

Philip Davies
Director, Retail Markets
Ofgem
9 Millbank
London
SW1P 3GE
philip.davies@ofgem.gov.uk

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Your Ref: Ofgem doc 191/07

Dear Philip

Modifying the arrangements for the use of objections in the non-domestic market for gas and electricity supply - open letter

energywatch welcomes the opportunity to respond to the issues raised in the open letter. This response is non-confidential and we are happy for it to be published on the Ofgem website.

As you will be aware from previous correspondence between us on this subject, energywatch has significant reservations about how certain non-domestic consumers are treated in the marketplace when they contract for their energy supplies. This is particularly the case for those non-domestic consumers which are small businesses.

Energywatch's own data indicate that small business consumers have difficulty understanding how suppliers' commercial activities relate to industry processes for switching and contract renewal. energywatch has in the past referred evidence to Ofgem of mis-use of the objections process and difficulties experienced by small business consumers who find themselves under contract to two suppliers at the same time. We have also lobbied in support of fairer treatment for small businesses and greater transparency in relation to the MRA switching processes.

The intention to extend regulated complaints handling standards and access to redress schemes, proposed under the Consumers, Estate Agents and Redress Act 2007, highlights the potential for consumer detriment amongst this group regardless of the extent to which energy markets are considered to be open and competitive.

In respect of Ofgem's specific proposals in this letter, these arise out of recent events which culminated in a successful appeal to the Authority by British Gas Trading regarding its interpretation of the rules relating to the non-domestic objections process under the Master Registration Agreement. As we now understand it, Ofgem intends to amend the supply licences to prevent an old supplier from using the objections window to re-contract with a customer who seeks to move to another supplier and then objects under the terms of the new contract.

Whilst we understand the logic of this position, it seems to us that it fails to address

the fundamental issue contended under the recent appeal. In essence, the terms of *existing* contracts are not covered, including any changes to these made by the supplier by giving the appropriate prior notice, meaning that objections under these terms continue to be valid (note that the principal ground for objection in new Standard Licence Condition 14.2 is where the provisions of the contract between the customer and the *existing* supplier permit an objection). Suppliers can therefore write quite onerous terms into **existing** and subsequent contracts, making it increasingly difficult to move to a different supplier without first being subject to significant penalties or other legal obstacles. In any event, it is consumers who will find switching onerous and the longer this goes on, the more competition will be stifled, with quite severe implications for a competitive non-domestic energy market.

Even if consumers wish to switch (and not necessarily because they have been offered a better price by a different supplier – they may be prompted to switch to move away from poor service offered by their existing supplier), the difficulties of extricating themselves from their current contract terms in effect constitute barriers to leaving. Ofgem must recognise that the recent appeal ruling will have given all non-domestic suppliers a signal that more onerous contract terms in existing contracts are a more certain way of retaining customers. The effect of this is that it will reduce choice for consumers to contract on essentially fair and equitable terms for their energy supply.

Whilst Ofgem now accepts that the objections window was not intended to allow re-contract negotiations, we would argue that this interpretation could have been ruled out through the Authority's decision on the recent appeal. Instead, the ability to place any kind of commercial interpretation on a process under the MRA which is simply intended to more effectively transfer data between suppliers when consumers have *already* exercised a choice to switch, subject to any genuine grounds for objections from the old supplier, has created further cause for consumer detriment.

Rather than the consumer exercising caution (the 'buyer beware' approach that Ofgem believes all non-domestic consumers ought to exercise), even the most knowledgeable consumers may find that they have little option but to sign up with a supplier who offers the 'least worst' contract terms to them. Those less knowledgeable may become trapped in contracts which offer them very little room for manoeuvre if they wish to leave their current supplier. This is hardly tantamount to a genuine and empowered choice for the consumer.

As we have mentioned in previous responses there is a significant imbalance of power between large suppliers and very small business consumers – the vast majority of whom have only a small number of, or no, employees and no access to the kind of legal or other support enjoyed by suppliers. It is ludicrous that a sole trader or a self employed home-worker who is afforded protection as a domestic consumer suddenly loses the need for that protection when he steps out of one room in his house and into another. In other sectors, small business consumers do benefit from similar protections to those enjoyed by domestic consumers – e.g. in the fixed line telephone market – and energywatch believes that, in energy where there are clear areas of consumer detriment, energy regulation should follow suit.

In striving to make the transfer process simple and predictable, we believe that Ofgem has failed to recognise that the contracting process should be based on an appropriate balance between the rights and obligations of supplier and consumer. Consumers are entitled to some basic level of certainty and transparency in contracting with, and switching, suppliers. Ofgem has decided to focus only on regulating industry process in the form of the use of the objections window (something that few consumers have ever heard of and of which even fewer understand the implications). energywatch believes that this is inconsistent with Ofgem's remit to ensure value for all consumers wherever possible through effective markets. An effective market is not only influenced by industry processes but also, to a very great extent, by commercial practices. Suppliers have shown us in the past that they will meet regulatory requirements but then deal with any potential commercial disadvantage by amending contract terms or commercial practices.

We believe that Ofgem's proposals to amend Standard Licence Conditions are only a partial solution, fail to address the underlying causes of consumer detriment in the non-domestic energy markets, and tip the balance further in favour of suppliers, creating conditions in which they will tie up consumers contractually and deny them an opportunity to exercise real choice, undermining effective competition. Unreasonable contract terms are only likely to be tested in court. How many small business consumers have either the inclination or means to pursue remedies through this process?

We believe that Ofgem's approach creates conditions where existing contract terms could become increasingly onerous for consumers. In those circumstances, clarity of the grounds for genuine objection in the supply licences is neither a limit on the ability of consumers/suppliers to contract or on innovative contract terms. Suppliers are unlikely to adopt different commercial strategies in pursuit of retaining consumers through *new* contract terms. There is a real risk instead that they will seek to 'outdo' one another in finding more innovative ways to tie consumers to *existing* contracts in the belief that the objections window will protect their positions.

We also believe that there remains a genuine issue about the use by large suppliers, given their ability to bulk purchase energy, of overall economies of scale compared to small players and new entrants. If large players are able to offer competitive prices, why would they not do so when a consumer's contract comes up for renewal? Why wait to see what is on offer from another supplier, object on the grounds of terms in the existing contract, and then make a counter-bid which can be a 'loss leader' price recoverable in other ways, perhaps from other consumers? Ofgem must be willing to explore this issue more thoroughly and determine whether there are effective barriers to competition as a result.

Going forward, we will continue to keep these issues under review as and when they are raised, always considering the possible impact on consumers.

We would appreciate being kept informed of the progress of the consultation and any related issues to enable us to comment as the need arises.

If you do wish to discuss our response further please do not hesitate to contact me

on 0191 2212072.

Yours sincerely

Carole Pitkeathley
Head of Regulatory Affairs