation is already happening</u> and should increase once Market Wide Half Hourly Settlement is in place. UW is a strong supporter of the move to MHHS and we have achieved over 70% smart coverage of our customer base. It is important now for Ofgem and DESNZ to seize new opportunities in policy-making that will increase customer uptake in this latter part of the smart rollout. This is the enabler for so much of a net zero retail market e.g. allowing pricing flexibility which will enable suppliers to create tariffs that meet their customers needs.
Q9	What measures could Ofgem take to improve the range of tariffs available to domestic retail customers?
	<ul style="list-style-type: none"> • <u>Tariff and standing charge innovation is already happening</u> and should increase once Market Wide Half Hourly Settlement is in place. UW is a strong supporter of the move to MHHS and we have achieved over 70% smart coverage of our customer base. It is important now for Ofgem and DESNZ to seize new opportunities in policy-making that will increase customer uptake in this latter part of the smart rollout. This is the enabler for so much of a net zero retail

	<p>market e.g. allowing pricing flexibility which will enable suppliers to create tariffs that meet their customers needs.</p> <ul style="list-style-type: none"> • <u>Continue to use the price cap.</u> A cost-reflective price cap ensures fair pricing and market stability; it is not a barrier to innovation in standing charges and it should remain cost-reflective. Whether a tariff is capped or uncapped, suppliers still recover their costs in the same way i.e. p/day and p/KWh basis; the price cap doesn't change the opportunity for supplier innovation on standing charges. Please refer to our Q1 response where we describe the importance of the price cap in keeping standing charges as low as possible. • <u>Cost reflectivity must be maintained.</u> The cost-reflective nature of this charging is not driven by the price cap, but by the fixed costs incurred by the supplier. If the standing charges were not cost-reflective, this would expose suppliers to the risk of not recovering their costs. Please refer to our Q1 response on cost-reflectivity. • <u>Market stability must be ensured:</u> We welcome the measures Ofgem has been putting in place to ensure market sustainability and believe that standing charge cost-reflective pricing is a key element in this.
Q10	Why do no suppliers offer rising block tariff products at present? Would these products offer benefits to consumers?
	<ul style="list-style-type: none"> • Please refer to our Q1 response where we set out that <u>cost-reflectivity is the principle of any tariff design</u>. The standing charges are cost-reflective, and as such suppliers are acting in a rational pricing manner, taking the least-risk approach to recovering their costs in an industry with very narrow margins. The cost-reflective nature of this charging is driven by the fixed costs incurred by the supplier. If the standing charges were not cost-reflective, this would expose suppliers to the risk of not recovering their costs. • It is also important to consider that the <u>complexity of rising block tariffs may pose a barrier</u> for consumers. For example, they may fear an unexpectedly high bill if they are not able to track their consumption, or reduce it where necessary. • A rising block tariff model may also <u>raise concerns for low income vulnerable customers</u> where their energy usage is loosely related to that household's income. For reasons of health or housing type, high users can be very low income and vulnerable customers. Distributional impact analysis conducted by the Social Market Foundation (SMF) in their Energy Bill Support Interim report⁴ suggested that 26% of households in the poorest decile could lose under a rising block tariff, while 62% of the richest would gain.
Q11	How significant an impact do standing charges have on customers' incentives to use energy efficiently? What evidence can you provide that this is the case?
	<ul style="list-style-type: none"> • <u>The overall bill is what drives behaviour:</u> It is our view that the overall cost of energy - the combined cost of standing charges and unit rates - is what drives consumption behaviour. As we have said in response to previous questions, industry fixed costs have to be recovered in order to cover suppliers operational, metering and networks costs. Without a standing charge, these costs would need to be recovered elsewhere, such as through a higher unit rate. • <u>Ofgem should continue to ensure cost-reflectivity via the price cap:</u>

⁴ Energy bill support – designing policies to support British households in an age of high prices 2022-<https://www.smf.co.uk/wp-content/uploads/2022/12/Energy-bill-support-interim-report-December-2022.pdf>

	<p>Cost-reflectivity is what drives tariff pricing; even where zero standing charge tariffs exist, we believe that the cost-reflectivity is still driving the pricing structure whereby the first KWh recovers the standing charge. Ofgem should therefore continue to ensure cost-reflective and accurate standing charges by scrutinising costs via the price cap mechanism. Please refer to our Q1 response where we describe the importance of the price cap in keeping standing charges as low as possible.</p>
Q12	<p>Are there any forms of intervention in standing charges that Ofgem might consider that would minimise the risk of producing negative outcomes for some customers?</p>
	<ul style="list-style-type: none"> • A <u>social tariff</u> is the most appropriate mechanism to support customers in need of bill support. Where customers have a vulnerability which justifies price support beyond that which is cost justified it is a matter to be dealt with through a centrally funded mechanism - either through general taxation/benefits or through a Treasury-funded social tariff (but this should always be in addition to, rather than instead of, the price cap).
Q13	<p>How can we identify the complex needs of vulnerable customers and ensure that they are able to receive tariffs that benefit them the most?</p>
	<ul style="list-style-type: none"> • <u>Work with the Government to develop a progressive, treasury-funded social tariff to sit alongside the price cap:</u> Rather than intervening on standing charges, we believe a social tariff is the most appropriate mechanism to support customers in need of bill support. Where customers have a vulnerability which justifies price support beyond that which is cost justified it is a matter to be dealt with through a centrally funded mechanism - either through general taxation/benefits or through a Treasury-funded social tariff (but this should always be in addition to, rather than instead of, the price cap). Please refer to our Q3 response where we set out why a social tariff is a better mechanism to support vulnerable customers in need of bill support. • We believe that <u>Market Wide Half Hourly Settlement</u> will also be a key enabler in understanding customer behaviour. Thus, we believe Ofgem and DESNZ should now support the <u>smart meter roll-out</u> through new policy levers that increase customer uptake as we enter this final phase of the rollout.
Q14	<p>What issues affecting standing charges in the non-domestic retail sector should we consider further?</p>
	<ul style="list-style-type: none"> • No response