

Deemed Contracts – Ofgem Discussion Document, 9 February 2006.

This document provides an overview of the key areas to be tackled in the Duty to Supply, Contracts and Information workgroup on deemed contract issues. Please note that this paper is for discussion purposes only and does not seek to represent the view of the Authority. The specific SLCs being considered are:

SLC 28 - Deemed Contracts
SLC 42(4) – Domestic Supply Contracts.

Background to deemed contracts

Schedule 2B paragraph 8(1) of the Gas Act and Schedule 6 paragraph 3(1) of the Electricity Act, respectively, provide that where a supplier supplies gas or electricity to premises or a consumer otherwise than in pursuance of a contract, the supplier shall be deemed to have contracted with the consumer for the supply of gas or electricity from the time when he began to supply that gas or electricity. Typically a deemed contract will occur where a customer moves into a new property and has not agreed contractual terms with a supplier who is supplying energy to that property or where a fixed term contract expires and there are no explicit provisions for terms and conditions for the period immediately after expiry¹.

Ofgem considers that deemed contracts play a vital role in the energy market. The nature of supply is such that it would be inefficient, given current metering technology, to disconnect a premise when a customer had moved out and reconnect the premise upon application for a contract by a new occupant. In addition, suppliers may not always be aware of customer movements until a period of time has elapsed after the event. A deemed contract therefore seeks to provide a sound and binding basis upon which suppliers will supply customers where a contract has not been expressly agreed. It also provides suppliers with a clear basis upon which to charge for that supply.

As by definition the terms and conditions of a deemed contract have not been expressly agreed between suppliers and customers, Ofgem considers that it is appropriate for these terms and conditions to be subject to regulation. In particular Ofgem considers that the charges levied under deemed contracts should not be unduly onerous and that customers being supplied under deemed contracts should be free to access the competitive market and transfer to the supplier of their choice. On this last point, domestic gas customers on deemed contracts can still be objected to on grounds of debt where this meets the criteria set out under SLC 46 or Section 16 of the MRA. In the non-domestic market customers on deemed contracts can not be objected to for debt or on grounds specified in the contract.

Finally, there is a strong link with the operation of the Supplier of Last Resort (SoLR) Arrangements and deemed contracts. Where a SoLR is appointed then they will supply

¹ Note that in this last example, where a fixed term contract expires and the contract makes provisions for "out of contract" rates then this is arguably not a deemed contract but is the continuation of a contract that the customer has entered into at the start of the fixed term period. In determining the answer to whether the customer is being supplied under an expressly entered into contract or a deemed contract the precise working of the contract would need to be examined.

those customers affected on deemed contract terms. The SoLR arrangements are being reviewed separately by the Section B issues (inc. SoLR) workgroup.

Background to the licence conditions

SLC28(2) and SLC28(3) restrict the level of charges that suppliers can levy under deemed contracts. They provide that such charges should not be “unduly onerous”. Terms shall be taken to be “unduly onerous” if the revenue derived from supplying gas or electricity to customers on those terms:

- (a) significantly exceeds the costs of supplying gas or electricity; and
- (b) exceeds such costs of supply by significantly more than the supplier’s revenue exceeds costs of supply in the case of the generality of its domestic customers or non-domestic customers, as appropriate (except where customers are supplied in accordance with SLC 29 (Supplier of Last Resort)).

Competition is unlikely to deliver value for customers in this area and Ofgem considers that it would therefore be prudent to retain such obligations. However, it is for discussion whether the definition of costs of supply under SLC 28(4) should exclude costs associated with the promotional, marketing and advertising activities of the licensee.

SLC28(5) requires a supplier to send a copy of their deemed contracts and revisions to such contracts to the Authority. Ofgem considers that this requirement could safely be removed as the provision of information on deemed contracts to the Authority, energywatch and customers would be safeguarded by the retention of the obligation under SLC28(6) to supply a copy of their deemed contracts to any person that asked. Given the uncompetitive nature of deemed contracts, transparency and access to terms and conditions is considered to be important. SLC28(6) could be interpreted as requiring suppliers to only provide a customer with their deemed contract terms. Ofgem considers that the obligation would benefit from redrafting to clarify that deemed contract terms should be available to any person that makes a request.

SLC28(7) sets out a requirement for the licensee to ensure that their deemed contracts include provisions required under SLC29 (Supplier of Last Resort) when in relation to deemed contract supply under a last resort direction. This appears to be a duplication of suppliers’ obligations and could therefore be removed. However, Ofgem would be interested to hear whether suppliers find clarification of this type helpful in determining their requirements

SLC28(8) provides that where a supplier supplies a customer with gas or electricity under a deemed contract, it shall use its reasonable endeavours to provide the customer with the details of the deemed contract and information about other domestic supply contracts that may be available to them. As the customer does not expressly enter into a deemed contract, Ofgem considers it appropriate for the supplier to make reasonable endeavours to provide customers with details of the principal terms of the deemed contract (SLC28(8)(a)) NB: there is no comment on timescales within the licence. In recognition that deemed contracts are unlikely to offer terms to customers that are better than those that could be achieved under domestic supply contracts then Ofgem also considers that it would be appropriate to inform customers of the availability of domestic supply contracts and how they may enter into such arrangements (SLC28(8)(b)). It is for discussion whether the provision of such information needs to be made in writing and whether the

supplier should be required to provide details of the terms of contracts available to domestic customers (SLC28(8)(c)). Ofgem considers that this last obligation may need to be redrafted or removed. The obligation could be interpreted as requiring supplier to provide a summary of all contracts including those offered by competitors. It would seem to be more reasonable to require a supplier to provide information on their contracts only. Ofgem further considers that there would be strong commercial reasons for suppliers to do this anyway and the requirement could be removed from the licence.

SLC28(9) sets a number of obligations for suppliers to include set terms within their deemed contracts. These obligations reflect requirements stated elsewhere on suppliers with respect to their express contracts and deal with;

- security and emergency arrangements (gas only),
- contracts to be terminable on appointment of a SoLR,
- security deposits,
- termination where a customer ceases to own or occupy a premise, and
- deemed contracts to be terminable at the point where a supply is taken under contract from the incumbent or new supplier

Ofgem considers that it is sensible for deemed contracts to include all of the terms currently required. This provides clarity for customers. However, it is for discussion whether suppliers find it helpful for these obligations to be clearly set out in SLC28 or whether the relevant requirements for express contracts elsewhere in the licence could simply be modified to make them a requirement on “contracts (including deemed contracts)”.

SLC28(10) of the electricity licence makes reference to SLC29(17) which is not present in SLC29 and SLC28(10) of the gas licence makes reference to SLC29(16) which appears to be wrong. In both instances the reference should be to SLC 29(15) which sets out the circumstances under which a deemed contract enacted under a last resort supply direction shall terminate. SLC28(10) allows suppliers to include additional termination provisions that do not derogate from those required in the rest of the SLC28. It is for discussion whether this provision adds clarity to suppliers’ allowable actions or is superfluous to requirements.

SLC28(11) places a requirement on the supplier to act in a reasonable manner including the use of any available consumption data for the premises and other relevant factors when determining the kWh of gas or electricity taken. Ofgem considers that in many instances an accurate actual start read for the deemed contract may not be available. It would therefore appear sensible to retain an obligation on the supplier to act reasonably in this instance. This test of reasonableness is additional to the rights of suppliers provided by the Acts to estimate consumption (Schedule 2B paragraph 8(9) of the Gas Act and Schedule 6 paragraph 3(8) of the Electricity Act).

SLC28(12) provides clarity that where a deemed contract is in place as a result of a last resort supply direction, requirements on the level of tariffs and provision of information on standard contract terms to customers in SLC28 are not applicable. SLC29 sets its own restrictions on tariff levels. It is unclear why customers on a deemed contract as a result

of a last resort direction should not be informed by the supplier of last resort of the availability of standard contract terms?

Finally, SLC42(4)(c) of the gas supply licence and SLC42(4)(b) of the electricity supply licence places a requirement on the supplier to ensure that their domestic contracts include terms that correspond as near as may be to the requirements on deemed contracts set out under Schedule 2B paragraph 8 of the Gas Act and Schedule 6 paragraph 3 of the Electricity Act. It is therefore permitted under Schedule 2B paragraph 8(9) of the Gas Act and Schedule 6 paragraph 3(8) of the Electricity Act, for suppliers to include terms and conditions for estimating consumption from the start of the contract until either a meter read is taken or the supplier ceases to supply the premises. Current industry practices provide for opening and closing meter reads on change of supplier but this may be a requirement in some instances, for example when a customer moves from a deemed contract to a domestic supply contract. It is therefore suggested that this provision remain.