

Dan Norton
Deputy Director, Price Cap
Ofgem
10 South Colonnade
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Dear Dan,

Thank you for the opportunity to give input into this discussion on Future Price Protection.

About Nous

Nous is an AI-powered 'copilot' that cuts bills for UK households by many hundreds of pounds a year. Nous saves money and time by intelligently managing services including energy, broadband and mobile, finding fair deals for its members with new and existing suppliers, monitoring service levels and pro-actively switching its members as required.

Nous believes a well-regulated market has four qualities:

- A healthy, vibrant and competitive landscape of suppliers that results in good consumer outcomes
- Innovation among suppliers and distributors to meet the needs of both engaged and disengaged customer segments
- Light touch regulation to ensure the above remains true and significantly adverse consumer outcomes are discouraged or prevented
- Support, ideally financed by government, as it is at heart a welfare and taxation initiative) for the truly vulnerable and those unable to pay for the energy they reasonably need

While an unusually high degree of intervention may have been necessary during the energy crisis, we believe it is of critical importance that Ofgem now seeks to reduce the level and extent of its regulatory intervention in order to allow private actors to compete effectively.

The emergence of MHHS and the transition to Net Zero, presents an opportunity to do this and to approach regulation differently. We would encourage Ofgem to seize this moment to transition back to much lighter touch regime, while continuing to monitor actors to ensure fair and acceptable consumer outcomes.

Yours faithfully



Greg Marsh
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Q1. Do you have any reflections on our list of the cap's successes and challenges?

Summary

- The Energy Price Cap (EPC) worked in the context in which it was designed
- The EPC is no longer fit for purpose, is inhibiting competition and leading to poor consumer outcomes
- The public is dissatisfied with a market that is failing to deliver good service or value for money

The Energy Price Cap (EPC) worked in the context in which it was designed

The EPC was designed to protect consumers against unfair pricing, with Ofgem estimating the “loyalty penalty” was costing consumers £1.5bn a year. Historically consumers faced a two-tier market, with disengaged customers who remained on expensive default tariffs as a function of their inertia effectively subsidising cheaper pricing for those who switched regularly.

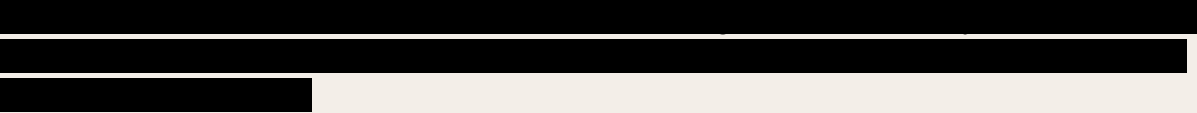
[REDACTED]

With the support of healthy price competition, these distribution innovations, along with significant market entry from new suppliers, ensured consumers enjoyed generally favourable outcomes:

- Switching reached record levels in 2019
- The 50% of the market who remained on default tariffs were protected from excessive pricing
- Fixed tariffs were lower for the 50% who did actively engage actively in the market
- Incumbent suppliers were encouraged to cut their operating costs
- Distributors as well as suppliers were encouraged to innovate to serve less engaged consumers

Distributors were incentivised to innovate to meet the needs of less engaged customers

[REDACTED]



The EPC is no longer fit for purpose and is leading to poorer consumer outcomes

The energy crisis was a Black Swan event caused by unprecedented spikes in wholesale prices. Many challenger suppliers had insufficiently hedged for this contingency and failed. As a result the market is now markedly concentrated, dominated by a small number of large suppliers and closely resembles a cosy oligopoly.

Compounded by other inhibitory regulatory interventions such as BAT and MSC, the EPC has become the de facto price for 90% of households and protects only the interests of large suppliers.

Customer electricity switching remains only 38% of pre-crisis level¹ This is driven by the lack of meaningful savings a customer can achieve for switching.

The cheapest large supplier fix at the time of writing is only 6% cheaper than the EPC. Pre-crisis it was common that customers would achieve savings of 25% vs the cap when switching. Consumers today therefore have little incentive to shop around for better deals. This has the effect of reducing the proportion of engaged consumers and breeds complacency and apathy.

Furthermore, since suppliers are effectively guaranteed a 2.4% profit margin, those with large established customer bases have no real incentive to invest in discounting or innovation in order to win new customers or improve service for their existing ones. Having ~90% of your base on an SVT without fear of losing them to competitors is a cosy place to be for a large incumbent.

Heavy-handed regulation combined with poor consumer outcomes results in exploitative supplier behaviour which may prove politically unsustainable

High salaries for bosses of large energy suppliers make for challenging news headlines and are only ever publicly acceptable if the companies in question are seen as offering a good service and value for money. Energy companies are once again seen as parasitic and exploitative.

Today we have a notionally privatised market, with private sector pay levels and increasingly robust returns to shareholders, but without effective competition. This will become politically unsustainable and is demonstrably resulting in poor consumer outcomes (see chart below).

Suppliers seeking to reduce operational costs to meet EPC targets have instead cut back on their customer services expenses. As a result, customer satisfaction with the ease of contacting their supplier has declined since the EPC was introduced.



Source: Ofgem

Q4. How quickly and at what scale do you expect customers, especially those with large flexible loads such as EV and solar/battery users, to take up ToU tariffs once MHHS is implemented?

Summary

- Those with large flexible loads have the most incentive to move to a TOU tariff
- There are infrastructure challenges to overcome to improve adoption rate

Those with large flexible loads have the most incentive to move to a TOU tariff and are most likely to do so quickly

This is the most engaged sector of the market made up of those who were likely to have been a regular switcher in the past. High financial incentives and high engagement mean they are likely to adopt TOU tariffs quickly, providing the regulatory environment enables this to happen.

There are challenges to overcome to improve adoption rate

However, the pace of adoption may be slowed by infrastructure challenges and consumer engagement. A Zap map survey from 2023 found that smart meter uptake was might higher than average amongst EV owners but that 28% were still without a smart meter. Further to that, 34% of households have no off street parking, excluding them from the benefits of TOU for EVs²

In 2022 only 1 in 4 EV drivers had a TOU tariff, implying issues around consumer engagement.

Q6. Do you agree that we need to retain some form of price protection in the retail market?

Summary

- Current price protections cause more harm than good
- Low income and vulnerable consumers should be protected
- Lighter price protection is crucial for delivering net zero goals

Current price protections risk causing more harm than good

There is some risk of exploitation for vulnerable and disengaged consumers if price protection were removed entirely. On balance however this risk is outweighed by the real harm resulting from Ofgem too tightly controlling pricing in the manner it has been for the last few years, resulting in low levels of competition on price and service. When consumers see little or no difference among suppliers, it breeds disengagement and cynicism, which obliterates the benefits of privatisation.

Competition should be the primary means of disciplining suppliers – with guardrails for vulnerable consumers

Ofgem should encourage market competition – rather than regulation – to discipline energy suppliers, while maintaining price protection for at-risk customers only. The bold way to do this is by removing all price protection except in respect of vulnerable or low income groups.

For unengaged consumers, a competitive market would once again see the emergence of Assisted Switching Services, further enabled by the ubiquity of AI and other new technologies to provide decision support and practical assistance to lower-engagement consumer groups to help them navigate complex markets or purchase processes.

Lighter price protection is necessary to deliver Net Zero

It is very hard to regulate for a market that is yet to become established and there's a real risk that over-regulation interferes with emerging innovation.

To give TOU the best opportunity to grow, Ofgem should let the market develop with lighter touch regulation to allow market solutions to develop that create conditions for price protection.

Q7. Do you have views on which of the three key parameters – the cap being flat, universal and stringent - should be relaxed when considering future price protection

Summary:

- Stringent nature of the cap could be relaxed in favour of a supplier relative cap
- A phased approach would help unlock short term benefits and long term market health

Stringent nature of the cap could be relaxed in favour of a supplier relative cap

Our preferred method of “light” regulation would be to move from a stringent cap to a supplier relative cap, where suppliers must set their default tariff price within a permitted variance of their cheapest fixed tariff. This could be the best balance that would allow sufficient price protection for unengaged customers without overly restricting supplier hedging strategies that could inhibit price competition. It could also be adapted across different tariff types, with additional provisions set for vulnerable customers around social tariff.

We acknowledge the risk that the system could be ‘gamed’ by suppliers increasing prices of cheaper tariffs rather than reducing prices of default tariffs. Hence we propose that vulnerable customers be afforded separate price protections so as to be at less risk of detriment. Ofgem should continue to monitor closely to assess whether competition was sufficient to ensure fair outcomes. Ofgem can also call out bad actors, and publish expected “best prices” for consumer visibility.

[REDACTED]

A phased approach would help unlock short term benefits and long term market health

Transitioning from a stringent to a supplier relative cap whilst removing the BAT at the first possible opportunity could help to unlock short term competition whilst offering consumers assurance that price protection is still there.

Q8. What are your views on options discussed? Do you have any preferred options or combination of options?

Summary:

- Market wide price protection could have catastrophic effects if consumers are not incentivised to participate in TOU
- Caps on dynamic TOU peak rate pricing could build consumer trust
- A permanent ban on acquisition only tariffs in a healthy market inhibits competition and thereby harms consumers

Market wide price protection could have catastrophic effects if consumers are not incentivised to participate in TOU

Providing flat and universal price caps for MHHS could dampen price incentives to change behaviour. This would prevent mass market savings from MHHS, by removing the incentive for large numbers of households to respond to price signals to balance their usage. This would prevent price competition and slow progress to Net Zero goals.

However, caps on dynamic TOU peak rate pricing could build consumer trust

A targeted price cap on peak rates would help encourage adoption of TOU for those concerned about spikes in wholesale rates.

Capped unit rates on dynamic tariffs, similar to those seen with Octopus's Agile tariff where prices are capped at 100p/kWh, are easy to understand and provide reassurances that customers will not be stung by volatile short term pricing. This is especially effective communicated alongside the average rate you can expect to pay.

Given the success of the Octopus Agile tariff and their self imposed cap, suppliers may see the value of following this approach to build trust with customers without Ofgem intervention.

A permanent Ban on Acquisition-only Tariffs in a healthy market inhibits competition and thereby harms consumers

While the principle of not offering new customers better pricing than existing ones has moral standing, it has evidently served to reduce the incentive for suppliers to offer competitive pricing on new tariffs. We strongly contend that the BAT is harmful to consumer outcomes and would encourage Ofgem to remove it at the first opportunity.

Q9. In particular, which options or combination of options do you think would best protect vulnerable customers?

Summary

- **Energy affordability is a public policy issue**
- **Targeted bill support is needed to help low income and vulnerable customers**
- **Specific price protection may still be required for TOU**

Energy affordability is a welfare issue

Because households must purchase energy in order to live comfortably, high energy costs act as a form of regressive taxation, absorbing a disproportionate share of household income for lower income groups. Energy affordability is therefore a public policy issue in which government intervention would be the ideal solution.

Targeted bill support is needed for low income and vulnerable customers

In the current market, fuel poverty and debt are a growing concern and action is needed quickly. Targeted bill support should be the first priority, delivered either through existing Warm Home Discount measures or through the introduction of a social tariff, ideally tax-funded.

Further interventions might include a universal right to a basic amount of energy for those who meet certain thresholds, delivered through existing measures or a non-profit state-run energy company.

Measures such as this would both require bold thinking from Government, but would negate the need for stifling price protection and allow Ofgem to focus more narrowly on matters related to market function. After all, other sectoral regulators are not expected to ensure socially equitable outcomes; these are effectively questions of wealth and income distribution which ought rightly to proceed from an electoral mandate.

Specific price protection may still be required for TOU

Long-term protections are needed for consumers who have no choice but to use more energy at peak times and will be exposed to high pricing.

Notwithstanding this, action is needed to tackle issues affecting consumers right now, and in the long-term under TOU pricing structures.

Q10. How should consumers with large flexible loads, mainly EV and solar/ battery users, be treated with regards to future price protection?

Summary:

- EV/Solar users on a TOU tariff are likely to be the most engaged in the market
- Low risk of customer detriment in this group
- Ofgem should let this market develop before implementing price protection

EV users on a TOU tariff are likely to be the most engaged in the market

Just as those driving a petrol or diesel vehicle would drive out of their way to get cheaper fuel, EV drivers will change behaviour and shop around for a tariff if they see the value in doing so.

Ofgem should let this market develop before implementing price protection

Earlier adopters to TOU tariffs are more likely to be engaged in the market, meaning less risk of allowing this part of the market to develop with lighter regulation.

Our recommendation would be to define a set of acceptable customer outcomes to monitor, but to not activate any price protection for those specifically on EV tariffs unless a risk of significant customer detriment emerges.

¹ Energy UK Electricity switching March 2024

<https://www.energy-uk.org.uk/wp-content/uploads/2024/04/Electricity-Switching-Report-March-2024-final.pdf>

². <https://www.zap-map.com/news/electric-cars-gateway-clean-energy>