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Dear Andy

Ofgem's Proposed Corporate Strategy and Plan 2008-2013: consultation

energywatch welcomes the opportunity to address the issues raised in Ofgem's further consultation. This response is non-confidential and we are happy for it to be published on the Ofgem website.

In our response to Ofgem's original open letter last August, we highlighted our general frustration that retail energy prices had fallen only modestly compared to the drop in wholesale prices. Ofgem's explanation indicated that there was a time lag in the feed through effects of wholesale price falls into retail prices. Widespread public scepticism remains, however, which energywatch shares. We do not believe that Ofgem adequately addressed these concerns at the time when the trend was for downward pressure on prices.

Over the last year, wholesale prices have risen. Recent events indicate that suppliers are more than ready to pass on price rises to consumers, with immediate effect, at a time which happens to coincide with the period of highest usage for most, if not all, consumers. The recent announcement by the BERR Select Committee that it intends to examine these issues in more detail indicates just how widespread these concerns are. Ofgem should engage constructively and openly with the committee to establish whether the structure of the energy market as it has evolved over recent years has diminished the benefits of effective competition to consumers.

Ofgem has asked a number of questions about its future strategy and corporate plan in this consultation. We address these issues below.

The validity of Ofgem's seven themes

Reading through the current document, it is apparent that there is a large degree of crossover of certain issues across the various themes. For example, smart metering is mentioned under the themes of creating and sustaining competition, helping to achieve sustainable development and helping to tackle fuel poverty. It appears, therefore, that there are certain priority issues which require Ofgem's engagement in the short to medium term and that these issues sit above the fundamental duties

of the regulator such as reviewing and setting price controls for networks for instance.

The key driver for prioritising and addressing these issues (which we highlight below) must be the protection of consumers' interests, now and in the future, through the facilitation of competition where that is possible or desirable. Consumers' interests, or perhaps more pertinently their expectations of energy providers, suppliers and the regulator, are that they deliver safe, secure and reliable energy supplies in an efficient and economic manner.

Open and competitive energy markets for all consumers

One priority area for Ofgem must be to address the lack of open, effective competitive markets here and in Europe. We support Ofgem's efforts to develop and work for more liberal energy markets in Europe so long as these markets remain illiberal.

We note Ofgem's views regarding the factors that drive GB energy prices, particularly the lack of liberalisation in the EU and the impact on gas supplies of a global LNG market. However, Ofgem is aware of energywatch views regarding the constraint on effective competition caused by the current market structure. The lack of any significant new entry should cause concern as to whether market structures create disincentives for new and emerging players.

We hope that the BERR Select Committee investigation will help Ofgem to focus on a number of issues of concern to consumers including:

- the effectiveness of Ofgem's market monitoring;
- whether 'product innovation' creates real consumer choice or simply masks a failure to price the basic product economically and transparently for all consumers, and the specific impact of this on vulnerable and fuel poor consumers;
- how much reliance can be placed on statistics on switching activity.

Although there is a great deal of focus, rightly, on domestic energy consumers, the small business consumer is also subject to many of the same pressures without the same level of protection when purchasing their energy supplies. The failure to mention small business consumers in the consultation is a significant omission. Ofgem should remain mindful of the real concerns we raised in our previous response about the impact of recent changes on re-contracting activity using the MRA. Ofgem should monitor what effect these changes are having on competition in the small business market; energywatch believes that there is only a limited degree of innovation in this market sector. The introduction of complaint handling and redress schemes to assist small business consumers to tackle detriment must be followed through effectively by Ofgem.

Addressing the problems experienced by vulnerable consumers

In a number of ways, vulnerable consumers have particular problems that need to be addressed by Ofgem as a matter of priority. Action to tackle fuel poverty and action on PPMs are two specific examples.

We believe that social tariffs that conform to some strong minimum standards would be a far more effective tool in tackling fuel poverty than the current voluntary approach. Price increases have been single-handedly responsible for undermining the progress that was being made towards meeting fuel poverty targets. Escalating prices have outstripped income growth and outpaced the rate at which energy efficiency and heating improvements can be installed. The net effect has been an increase in fuel poverty, with the 2007 Energy White Paper observing that UK fuel poverty was back at the 4 million household mark – double the 2004 figure and a return to pre-Strategy levels. The part of the government's 2001 UK Fuel Poverty Strategy which referred to maintaining downward pressure on energy prices has simply collapsed.

As those suppliers who have led the way in offering voluntary initiatives have indicated, unless there are common standards that create a level playing field, they will review their activities. Ofgem's continued opposition to a common set of standards for social tariffs on the grounds that it would stifle innovation, can only prevent a levelling up of social tariff provision. We believe that this is an area where Ofgem's duty to protect the most vulnerable consumers overrides the desire of suppliers to develop solutions independently.

Debt blocking as a means of impeding switching by vulnerable consumers must be addressed through greater regulatory action. Examining why vulnerable or fuel poor consumers do not switch supplier must not be restricted only to looking at debt blocking. Debt blocking must be addressed as part of a comprehensive strategy for dealing with fuel poverty. Ofgem should ensure that fuel poor consumers have confidence in, and are not prevented from accessing the benefits of a competitive market based on their level of debt with a current supplier. Ofgem must recognise the disparity of bargaining power between consumer and supplier when such a situation occurs.

PPM consumers tend to be amongst the most vulnerable of consumers. The issues they face are well documented. These are:

- high (increasing) PPM differentials;
- lack of access to cheaper online or direct debit tariffs;
- low awareness of PPM premium coupled with the lack of ability to compare tariffs;
- almost non-existent switching rate from PPM to PPM or from PPM to other tariff;
- lack of take up of relaxation of debt blocking on debt under £100;
- increased susceptibility to self disconnection;
- increasing debt.

As long as there continues to be outstanding problems around the ability of these consumers to switch supplier with the same ease as other consumers, thus preventing them from enjoying the same benefits of competition as others, then

Ofgem must act. Ofgem must also explore why significant price differentials remain between PPM tariff consumers and others. As part of the customer journey work that it is leading to the transition to the new organisation, Ofgem must address the difficulties PPM consumers face in obtaining price comparison information. This is especially important as many of these consumers use price comparison leaflets as an aid to understanding suppliers' offerings and these may not be available under new consumer representation arrangements.

Recent attempts to modify the MRA to use data flow information to alert sales teams to the existence of token PPM meter households which could then be filtered out of walk routes highlights the vulnerability of this group of consumers and the failure of suppliers to deliver fair policies despite the competitive market. Ofgem should consider carefully, the ability and genuine willingness of suppliers to voluntarily address such issues.

Generally, we remain concerned that Ofgem places an undue emphasis on supplier-led solutions to vulnerable consumers' problems. While suppliers can go some way towards addressing these problems, they cannot provide an effective approach in every case. One of Ofgem's duties lies in protecting the subset of consumers who remain disadvantaged.

Complaint handling and redress

This should be another priority area for Ofgem. We look forward to seeing Ofgem's proposals for the introduction of alternative complaint handling and redress schemes which ought to complement one another and existing schemes to optimise the consumer's ability to tackle detriment effectively.

Ofgem's Consumer First project should:

- identify any gaps in complaint resolution and consumer redress;
- include a plan to deliver an adequate service to consumers, both by raising their awareness of the services which they can access to respond to potential issues, and by providing satisfactory resources if Ofgem needs to be approached directly;
- identify what is required to address consumers' needs, whether these relate to energy supply or to networks;
- adequately publicise the service on consumers' bills in clear, plain language, accessible in all forms as required by different types of consumer, as a minimum requirement.

It would be helpful if Ofgem could state what progress is being made on Consumer First, paying particular attention to the above points.

Any voluntary initiatives from the industry should sit alongside other forms of redress. If suppliers are increasingly the first port of call for consumers, there must be independent evidence of how effectively suppliers handle complaints and enquiries from first contact through to resolution. Ofgem must ensure that robust and audited monitoring and reporting of this activity occurs. Reporting will allow the relative

performance of suppliers to become part of the competition between them. Consumers need assurance that the various new schemes, in conjunction with any voluntary initiatives from the industry, provide an effective network of protection. If this is not delivered, then confidence in their dealings with energy companies may be adversely affected, increasing the pressure for more regulatory intervention.

Smart metering and sustainability issues

Energywatch supports smart metering as necessary mechanism in improving consumers' understanding of their everyday energy usage, how they can become more energy efficient and equally important, to rid consumers, particularly the fuel poor, of the problems created by inaccurate or estimated bills.. We believe that smart metering has the potential to:

- further increase competitive pressures on suppliers to deliver lower prices to consumers;
- encourage suppliers' ability to innovate and further reduce costs to serve for consumers;
- impact positively on the development of robust, flexible and active network management by operators;
- allow consumers to contribute effectively to Government sustainable energy objectives.

We do, however, have concerns about some of the current proposals and the amount of power they would place in the hands of suppliers. Ofgem must ensure that consumers are fully protected pre and post the smart meter roll out.

Ofgem can use the outcome of the current smart metering trials to take a strategic role in all these areas, furthering its secondary duty to promote sustainable energy use and helping to develop a 'joined up' solution alongside other government agencies. This approach would not stifle any innovation by suppliers or meter operators who could provide 'value added' services for additional cost to consumers who desire it. The basic smart metering product that all consumers will need to access through a wide roll out can be delivered more effectively through a coordinated strategic plan. A fragmented approach would simply dissipate any wider benefits from the use of smart meter technology.

Ofgem must ensure that whatever solution is chosen, it:

- helps to solve the problem of poor account management and inaccurate customer data;
- recognises how smart meters, combined with integrated programmes of consumer education, advice and support, can help consumers reduce their own carbon footprint; and
- ensures fairer tariffs for consumers.

Energywatch has participated in Ofgem's project to update its green tariff guidelines and establish an accreditation scheme. We welcome Ofgem's work in this area and support many of the proposals in its recent consultation. However, we are

concerned that the proposal to issue two sets of guidelines, one for 'renewable' and another for 'low carbon', will only add to consumer confusion. Research evidence supports our concern. We also consider that the accreditation scheme must be fully independent of suppliers and be perceived as such. We are concerned about the lack of consumer representative involvement, to date, in establishing the scheme.

Energywatch considers it essential that suppliers provide clear and accessible information to businesses and households about the renewable and carbon content of every tariff they offer. This would only require a small change to the current fuel mix disclosure obligations. Currently, suppliers are obliged to disclose accurate overall information about the generation fuel mix of the electricity they supply. Suppliers have the option to disclose this information for individual tariffs as well. This simply needs to be made mandatory. The change to regulations would be easy to introduce and would not impose substantial costs on suppliers. We consider the provision of such information would make a valuable contribution towards the goal of a consumer-driven sustainable energy market.

Energywatch considers that CERT and the post-2011 supplier obligation have important implications for the future shape of Britain's energy market. We welcome the Government's vision for a transformed energy market, whereby consumers are engaged in energy issues and play a key role in driving a market for sustainable energy products. We welcome Ofgem's work in this area and will continue to work with Ofgem in helping shape the supplier obligation and in exploiting opportunities within CERT to realise the transition desired. We urge Ofgem to continue to press for better integration of CERT with other energy efficiency programmes, such as Warm Front and Decent Homes, and to continue its work in helping suppliers fully realise the potential provided under the Priority Group flexibility fund.

Better regulation

Ofgem has indicated an increasing willingness to steer away from direct effective regulation and move towards facilitating and initiating debate within the industry and with wider stakeholders. This is reflected in Ofgem's budget and cost projections that highlight that reducing costs seems to be an increasing priority. Clearly there is a balancing act that it must perform between appropriate levels of direct regulation in support of its statutory duties and leaving the industry to develop effective solutions through self-regulation.

Ofgem will recognise that all industry players necessarily approach issues from a commercial perspective. This does not naturally lend itself to effective progress on issues where there may be significant disagreement or when compromise positions are reached which may constitute real areas of detriment to consumers. For instance, there are ongoing concerns about addressing poor data quality in the gas market, specifically as IGT connections increase. IGTs, distributors, shippers and suppliers have yet to show that there is a meeting of minds on developing effective data flows and lines of communication which reduce the transfer of erroneous data. The failure to address these issues will simply increase the ultimate costs to serve consumers and other detriment, such as confusion amongst consumers connected to IGTs about who supplies them and the risk of suppliers sending inaccurate or large

bills when suppliers catch up with consumers. Ofgem must show more willingness to act if the perception is that the industry cannot adequately address some issues.

Ofgem has highlighted that a review of existing Guaranteed Standards of Performance (GSoP) as they apply to suppliers will take place in the near future. This review should be conducted with an open mind and without a subtext that 'competitive' markets are delivering more effective remedies for consumers. Suppliers have shown no proven and longstanding track record of compensating consumers when they have failed to deliver the highest standards of quality of service to them. That has been the rationale for maintaining statutory GSoPs. Until there is a clear and transparent track record of suppliers' delivery of quality customer service, especially after alternative complaint handling and redress schemes are implemented and bed in, the GSoPs continue to have a place as a form of redress for consumer detriment.

We believe that Ofgem should undertake a post-implementation review of a number of recent and forthcoming initiatives in the coming years to gauge how effectively these have been and whether further regulatory action may be required. Specifically, the recent changes to supply licences will need to be considered both in terms of their effectiveness and of suppliers' compliance with them. We hope that Ofgem will not just assume that all the licence conditions are working for consumers or that they cannot be refined further where problems are discovered. Ofgem has indicated that it will undertake a review of the removal of metering price controls in 2008 and we would expect Ofgem to do so as soon as possible and to align this work with other meter related issues, such as the difficulties faced by PPM consumers and the service offered to consumers outside normal working hours as recently highlighted by the DCUSA modification proposal DCP008.

Similarly, once new complaint handling and redress schemes are developed and implemented, their effectiveness must be assessed after a reasonable period. Ofgem must follow up on the shortcomings that it identified with the ESO performance and ensure that these do not arise in the new scheme.

Of equal importance is the need for Ofgem to ensure that reliable information is made available to consumers (post energywatch) on the quality of service provided by suppliers to help informed decisions on switching. This could be through use of audited complaints data via the new standards, through Ofgem's information gathering powers, or from qualitative research commissioned by Ofgem.

Ofgem has recently started a process for assessing the effectiveness of industry code governance and whether the status quo is appropriate or not. We believe that Ofgem must approach the review with an open mind, without making an assumption that increased self-regulation will automatically provide a 'best fit' with its better regulation agenda. Consumer representation on the various code Panels will be an important aspect of the review and we intend to engage fully in the debate with Ofgem and other stakeholders.

Other issues

There is a strong argument for reducing and tackling the barriers to entry for potential market players which stifle competition and innovation, and which keep costs to consumers high, rather than consider the status quo or further reduction in the diversity of ownership as acceptable. Ofgem must thoroughly investigate any such future developments, keeping consumers' interests at the heart of its scrutiny.

We will continue to keep these issues under review as Ofgem develops its strategy, always considering the possible impact on consumers, and comment further 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

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