



Sent by email

*Promoting choice and
value for all customers*

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Date: 21 April 2008

Dear Colleague

I am writing to seek views on our monitoring and reporting of suppliers' social initiatives to help vulnerable customers.

As you are aware, in the 2008 Budget the Chancellor spoke of an increase in suppliers' collective expenditure on their social programmes to at least £150m each year over the period ahead. Government has now secured an agreement with suppliers building up to deliver this commitment over the 2008-2011 period.

Continuing upward pressure on energy prices will create difficulties for lower income customers and those in, or at risk of, fuel poverty. It remains Ofgem's priority to ensure that the energy market operates competitively as this is the most effective means of securing the lowest prices for all energy consumers.

Government has requested that Ofgem lead a process to set the parameters for what can be included by suppliers as part of their spend on social initiatives and the associated reporting arrangements. In June 2007 we developed a framework for presenting the information received from suppliers on their social initiatives. The aim was to provide a clear way to identify what social initiatives are available to assist vulnerable customers and to provide details of each of these offerings. In our August 2007 review¹ and the subsequent October update², we reported on data received from the six major energy suppliers using this framework.

For the August review we developed a methodology looking at social tariffs, rebates and trust funds. In the subsequent October update we sought to take account of the wide range of other initiatives and support suppliers offer which do not fall into the social tariff, rebate and trust fund categories. This update also looked at suppliers' pricing strategies. Whilst this does not form a part of suppliers' spend on their social initiatives, as outlined above, we consider it provides important additional context to suppliers' activities in this area. A summary of our methodology is attached in the Annex to this letter.

We recognise that there are many different approaches that suppliers are taking to assist their vulnerable customers and BERR have made it clear that they are looking for suppliers to innovate and indeed compete in this area. Our current social initiatives reporting

¹

<http://www.ofgem.gov.uk/Sustainability/SocAction/Suppliers/CSR/Documents1/Review%20of%20suppliers%20voluntary%20initiatives.pdf>

²

<http://www.ofgem.gov.uk/Sustainability/SocAction/Suppliers/CSR/Documents1/CSR%20update%20open%20letter%2023507.pdf>

framework aims to capture and reflect the work done by energy suppliers in this area. We welcome views on whether there should be any changes to the framework, what these might be and the reasons for them.

Your responses should be returned to Sarah Piggott, either by email or post at the details above, **by 5 May 2008**. If there are elements of your response which you consider to be commercially confidential, please bring this to our attention.

Once we have considered all the responses and discussed them as necessary, including with BERR, we intend to put out a proposed framework *for consultation* at the end of **May**. We then plan to publish the final framework by the end of **June** to allow suppliers to progress their plans for 2008-09.

We hope that the framework will be sufficiently comprehensive that suppliers will be clear whether future initiatives will fall within scope. However, should questions arise subsequently we would be happy to provide clarification.

Finally, as BERR have made clear, if we cannot secure agreement to the framework with suppliers, or if any supplier does not meet their commitments, we will flag the matter to BERR who will review the voluntary basis of these arrangements going forward.

Yours sincerely

Maxine Frerk

Director, Governance, Consumer and Social Affairs

Annex: Methodology for social tariff analysis

Our social tariff analysis is based on several assumptions which are set out below.

Average saving made by customers moving to the social tariff

1.1. The estimated cost of the supplier's social tariff is based on information provided by the relevant supplier. However, we have also calculated the estimated saving made by customers moving to the social tariff.

1.2. Where a supplier has indicated that its social tariff is based on a discount to a qualifying customer's current tariff, we have used the average tariff, based on the supplier's standard credit and prepayment tariffs and weighted for the number of customers on each of these payment methods. The social tariff discount is then applied to this figure.

1.3. To calculate the saving a customer makes by being on the supplier's social tariff, a weighted average bill based on the supplier's standard credit and prepayment tariffs for non social tariffs is calculated. The suppliers' average annual social tariff is then subtracted from the weighted average bill to give the saving offered by the supplier on a per customer per year basis. This value can then be multiplied by the total number of customers on the social tariff in order to estimate the total saving to a supplier's customers. For comparison, the benefit to customers was also calculated using each supplier's best offer and the market best offer (including internet tariffs).

1.4. Annual bills have been calculated assuming an annual consumption of 3,300 kWh for electricity and an annual consumption of 20,500 kWh for gas.

1.5. Powergen's Staywarm tariff has not been compared with the other social tariffs because of difficulties in judging both annual bills and consumption levels. However, we have made use of Powergen's estimate of how much the scheme costs them and how many customers are on the tariff. We have published all suppliers' cost estimations alongside our calculation of the savings offered by the social tariffs.

Best offer prices

1.6. The best offer price is drawn from Ofgem's tariff database, with data from The Energy Shop. For "best offer" we have selected the lowest (non-fixed) price tariff available to new customers as of July 2007. The tariff must be available in all 14 ex-PES regions. If the lowest tariff varies by region we have taken an average. In some cases, standard credit and PPM customers would have to switch meter/payment type in order to take advantage of the best offer tariff. Customers may face a charge to change the meter if they switch payment type from PPM. This potential cost to a customer accessing a best offer price has not been taken into account in the analysis.

Rebates

1.7. Information submitted by suppliers on the number of customers on their rebate scheme and the average available rebate have been used to estimate the total benefit of the rebate to consumers.

Pricing strategies

1.8. In the October update we included a chart to show the difference in each supplier's average annual gas and electricity bill weighted by the proportion of fuel poor customers on each payment method. An average across all suppliers was then taken and the difference from the average was calculated for each supplier. The chart however assumed that the customer takes both electricity and gas from the same supplier. In future reporting, we intend to produce a chart which shows the difference for each supplier to the average price paid by the fuel poor on a per account basis reflecting the actual mix of gas and electricity accounts for that supplier.