

energywatch's response to

OFGEM'S PROPOSED CORPORATE STRATEGY 2004-7

Introduction

energywatch welcomes the publication of Ofgem's Corporate Strategy and believes that it has identified the key themes for the next three years. We also welcome the commitment given in the Foreword to full and open consultation, the readiness to consider evidence and arguments which challenge Ofgem's policies, and the commitment to explain the approach that has been chosen.

In particular, we think that creating and sustaining competition is of prime importance for energy consumers. It is also increasingly necessary for Ofgem to respond to the new challenges presented to the industry such as the increased regulation and legislation from the EU, and promoting and protecting the environment.

energywatch notes that Ofgem will be consulting on their Corporate Plan in March. We look to that document to set out in considerably more detail the measures and actions that Ofgem will be taking under each of the key themes to protect the interests of consumers.

The response will first consider additional approaches or themes that might have been included, and areas of the plan that could be improved upon. Part II will comment in turn on the themes identified by Ofgem in the document. Finally part III of the response will summarise the ways in which energywatch could productively work with Ofgem in developing a compliance agenda.

PART 1 HOW THE PLAN COULD BE IMPROVED

Defining a regulatory philosophy to inform Ofgem's plan

Whilst we accept this is a high level planning document it would have been useful to outline a set of principles or values that Ofgem intend should inform their strategic direction. The section "better regulation" does not fully address this purpose and is very generic. We would have liked Ofgem to articulate a long term regulatory philosophy. In particular there are references to both market and regulatory solutions in the document. It would have been useful to see a broad summary of what guiding principles would underpin a decision to use a market solution over a regulatory one (for example the use of cross subsidy or cost reflectivity). We note for example, that the OFT's Annual Plan sets out the organisation's values (chapter 2) and a set of principles that underpin its strategy (Chapter 3 Para 3.3).

Keeping the corporate plans relevant throughout the planning period

We believe Ofgem need to consider which of the themes they have identified in 2004 will be relevant in 2007. If the themes are too loosely defined to account for almost any future event, they will be of little use for planning purposes and may even create regulatory uncertainty. It is possible to imagine a number of scenarios that would require different regulatory solutions. For example after around 2007 the UK will become a net importer of gas (Transco Ten Year Statement) but it is not known exactly where the gas will be landed (LNG or from the interconnector) or even the implications of changes to gas quality. It would therefore have been appropriate to consider a regulatory version of scenario planning in this document to indicate at the broadest level how Ofgem's might alter its themes accordingly. An example of how this might be achieved by considering the external environment can be found in the Financial Services Authority Plan and Budget (2002-3) as it attempts to consider the interaction of the external environment and regulation by considering the "wider context of their work" (p13).

Prioritising and defining strategic aims

As a consequence of not defining a clear philosophy or how the external environment could change it is difficult to understand how Ofgem intends to prioritise and define its strategic aims. Can we assume that theme 1 "creating and sustaining competition" has a higher priority than "helping tackle fuel poverty" (theme 7)? If each is equally important then can we assume that equal priority be given to both?

A number of other regulatory bodies define high level strategic aims and strategic outcomes. It would have been helpful to consider such an approach as an integral part of the themes identified in the document.

Evaluating performance against strategic plan

In order to develop its corporate strategy it would have been helpful to include some indication of how Ofgem's performance could be measured as it progresses these themes. Even a relatively high level commentary on broadly defined indicators would add real value to the document. For example a simple table indicating the stated aim of the objective, relevant indicators, what the particular indicator tells the regulator. The targets could be aggregated in order to develop a high level set of key performance measurements.

Resource allocation

Some indication of resource allocation would have been useful. Clearly some activities are more expensive to implement than others but nevertheless a broad indication of expenditure on the themes would improve the plan.

It is also prudent to consider demonstrating value for money as an integral part of the planning documentation.

Contingency planning and risk

Finally, the presentation of the plan might be improved by including a risk assessment and a contingency plan. The sale of NGT's gas networks is a case in point. Ofgem will need to devote substantial resources to a wide ranging

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regulatory problem not included in its original work plan. There needs to be included in the strategy-

- Scope for re prioritisation if for example Ofgem initiates a market investigation as a result of an application of a super complaint or a merger referral.
- Contingency planning if it looks like Ofgem is falling short of a strategic goal.

The missing theme: a compliance perspective

energywatch's principal general comment on the Corporate Strategy relates to compliance and enforcement. Ofgem state in the foreword, under the heading of Better Regulation, "we shall make vigorous use, wherever necessary, of the enforcement powers we have under energy and competition legislation." Given the positioning of such a statement, it would be logical to conclude that Ofgem's compliance strategy would assume a position of significance in their Corporate Strategy.

Paragraph 2.7 states (in the context of wholesale markets) that where abuse in the market is found vigorous action against companies will be taken, but that is the only direct mention of their compliance activity in the document. Ofgem acknowledges in paragraph 2.11 that the market is still evolving and that specific regulation will probably be necessary "given continuing customer concerns."

Ofgem places great emphasis on monitoring and examining the services companies provide to consumers, but there is a dearth of reference to taking enforcement action to protect consumers and using compliance as a means of promoting consumer confidence in the market. We welcome the commitment to create more targeted regulation where appropriate, but this must be linked with a clear sign to industry that both current and future regulation will be enforced effectively and automatic compensation payments made to consumers to encourage compliance where necessary.

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It would be useful for the document to have indicated more specifically how as a regulator it deploy the use of the following regulatory methods

- Fines
- Codes of practice
- Incentive regulation
- Licence changes
- Voluntary agreements

We believe there is a case for integrating these initiatives across directorates to form a compliance agenda.

PART 11

COMMENTS ON THE THEMES IDENTIFIED IN THE PLAN

Theme 1 Creating and Sustaining Competition

We are pleased that Ofgem have taken some of our concerns seriously enough to include them in this document. energywatch welcomes Ofgem's commitment to working bi-laterally "in dealing with customer concerns and providing tools for customers to learn about the benefits of switching" (2.13). However this must be take place within a wider commitment to improve consumer confidence in both the transfer process and the market as a whole. There is a certain amount of inconsistency between some of the aims put forward by Ofgem in relation to retail markets. There is no commitment to end debt blocking, merely to scrutinise supplier's application of their right to debt block. Ofgem however states a commitment to ensure that all vulnerable consumers have access to the benefits of competition. Working on the assumption that the more vulnerable in society make up the greatest proportion of those in debt, it may prove difficult for Ofgem and energywatch to encourage switching in that group without an outright ban on debt blocking.

We think there is scope for a bench-marking exercise comparing the degree of competition in a different liberalised energy markets when considering enforcement action.

Theme 2 Regulating Network Monopolies

We welcome Ofgem's proposal to introduce a new quality of service scheme for implementation in April 2005. We believe there is good opportunity to contribute to the debate on quality of service by using (for example) energywatch's complaints database as a means of illustrating the problems consumers have with the networks. Our work in this area with Ofgem is likely to increase over time and we are planning to discuss with them in some detail reports that we are producing on what consumers want from the Distribution

Price Control and the sale of LDZs. However, Ofgem do need to be aware of the difference in resources available to both organisations and their expectation regarding our involvement needs to be managed.

Theme 3 Helping Protect Security of Britain's Energy Supplies

Many respondents to the first phase of Ofgem's consultation on their work priorities expressed the view that competition alone cannot deliver security of supply. Ofgem's commitment to undertake RIAs is welcomed in this context. We are keen to understand how Ofgem will balance the risk of a little inefficient investment or regulatory intervention with the risk of late delivery of investment that jeopardises supply security.

Theme 4 A Leading Voice in Europe

As the European Union will become an important part of energy regulation (on wholesale prices) we welcome the statement that Ofgem's "objective remains to assist in developing genuinely competitive European electricity and gas markets as quickly as is feasible..." (5.1). There is some scope for energywatch to work with Ofgem to shape the EU's energy agenda. We would be interested in defining precisely how, when and with what outcomes.

It would have been instructive to consider the extent to which the British model of liberalisation will be adopted by other European member states with very different traditions of the role of the state in the market. There are also issues such as the relationship between European oil and gas prices that have an important impact on the UK's wholesale gas prices.

Theme 5 Helping Protect the Environment

With our commitment to the provision of pricing information we think there is opportunity for Energywatch to work with Ofgem (if not lead) in the area of guidelines for green tariffs and appliance information.

Theme 6 Helping Tackle Fuel Poverty

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Energywatch welcomes the inclusion of this theme and the recognition of Ofgem's key role in helping tackle fuel poverty. The likelihood of increasing energy prices over the coming years could well lead to a reversal of recent progress in reducing the numbers in fuel poverty, and a substantially enhanced effort will be required by all organisations involved in this area of work. We believe that there is a need to disaggregate the overall numbers of those in fuel poverty, and to consider policy measures appropriate to each group of fuel poor customers.

Ofgem's main area of work to help reduce electricity and gas disconnections has been based around the debt prevention guidelines and we have already been working together closely to monitor suppliers' performance to try and effect change in companies' behaviours. We would like to further understand how Ofgem are going to ensure that suppliers are fully committed to their social obligations. In this regard there are a number of issues that we could usefully co operate with, for example-

- Joint working to better target vulnerable consumers with the benefits of switching supplier
- Pressing companies for improved tariff innovation (and in particular social products for vulnerable consumers)
- More policy development on debt and disconnection with enforcement action from Ofgem where companies are non compliant
- Work together to promote the Priority Services Register and increase take up and ensuring that the energy companies to improve their PSR performance.

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WORKING WITH OFGEM ON THE COMPLIANCE THEME

Working with Ofgem

Ofgem refer to working with energywatch in a number of ways, such as on debt prevention and management and encouraging consumers to switch, especially the vulnerable. energywatch is already working with Ofgem over a number of issues and would like to see our joint operations extended: examples have been given in Part II above. There is a great deal of common ground between the themes identified in this Corporate Plan and those which form the basis of energywatch's draft Forward Work Programme for 2004/05.

In order to assist Ofgem in its compliance work, energywatch is committed to providing, in a useable form, data and intelligence about potential licence breaches and evidence leading to a super complaint for example. We look to Ofgem to act on this information wherever appropriate and in a timely manner. We would like Ofgem to take the opportunity to signal to the industry that Ofgem will work with energywatch to develop more effective processes of turning complaints data and other consumer feedback into formal company or market investigations in line with their compliance and enforcement policy.

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