

Metering price control review

response to Ofgem consultation 108/06 by the National Consumer Council

About the National Consumer Council

The National Consumer Council (NCC) makes a practical difference to the lives of consumers around the UK.

With changes in provision of services by government and companies, there is apparently more choice, and more talk about meeting consumers' needs. Yet, the rhetoric does not always match people's experience: markets can operate in ways that act against consumer interests; and consumers who are disadvantaged or inarticulate can be ignored.

The NCC uses its insight into consumer needs to advocate change. We conduct rigorous research and policy analysis to investigate key consumer issues, and use this to influence organisations and people that make change happen. We don't just respond to policy discussions, but shape future debate through our groundbreaking thinking.

An open and collaborative organisation, we seek to work with public service providers, businesses and regulators. We hold regular policy forums which provide us with a unique opportunity to exchange views and test our thinking.

Our relationship with the Department of Trade and Industry – our main funder – gives us a strong connection within government. But we are ready to challenge any organisation, public or private, that does not give consumers a fair deal.

We have linked organisations in Scotland and Wales, and a close relationship with colleagues in Northern Ireland. We play a leading role within European and worldwide consumer groups, ensuring that cross-border consumer issues are tackled and the consumer voice is heard within global institutions.

Please check our website at www.ncc.org.uk for our latest news.

We can often make our publications available in braille or large print, on audio tape or computer disk. Please contact us for details.

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1. Introduction

The National Consumer Council (NCC) uses its insight into consumer needs to advocate change, working with public service providers, businesses, regulators and Government. NCC conducts rigorous research and policy analysis to investigate key consumer issues, and uses the results to influence organisations and people that make change happen. NCC receives the bulk of its funding through the DTI.

NCC is committed to the principal of universal access for essential goods and services, including gas and electricity. This is defined as 'availability and continuous accessibility and affordability of goods and services at a specified minimum quality for all consumers'.

In particular, NCC has a remit to promote the interests of disadvantaged consumers. These are people who - for example, because of low income, living in a deprived area, or a disability - are excluded from adequate provision of everyday essential goods and services or are obliged to pay more for them than better-off consumers. One of the aims of the Government's energy policy is to ensure that every home is adequately and affordably heated. Ofgem has a specific duty to protect the particular interests of low-income consumers. It is well accepted that households with pre-payment meters are almost exclusively on low incomes (other than where they are second homes). NCC therefore welcomes the opportunity to comment on Ofgem's Metering Price Control Review consultation (108/06), particularly those aspects of it that relate to pre-payment meters (PPMs).

It is NCC's view that a competitive market can sometimes work against the interests of consumers, particularly disadvantaged (including low income) or otherwise vulnerable consumers. Put another way, the benefits of a competitive market are not always evenly distributed across all groups of consumers. In such cases of 'market-based exclusion' for some groups of consumers, NCC believes that interventions in the market can be justified, even at the expense of some economic growth.

In view of this, NCC cautions Ofgem against taking decisions, particularly on prepayment meters, that could result in higher charges being passed through to low-income consumers on the basis of uncertain outcomes. This is particularly important at a time of rising prices, before taking any decisions that could result in higher relative gas or electricity prices for them. Where there is any doubt as to what the outcome of its decisions will be, NCC urges Ofgem to err on the side of caution.

2. Pre-payment meters

Prepayment meters allow small and controllable cash payments to be made for energy, making them popular with low-income consumers. There are around 5.9 million PPMs in use in Great Britain. This represents around 13% of domestic meters. Of these, 2.1 million are gas PPMs, accounting for 10% of domestic gas consumers, and 3.8 million electricity PPMs, accounting for 15% of domestic electricity consumers. Around 1.2 million households, or 5 per cent of all domestic consumers, are currently paying an energy debt through a PPM and this is likely to rise after the 2005/6 winter price rises.

PPMs are the most expensive payment method, with consumers on prepayment and standard credit tariffs paying a little under 10 per cent more for their energy than those on direct debit. If this gap could be removed energy bills for many low-income consumers would be cut by £60 a year¹, or perhaps more. The difference in price between the cheapest direct debit gas tariff on offer and the most expensive prepayment meter gas tariff on offer currently equates to some £150 per year². (Two suppliers provide PPMs at no additional premium over standard credit, a policy NCC would like to see emulated by the others.)

NCC considers that Ofgem should take into account the broader implications of these figures for low-income households when deciding on its policy on price controls for metering. The analysis that underpins the decisions that it takes needs to recognise that different socio-economic groups of consumers can benefit in different ways from

¹ Fuel Poverty Advisory Group (for England), Fourth Annual Report, 2005, published in March 2006.

² energywatch, March 2006, for an average household consumption.

competition, just as different geographical groups of consumers do.

In weighing up the costs and benefits associated with the various policy options set out in the consultation document, NCC considers that Ofgem should weight any additional costs for households in the lower income deciles more heavily than those in the higher income deciles. This will take account of the proportion of total disposable income that any additional costs account for. It would be helpful if these costs and benefits could be set out clearly in a Regulatory Impact Assessment, along with the assumptions that underpin them.

NCC further considers that Ofgem's aim, in taking decisions that influence the way the costs of prepayment meters are passed on down the supply chain, should be to ensure that low-income consumers do not pay more for their gas and electricity than other groups of consumers.

3. Gas pre-payment meters

NCC supports Ofgem's proposal not to review the cap on prepayment meters until it undertakes a full-scale review of the treatment of gas prepayment meters in the price control. This is likely to be after the conclusion of the Competition Act investigation into National Grid's gas metering arrangements.

As part of a future review, NCC would welcome a fuller understanding of the market in gas PPMs, including the true costs of the meters, and the profit margins of the manufacturers and meter operators. The development of the market to date does not appear to support the contention that allowing a higher differential charge, or removing the differential cap altogether, would necessarily result in lower charges for households with gas PPMs in the longer term.

NCC would want to see much more targeted incentives to ensure that such a move did not simply end up in higher prices without any attendant benefits. This is especially important for PPM consumers, many of whom are not in a position to change their payment method or supplier.

4. Electricity pre-payment meters

NCC finds Ofgem's review of the electricity metering market very optimistic. It is not at all clear that competition in electricity meters will develop in the way that is predicted in the review. For example, when British Gas negotiated contracts with competitor providers for its metering services, these contracts did not require any improved functionality for the meters. Indeed, it appears that the specified meter functionality actually reduced.

Consumers are unlikely to understand or be interested in the complexities of who provides their meter for them. (Most consumers do not appreciate the difference between distribution and supply and are confused by the different companies that they deal with.) What is important for consumers therefore is the outcome achieved.

The introduction of competition into metering has not resulted in improved technology of pre-payment meters to date, despite the fact that advanced, secure pre-payment meters are available on the market, offering benefits to all parties. Such meters do not permit self-disconnection, at least for minimal cooking and lighting purposes, and offer improved ways of buying prepay credit and more flexible emergency credit arrangements.

To achieve real service improvements for low-income households, NCC proposes that Ofgem should set minimum standards for the functionality of PPMs, allowing DNOs to recover costs only at a level that reflected the economies of scale that would be achieved by accelerated replacement.. This will ensure that more advanced, reliable technology can be introduced and the existing 1.5 electricity token meters are replaced as a matter of urgency. (Token meters have greater susceptibility to fraud and mis-directed payments, and have high maintenance costs due to the need for site-visits to set tariffs and obtain meter readings.)

Higher asset costs should be offset by lower operational costs, and so consumers need not face higher charges. As long as the minimum standards apply to all metering providers, then it should not prevent competition from developing. In this way, NCC believes that Ofgem can provide consumers, regardless of their income levels, with a more reliable, user-friendly, stigma-free means of controlling their budgeting.

For these reasons, NCC considers that Ofgem should adjust the metering price controls in 2007 for PPMs to provide the incentives outlined above, and then undertake a further review of market developments in the run-up to 2010 when the rental for incumbents' legacy meters will in any case be reviewed.