

Domestic Competitive Market Review 2004 – Review Document

We welcome Ofgem's overall conclusion that the gas and electricity supply markets are competitive with evidence of continued market entry, a range of competitive prices and significant customer switching activity. However, we have a number of concerns about the detailed analysis and have outlined these below.

Regulation of the Competitive Market

In particular, we are concerned that while Ofgem conclude that competition is established there is no overall plan to withdraw from direct regulation of the market. Indeed, in one or two areas we are concerned that regulation may actually be increasing, for example in relation to direct selling, the transfer process and consumption information. We comment on each of these in detail below but, more generally, we would urge Ofgem to develop a robust plan for the complete withdrawal of sector specific regulation of energy supply. As a first step in that process, we would encourage Ofgem to undertake a thorough review of the existing licence conditions with a view to removing those areas of the licence that are no longer necessary. We note that such a review was promised in Ofgem's corporate plan a number of years ago.

D) Direct Selling

Throughout the paper Ofgem recognise that direct selling is an important way of attracting new customers. Indeed, table 2.30 in the paper illustrates the continuing importance of doorstep sales as the main channel for contacting customers. Without this form of attracting new customers suppliers would rely mainly on telephone contact. Information provided on the doorstep is often the main way in which customers can make comparisons of prices which in many cases is of utmost importance when making the decision to switch supplier.

Against this background, we support the aim of constantly striving to minimise direct selling (or indeed any) complaints. However, we are concerned that Ofgem's view of compliance with SLC 48 increasingly appears to require a supplier to achieve zero direct selling complaints from customers. As presently drafted, SLC 48 does not provide for the regulation of each and every sale/complaint and it would be unreasonable to attempt to enforce it in this way.

As long as suppliers undertake cold doorstep sales, it will be impossible to completely eradicate mis-selling in the energy market. There will always be a few rogue salesmen who are willing to break rules in order to make a sale. Similarly, there will always be potential customers who may feel genuinely confused or uncertain after receiving a doorstep visit, no matter how clear or truthful the salesman has been.

If this is not recognised in Ofgem's approach to SLC 48, there is a risk that regulation will effectively result in a de facto ban on doorstep selling (with the consequent knock on effect on competition). Indeed, Ofgem note in the paper that there has recently been a fall in the number of customers who have been contacted by a doorstep sales

agent. This highlights the risk of excessive regulation phasing out doorstep sales. As a consequence, we do not see any justification for reforming the current marketing licence condition.

ii) Customer Transfer Process

We note Ofgem's commitment to review the customer transfer process. In our view, there are four issues in considering possible improvements to the transfer process: direct selling; erroneous transfers; data/communication flows; and customers' expectations. We have already commented on direct selling, but discuss the other issues below.

Erroneous transfers can significantly affect a customer's experience of the transfer process. In our view, where an erroneous transfer occurs the key issue is how quickly and efficiently the erroneous transfer is dealt with. We believe that the present customer charter and supporting processes provide a robust framework for dealing with erroneous transfers as they arise.

In addition to the above, one possible way of reducing erroneous transfers could be through enabling the withdrawal of registrations in electricity. This is currently available in gas where a customer initially agrees to change supplier but subsequently changes their mind. Allowing suppliers to stop or withdraw a registration could therefore reduce the numbers of associated complaints.

In relation to data/communication flows, we believe that there is considerable scope for suppliers to improve their current performance in managing data and communication flows within the existing transfer process to deliver tangible improvements to customers in a relatively short period of time.

For example, systematic failure to issue timely and accurate bills on change of supplier is, in our view, often due to individual suppliers' systems and not, as some have claimed, industry processes. This is supported by our level of Energywatch account and billing complaints (0.016) compared to the industry average (0.082). Indeed, if all suppliers improved to our standard of performance this would secure an immediate reduction in Energywatch transfer-related complaints of more than 80% within the industry as a whole. Moreover, this could clearly be achieved with no change to the existing processes and systems, since we would be asking rival suppliers to do no more than match our current level of performance.

That said, there are some changes to the industry processes that would help all suppliers to further improve. In particular, a change to the Network Code that has been agreed will bring gas in line with electricity allowing the old gas suppliers identity to be released to the new supplier when a customer changes supplier. We believe that this will further improve data and communication flows.

When a customer decides to switch supplier they have certain expectations. They not only expect the transfer process to go smoothly, but during the transfer they expect suppliers to take responsibility for any problems that might arise. They do not expect to be misled by suppliers. Customers do not expect to be transferred unless

they agree to a transfer taking place. If they are transferred without having given consent they expect to be returned to their supplier quickly and smoothly. They also expect their first/final bills to be accurate and sent to them on time.

We believe that these minimum standards could be set out in a “Customer Transfer Charter”, along with detailed undertakings on each stage of the transfer process, that all suppliers could publicly sign up to. Suppliers’ performance could be measured and published under the Customer Transfer Charter. This would highlight those suppliers who were not meeting agreed standards and would ultimately be an incentive on them to improve their performance.

To conclude, there is much that can be achieved to improve customers’ experiences of the transfer process by improving individual suppliers’ internal processes and with a few modest changes to the existing processes. Wholesale change of the transfer process is not therefore justified by the findings of Ofgem's Competitive Market Review or on cost grounds.

(iii) Information provided to customers

Ofgem has stated that it will continue to monitor pricing information to customers and will also publish proposals on improving the information available to customers to aid them in deciding whether or not to switch supplier. As part of that, Ofgem also suggest including additional consumption information on customers’ bills.

Ofgem suggest in the paper that customers have difficulty in getting independent price information about all the available offers. However, Energywatch and Uswitch are well known for providing customers with pricing information as well as other information about the industry and customers’ rights. We do not therefore believe that there is any need to take action on pricing information. Indeed, according to Ofgem’s analysis a majority of customers find it very easy or fairly easy to compare prices. For example table 2.13 shows that overall that majority of customers found it fairly easy to compare prices between suppliers.

There are already requirements in place to provide a wide range of information on customers’ bills. This includes pricing information, useful numbers and addresses as well as additional information for customer service information, how to contact the supplier for queries by post or telephone, details of how and where to pay bills, and also encouragement to contact the supplier if there are any problems in paying the bill. There are also additional regulations to include further information to be provided on or with bills, in particular the EU’s requirements with respect of energy labelling.

As a consequence, we do not believe that Ofgem have provided sufficient evidence that there is a material problem for customers in comparing prices or understanding their consumption to the extent that further regulatory intervention is justified.

This point notwithstanding, if Ofgem are to intervene in the provision of pricing and consumption information, we firmly believe that there should be consideration of the

benefits of such increased regulation, ensuring those benefits outweigh the costs and will deliver a marked (and sustained) reduction in consumption.

Considering this we are concerned that additional information would over-complicate the appearance of bills and put the customer off reading them. There is only so much useful information that can be included on a bill made clear and simple.

Review of Competition in Scotland

We firmly believe that competition is equally developed in Scotland compared to the rest of Great Britain.

As stated in Ofgem's paper, the awareness by demographic breakdowns in gas show that there are similar levels of customer awareness between North and South of Scotland as well as between Scotland and England (e.g. table 2.4). Furthermore, it is clear that customers in Scotland have at least the same number and level of discounts available to them from rival suppliers and this applies to all payment methods. It is true that there has been a slightly lower cumulative level of customers switching in Hydro's region leading to a slower loss of market share compared to other areas, but this does not indicate a lack of competition or barriers to entry and certainly does not justify concluding that competition in Scotland is less effective than in England and Wales.

The introduction of BETTA in Scotland will introduce the same trading conditions across Great Britain. This will mean that all suppliers and generators will be subject to the same wholesale and balancing arrangements, wherever they supply customers.

There is therefore no evidence of less competition in North of Scotland or of any problems faced by customers in taking advantage of their ability to choose supplier.

Barriers to Entry

Ofgem's paper discusses potential barriers to entry into the supply market. In our view, one of the key barriers to entry is the increasing pace of regulatory change. We believe that the uncertainty created by this ongoing large scale regulatory reform must be a significant barrier to entry in the UK energy market.

The way to reduce barriers to entry would be to stabilise the market by minimising the rate of change. In particular, we continue to believe that the volume of regulatory reform is unsustainable. For example, at the current rate, Ofgem appear to be on course to publish around 300 consultation or substantive policy papers this year, most of these include significant industry change with material implications for market participants' profitability. This contrasts with around 50-60 policy papers that Offer/Ofgas were producing a year in 1997/1998.

The broader background of Ofgem's work plan suggests to us that there is not a single area of the energy supply chain that is not currently subject to some form of review and change. For example:

- In supply, there is the ongoing customer transfer programme, together with a considerable programme of ex-ante supply compliance work by Ofgem;
- Associated with Metering, there is much work ongoing in relation to competition;
- In Distribution, there is the ongoing review of charge structure in electricity and now the recently initiate review of the charge structure on gas;
- BETTA and RETS are major projects in electricity transmission, while in gas a review of exit capacity has recently been initiated with a little justification; and
- On the Generation and Production side of the energy industry, BETTA is a force for change in electricity, gas is now subject to a review of top-up, and cash out mechanisms in gas and electricity are now also under review.

We believe that a regulatory strategy that would seek to minimise the scope of change that is introduced at any one time would be more commendable. Such an approach would bring together stability to the energy industry and its customers, even out the regulatory workload generated for industry and has the potential to reduce the level of resources that Ofgem itself requires. We also believe that a reduction in the amount of regulatory reforms being brought forward would make it easier for potential new entrants to compete in the supply market. Indeed Ofgem note that new entrants have highlighted the fact that some of the regulatory requirements are “unnecessary burdens on them”. In our view, this highlights the need for review and removal of unnecessary obligations.

Conclusion

We believe that competition is successful and we do not therefore believe that there should be any further regulatory intervention. Indeed, we would urge Ofgem to develop a robust plan for the complete withdrawal from regulation of the energy supply market. We have commented above on some of the specific areas that appear to be subject to increasing regulation. In short:

- We believe that doorstep sales agents remain suppliers main way of attracting new customers and we believe that further regulation in this area would possibly result in suppliers discontinuing to provide doorstep agents. As noted above, a number of suppliers have already scaled down the numbers of doorstep agents and are concentrating mainly on telesales;
- In relation to the transfer process there is much that can be achieved to improve customer experiences of the transfer process through improving existing internal processes and with some relatively minor changes to industry process at minimal cost. We certainly would not support wholesale change to include IT systems, which would result in significant cost; and
- There are already requirements in place to provide a wide range of information on customers’ bills, and we are concerned that additional information would over-complicate the appearance of bills and put the customer off reading them.

We strongly believe that competition in the North of Scotland is equally as competitive as the South of Scotland and England and Wales. In particular, there is no evidence that there is less competition or information available to customers in the North of Scotland. It is customer choice whether or not they want to change supplier.

Finally, we believe that one of the key barriers to entry is the ongoing substantial rate of change to regulatory rules. We believe that the way to reduce barriers to entry is to stabilise the market by minimising the rate of change.