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### “Standing Charges: Call for Input” – So Energy Response

Dear James,

So Energy is a leading energy supplier providing great value renewable electricity to homes across England, Wales and Scotland. We have consistently been recognised by our customers and the wider industry for our outstanding customer service since we were founded in 2015, including being a Which? Recommended Provider and have topped the Citizens Advice’s Supplier League Table. So Energy is one of the early adopters of the EUK Vulnerability Commitment launched in 2020, helping create a better customer experience for vulnerable customers year on year. In August 2021, So Energy merged with ESB Energy, and our combined business now supplies around 330,000 domestic customers. As one of the last challenger suppliers left in the market and one that is backed by ESB’s resources and expertise, So Energy can provide a unique view of today’s energy market.

We understand the context behind this work and certain stakeholders’ requests for Ofgem to consider options regarding the removal of the standing charge, especially considering the increased cost of standing charges post-Targeted Charging Review (TCR). However, we think removing the standing charge is a poor and deeply problematic alternative to a social tariff as it relies on weak proxies for fuel poverty and will result in many wealthy consumers paying less while fuel poor consumers pay more. Our worry is that, should these proposals be enacted, policy makers will consider fuel poverty to have been ‘addressed’ while millions of the most fuel poor will end up paying more.

In our response to the call for input we set out in plain terms our concerns regarding the impact of removing the standing charge under the current price cap on Britain’s most vulnerable energy consumers. According to our reading of the questions, Ofgem are trying to address the following problems:

1. Customers want greater control of their bill and find standing charges inherently unfair.
  - a. Standing charge rates have also increased which has exacerbated the point above.
  - b. Ofgem are now thinking about redistributing or repackaging these charges in response to calls from stakeholders.
2. There is a lack of innovation/variety in the form of tariff offerings in the market. If suppliers had tariffs without a standing charge on offer, then customers would be able to pick these tariffs if they wished, and Ofgem would not need to consider a regulated solution to the use of standing charges.
3. Removing the standing charge will inevitably result in ‘winners’ and ‘losers’ and the amongst the losers will be some of Britain’s most vulnerable households. Ofgem want to try to prevent there being losers if it decides to remove standing charges from the market.

Having read the call for input, we agree with Ofgem's analysis regarding the issues that would arise if the standing charge were removed, but would add greater emphasis and clarity with the following points:

1. We agree with Citizens Advice's view that consumers understanding of standing charges are flawed. Consumers believe that the removal of the standing charge will save them money, however, this in most cases is incorrect. Tariffs with no standing charges, include risk premiums and simply redistribute the standing charge fees across to the unit rate. This means unless the customer is a super low user, they will very likely pay more for their energy than they would have with a tariff that has a standing charge. At the same time, most vulnerable and low-income/high usage consumers would face even higher costs than they do today<sup>1</sup>. Therefore, any attempt to address consumers concerns about the increased costs of the standing charges or around lack of control over having to pay a standing charge will only make things worse. The regulator, suppliers and consumer bodies must all play a role in educating consumers on these dynamics.
2. The price cap stifles innovation - it changed the regulatory landscape of the competitive market which in turn has resulted in a change of behaviour from suppliers. New rules mean new commercial realities, in this case, the price cap presented greater risk to recovering fixed costs<sup>2</sup> from tariffs like rising block or multi-tier offerings, as there is a cap on how much we can compensate for the loss of the standing charge by increasing the unit rate. This is a fundamental issue and will exist as long as the price cap exists. To address this, the price cap must be removed and some form of targeted support for vulnerable customers introduced in its place (such as a social tariff<sup>3</sup>). Under the price cap, there is no simple solution to removing the standing charge, it results in proposals with significant unintended consequences which further complicate the market, such as we have seen with tariff levelisation.
3. So Energy believes that consumers as a whole should be charged at the lowest and most cost reflective manner possible. Then, issues of fairness and ability to pay should be addressed through a social tariff or other form of targeted support. For us this means keeping the standing charge in place, removing the price cap, and implementing a social tariff to address affordability issues. This in turn will likely result in greater innovation of tariff offerings as it returns control of pricing and hedging to suppliers.
4. We note that Ofgem have not considered the potential impact the removal of the standing charge will have on investors confidence in the supplier and network market. This should be factored into the decision-making process.

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<sup>1</sup> [Why standing charges are fairer than you might think | by Alexander Belsham-Harris | Dec, 2023 | We are Citizens Advice](#), Citizens Advice, 19/12/2023

<sup>2</sup> Standing charges are made up of; residual charges (costs of providing existing pylons and cables, and the differences in charges faced by smaller distributed generators and larger generators), supplier operating costs and SoLR mutualisation. For the purpose of this consultation we will refer to these as fixed charges.

<sup>3</sup> When we refer to social tariff in this response, it is a catch-all phrase for cross subsidies that benefit fuel poor energy consumers. The WHD would qualify as a 'social tariff' in this instance.

**Q1: What are the barriers to suppliers using the existing flexibility under the price cap?**

The price cap is the barrier. The price cap makes anything other than applying a standing charge, commercially unviable. For example, if standing charges were removed and the price cap remained, we would have to recover the costs of the standing charge via the unit rate. In addition to recovering the lost standing charge revenue, would have to include a risk premium, in case consumers use less energy than the price cap benchmark. So, removing the standing charge would either take us over the cap or if it were a fixed price product would make it too expensive to attract customers (due to the addition of risk premiums). The research makes clear that customers switch tariff/supplier firstly for lower price (73%)<sup>4</sup>. Some might argue that a standard single rate tariff product with no standing charge (but with the fixed charges distributed to the unit rate and risk premiums included) will still attract low users, such as second homeowners. However, this would also not be commercially viable to suppliers, and we would essentially be left at the end of the contract with most of our fixed costs left unpaid.

**Q2: Why are suppliers not innovating on standing charges for tariffs not covered by the price cap?**

The introduction of the price cap meant that the rules of the market changed and therefore the strategy of suppliers changed also, resulting in less innovation. In addition to the points made to the former question, we reiterate that it simply is not commercially viable. The price cap is the main barrier. Under the price cap, the risk of not recovering the full balance on the fixed charges is very high. If the standing charge were moved to a volumetric basis, then there would be a risk that the low energy consumer would not consume enough energy to cover the 'nil consumption cap level' or 'fixed charge'. To ensure we recover the costs, we would have to increase the unit rate by the fixed charge amount and then include the appropriate risk premiums, under the cap this is not possible to do.

**Q3: What changes could Ofgem make to improve provision for lower standing charges under the cap?**

Any kind of removal or reduction of the standing charge without the appropriate remedial action will create winners and losers. The fixed charges faced by suppliers are deliberately set with regards to funding the future of the electricity network and therefore removal of those charges is not an option, the bill needs to be paid. Ofgem in its TCR decision state that they "decided to make changes to the way in which some of the costs of the electricity networks are recovered, so that the 'residual charges' are recovered more 'fairly' now and in the future. We have also decided to remove some remaining distortions called 'non-locational Embedded Benefits' which can increase costs for consumers and affect competition."<sup>5</sup> In other words, what fees make up the network element of the standing charge, have been reviewed and restructured to provide a fairer and lower cost outcome. Given that the bill must be paid and that everyone uses the energy grid infrastructure, Ofgem could request that some or all of the fixed charges are shifted over to general taxation.

Ultimately, the best approach is that the price cap be removed and replaced with a social tariff in order to lighten customer financial burdens related to standing charges.

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<sup>4</sup> He, X., & Reiner, D. (2017). Why Consumers Switch Energy Suppliers: The Role of Individual Attitudes. *The Energy Journal*, 38(6), 25–54. <https://www.jstor.org/stable/26534389>

<sup>5</sup> <https://www.ofgem.gov.uk/publications/targeted-charging-review-decision-and-impact-assessment>

**Q4: 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?**

In Ofgem's TCR decision it concluded that moving residual charges to a fixed network charge under the standing charge would result in greater fairness, reduce harmful distortions and is proportionate to the benefits that the changes are expected to bring for consumers<sup>6</sup>. We note that had the TCR not been implemented, consumers would have paid even more during the recent energy crisis. We think to go back on this would undermine the decision and impact assessment from that previously undertaken for the TCR. If Ofgem do abolish standing charges and require suppliers to recover those residual fixed charges in addition to the other fixed charges via unit rates, they will essentially undo the benefits of TCR as risk premiums will need to be added to account for transferring fixed costs into variable charges. Ofgem understood the importance of the fixed charges to the future of the electricity network - putting the collection of those fixed charges at risk by collecting via a unit rate, does not make sense.

**Q5: What are the reasons for regional variations in electricity standing charges?**

The cost to deliver energy through the network to end users differs depending on the location of the customer. This is something Ofgem could alleviate through some form of cross subsidy between network operators, but it's complicated.

Then there is the consideration to the Review of Electricity Market Arrangements (REMA). REMA has been looking at zonal and nodal pricing on the wholesale level. It would seem inconsistent to push for the regionalisation of energy charges upstream, only to pursue the opposite downstream. This could also remove incentives on where to site generation assets and increases cost through the introduction of risk premiums. Essentially, Retail and Wholesale markets need to align on whether charges should differ regionally.

**Q6: Can we learn from other sectors about how to improve suppliers' tariff offering in the UK energy market?**

As seen with some of the examples given by Ofgem, most industries are moving towards fixed charges (like standing charges) rather than volumetric pricing. This makes sense because people value the certainty of a fixed charge. For example, many people now choose mobile deals that come with unlimited minutes, texts and data. No one ever needs that much data or minutes but for a fixed charge, they won't need to top up and they know they can't exceed the bill amount agreed. It gives them assurance. This works well because running out of minutes and data is something most people would have experienced and as a result have placed value on a fixed offer. They have a learnt experience that tells them fixed price deals are a good thing. To compare this with energy, the standing charge should assure customers that they will contribute to Net Zero and fund the maintenance and repair work of the energy system we all rely on but this doesn't appear to be well understood. We think the greatest lesson we could take from other sectors is how to educate customers on the charges on the bill. Customers should know that without the money recouped via the standing charge there is funding for our critical national energy grid infrastructure, upon which modern civilisation relies.

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<sup>6</sup> [Targeted Charging Review: Decision and Impact Assessment | Ofgem](#), P.23, 2019.

**Q7: Why do so few suppliers offer multi-tier or zero standing charge tariffs to their customers?**

So Energy do not offer zero standing charge tariffs because of the risk associated with recovering the fixed costs the variable unit rate. From a customer cost perspective, suppliers will have to increase the unit rate to make up for the loss of the standing charge and add a risk premium to ensure the fixed costs are recovered, should customers use less than expected. Therefore, it's likely that customer with typical usage will end up paying more while high users, including some vulnerable customers, will pay much more. From a supplier cost recovery perspective, we would be playing a risky game trying to recover the fixed costs via the unit rate when we have much greater certainty recovering fixed costs via a standing charge.

It is worth noting the question of whether to abolish the standing charge has arisen in the past and the standing charge has always been retained; 'When the price cap on gas was first reviewed in 1991, Ofgas considered the implications of rebalancing the tariff by reducing the standing charge, but found no convincing arguments on efficiency or equity grounds to do so.'<sup>7</sup> Tampering with the standing charge is not a new consideration but as seen in the 90's, the standing charge provides certainty and lower cost outcomes.

In addition, offering multi-tier tariffs would require billing system changes and it is unlikely consumers would find such offerings to be compelling. We do not think there is enough demand from customers to make this kind of investment.

**Q8: Why are zero standing charge tariffs no longer offered in the market, with the exceptions cited in this paper?**

The market changed in 2019 when Ofgem introduced the price cap, with that suppliers' strategies also changed to adapt to new risks and offering a tariff with no standing charge under the cap would be commercially unviable. Beyond the immutable issue of the price cap, two further issues arise that suggest offering a tariff without a standing charge may be unwise.

Firstly, the energy market is changing and has an increasing number of customers generating their own electricity (via solar panels) and therefore not using much, if any, electricity drawn from the grid (so recovery of the fixed charge will be completely unobtainable via the unit rate)<sup>8</sup>.

Secondly, the energy market has seen a huge increase of payment difficulty issues and bad debt<sup>9</sup> - forcing low income, high energy users, who are already most at risk, to pay even more for their energy is irresponsible.

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<sup>7</sup> Hancock, R., & Price, C. W. (1995). Competition in the British domestic gas market: efficiency and equity. Fiscal Studies, 16(3), 81-105.

[https://scholar.google.com/scholar?hl=en&as\\_sdt=0%2C5&q=Competition+in+the+British+domestic+gas+mar ket%3A+efficiency+and+equity&btnG=](https://scholar.google.com/scholar?hl=en&as_sdt=0%2C5&q=Competition+in+the+British+domestic+gas+market%3A+efficiency+and+equity&btnG=)

<sup>8</sup> Targeted Charging Review: Decision and Impact Assessment | Ofgem, 2019.

<sup>9</sup> <https://www.ofgem.gov.uk/publications/energy-regulator-sets-out-proposals-help-ensure-customers-risk-getting-debt-are-better-supported#:~:text=However%2C%20energy%20prices%20are%20still,led%20to%20unpaid%20energy%20bills.>

The only way to make a multi-tier tariff commercially viable as an alternative to a standing charge is to make the first few kWhs used so expensive that it collects the full day rate of the fixed charge in the unit rate. However, as Ofgem has pointed out in the call for evidence, ‘a break point this low means the payment of a high initial unit rate is essentially unavoidable and effectively acts as a standing charge, unless the customer uses no energy at all that day’<sup>10</sup>. From a So Energy perspective, we believe mandating multi-tier tariffs of this sort instead of a standing charge is inherently deceptive to customers who think they’re escaping the standing charge but are in fact facing a similar or worse (when risk premiums are taken into account) outcomes.

As Citizens Advice points out, while that tariffs with no standing charges could protect consumers with low energy use by ensuring their essential needs are met and increase incentives for higher users to reduce their usage, “there is a relatively loose correlation between income and energy usage. Analysis of this type of approach showed that 26% of households in the lowest income decile would be worse off, while 62% of the richest would gain.”<sup>11</sup> Some customers have no control over their energy consumption and have highly inefficient home heating and appliances. For example, a customer can be very frugal with their energy consumption in a new build and live very comfortable with low energy use. That same individual in a much older, less efficient house, is instantly going to have to pay significantly more to reach anything close to the first scenario’s level of comfort.

While the standing charge has increased in recent years, this is a small part of a much bigger problem relating to the nation’s struggle with recent cost of living increases. All meaningful changes required to address this fundamental issue can only be made at government level by removing the price cap and replacing it with a social tariff. Any amendments to the standing charge will be futile and we strongly encourage Ofgem to put its efforts into informing the government of the detriment the price cap is having on the market and need for a social tariff instead.<sup>12</sup>

**Q9: What measures could Ofgem take to improve the range of tariffs available to domestic retail customers?**

The only thing Ofgem can do is advocate for the removal of the price cap. Failure to remove the cap has resulted in less choice, less investment and less innovation. The price cap was always supposed to be a temporary measure and is no longer suitable for the current market. Instead, we need more targeted approach the less well-off, such as a social tariff<sup>13</sup>. If the government removes the cap and introduces a social tariff (or something that provides targeted support) we would see suppliers innovate with tariffs once again, while ensuring vulnerable customers are protected.

**Q10: Why do no suppliers offer rising block tariff products at present? Would these products offer benefits to consumers?**

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<sup>10</sup> [Standing charges – call for input | Ofgem](#) p.36, 2023.

<sup>11</sup> Citizens Advice, Ripping off the band-aids, <https://www.citizensadvice.org.uk/about-us/our-work/policy/policy-research-topics/energy-policy-research-and-consultation-responses/energy-policy-research/ripping-off-the-band-aids/23/11/2023>

<sup>12</sup> Littlechild, S. (2021). The challenge of removing a mistaken price cap. *Economic Affairs*, 41(3), 391-415. [https://scholar.google.com/scholar?hl=en&as\\_sdt=0%2C5&q=The+challenge+of+removing+a+mistaken+price+cap&btnG=](https://scholar.google.com/scholar?hl=en&as_sdt=0%2C5&q=The+challenge+of+removing+a+mistaken+price+cap&btnG=)

<sup>13</sup> Littlechild, S. (2021). The challenge of removing a mistaken price cap. *Economic Affairs*, 41(3), 391-415. [https://scholar.google.com/scholar?hl=en&as\\_sdt=0%2C5&q=The+challenge+of+removing+a+mistaken+price+cap&btnG=](https://scholar.google.com/scholar?hl=en&as_sdt=0%2C5&q=The+challenge+of+removing+a+mistaken+price+cap&btnG=)

There is no way to offer a commercially viable rising block tariff within the current price-capped market. We wouldn't be able to recover our costs. A rising block tariff would attract low energy users, meaning suppliers would not cover their fixed costs, rendering it commercially unviable. To counter this risk, we would need to include substantial risk premiums which would then make the rising block tariff too expensive to be an attractive commercial proposition.

**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?**

We do not think the standing charge currently impacts customer's decision making to be more energy efficient. Second homeowners would benefit greatly by having a non-standing charge tariff, but we do not think this is energy efficiency driver, as the property is already not using much energy anyway (which is what makes the tariff attractive in the first place). If customers understood the make-up of the standing charge, then perhaps this would encourage customers to pick tariffs with a standing charge so they can help fund Net Zero, which involves a move away from commodity driven costs.

If anything, we think a standing charge has the potential to incentivise customers to step away from gas and make the transition to electrifying their home entirely, because they'd reduce their standing charges from 2 to 1. Ofgem should consider how removing the standing charge would affect customers not only on low incomes but also customers who have taken steps to reduce their carbon footprint by purchasing an EV and consequently installed an EV charger. These are high energy users who would end up paying more if the standing charge was removed.

**Q12: 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?**

Not that we can foresee. If you remove the mechanism that was specifically designed to recover charges fairly and efficiently (via the TCR review) and move it on to volumetric charges, Ofgem will inevitably see negative outcomes. Those most at risk of this intervention, high energy users, are some of Britain's most vulnerable customers. To really be able to come up with an intervention, we need to understand the desired outcome from stakeholders calling for the removal of standing charges:

1. If they want to replace the standing charge with a higher unit rate or rising block tariff then they have to accept that most consumers will pay more for their energy, this is a fact.
2. If they want increased transparency, then Ofgem should produce guidance on the all the fixed costs that make up the standing charge, rather than pretending these costs don't exist.
3. If they want a reduction in the fixed charges that make up the standing charge, then we have to reverse the TCR and accept that meeting our Net Zero targets will be more expensive than it needs to be.

We don't think any of these outcomes are the desired outcomes because the real issue is not the standing charge. We think the root cause of all the issues raised by various stakeholders is the overall cost of energy, which is best addressed by keeping the standing charge in place, removing the price cap and implementing a targeted social tariff. The increase in discourse around removing the standing charge correlates well with the overall energy crisis.



We're aware that some stakeholders have suggested reconciliation or true up mechanism would somehow address the issues presented by removing the standing charge. However, as we have made clear in our response to Ofgem's consultations on payment method levelisation, we see this mechanism as unforecastable and unmanageable, adding greater complexity to what is already a very complicated market. In the interest of transparency and minimising ugly unintended consequences, we strongly discourage the use of reconciliation mechanisms.

**Q13: How can we identify the complex needs of vulnerable customers and ensure that they are able to receive tariffs that benefit them the most?**

Registering vulnerability in energy is an honour system (in its current context of the PSR), there are no eligibility checks. Everything is done on trust. To create a system whereby vulnerable customers benefit financially from a special tariff would undermine the current energy honour system. If existing government data was to be used to identify vulnerable customers, then it would be simpler and more straightforward to enhance the existing WHD.

Our concerns, aside from creating a risk where currently there is not one (making suppliers recover fixed charges via a unit rate), is that high users and low users are not strong indicators of wealth. We agree with Ofgem's own assessment that 'Amongst households with the lowest incomes, whilst five million households would benefit from a measure to shift electricity costs from standing to volumetric charges, one million would lose out'. As a supplier it's hard to support this proposal when the one million who lose out are likely to be high users due to circumstance out of their control – rented housing conditions, health, age and old and inefficient appliances – these customers are most at risk as their energy costs are already high. Furthermore, Ofgem noted 'whilst the overall effect would be progressive, those lower-income households that would lose out would see an increase in their bills by twice as much as gainers would see their bills fall'<sup>14</sup>. That analysis has not factored in the risk premiums that suppliers will need to include on tariffs with no standing charge – we would expect Ofgem to factor this consideration into any future analysis and report its findings. However, if we keep the standing charge in place and replace the price cap with a social tariff, the most at risk consumers should all benefit from reduced energy costs - suppliers would not need to include a risk premium and no vulnerable customer would have to pay more because they live in poor quality housing.

The last consideration that we do not think Ofgem have fully factored in is the likely increase on electricity usage to come in the near future with the use of heat pumps and EV charging. With no standing charge, these green seeking technology customers will face a much higher unit rate and therefore pay more for moving away from fossil fuel solutions. To add to the complication, the growing number of domestic solar and battery customers makes it increasingly difficult to set the right rate to recover the fixed charges as they will be using less. It's difficult to see how Ofgem can reconcile these complex issues. Other solutions, such as a social tariff, are better suited to addressing these conflicts.

Regards,

Joshua Field  
Regulation Manager

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<sup>14</sup> [Standing charges – call for input | Ofgem](#), p.8, 2023.