

Sarah Piggott
Ofgem
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Dear Sarah

Monitoring Suppliers' Social Initiatives – proposed reporting framework

Please find attached our response to the above consultation. We support the general direction suggested by Ofgem in terms of what should be included and excluded as part of a supplier's social spend. In particular:

- The view that a social tariff should be “at least as good as the supplier's standard direct debt tariff” is a reasonable starting point
- Recognition should be given to Trust Funds and Rebates.
- Energy efficiency initiatives should be included where true additionality can be identified.
- Current collective initiatives such as the Home Heat Helpline and data sharing schemes with DWP, all of which provides tangible and effective benefits to consumers, should be included.

We are however concerned that Ofgem's reflections on the concept of determining the validity of a supplier's social tariff by reference to a comparison with the lowest tariff available in the market show little insight into how seriously this would interfere with the efficient functioning of the market. This in turn would mean higher costs for all customers in the long run, including the fuel poor.

Reiterating the views expressed in our earlier response of the 2nd May 2008, we think it is essential for flexibility to be built into the governance and controls of this framework. Suppliers should be allowed the flexibility to innovate further in terms of providing targeted assistance to their customers. It is therefore important that this framework takes into account the full extent of the investments being made and more particularly the progress of suppliers in meeting their funding commitments.

As always, should you wish to discuss any aspect of our response, please do not hesitate to contact me.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Philip Arend', is centered within a light gray rectangular box.

Philip Arend
Senior Regulatory Manager

Question 1: What should the qualifying criteria be for a social tariff? Do you agree with our proposed approach?

We agree in principle with the approach identified.

A social tariff in its basic form is a mechanism of providing tariff relief to a specific segment of customers, with the primary aim of reducing household expenditure on energy.

British Gas' Essential tariff, delivers precisely that. It provides British Gas customers (in receipt of a prescribed list of benefits) access to direct debit rates regardless of the payment method they are on, which in turn helps reduce household expenditure on energy.

With such a scheme in place, delivering tangible benefits to customers, we accept the proposal to maintain the current approach, namely that of a social tariff being at least as good as the supplier's standard direct debit tariff. Ofgem indicates that this definition may be subject to change depending on the findings of the supply market probe and if changed could then be replaced by a tighter standard in 2009. While we understand the desire not to pre-empt the outcome of the probe, this does not send a positive signal to suppliers about the future regulatory environment. British Gas has led the way in this area through its Essentials product. While we will continue to look at the most effective ways of providing support to those who need it, the prospect of a more prescriptive standard possibly being introduced clearly dampens our incentive to look at further radical innovations in this area given the prospect that Ofgem might decide to change the rules of the game next year.

Question 2: Do you agree with the changes we have proposed to calculate suppliers' contributions from their social tariffs?

In our response of the 2nd May we expressed the view that the methodology of reporting social tariffs was imperfect in that it failed to include the operational costs of supporting them. Whilst we still hold this view, we accept your proposal to continue your current approach of calculating a suppliers' contribution based upon the outcomes and benefits to consumers.

Question 3: What are the potential implications and benefits of assessing a supplier's social tariff against the lowest available for that payment method?

We are concerned about what the discussion from section 2.1 to 2.16 suggests about Ofgem's approach to social tariffs. Ofgem has a primary duty to promote competition where that is in the best interests of customers. It is disappointing that there is insufficient recognition of the impacts that a social tariff could have on the competitive market if Ofgem were to proceed with a definition according to which a tariff only counts as a social tariff if it is the lowest available in the market for that payment method.

The costs this would lead to are more fundamental than any "practical issues" that this approach might encounter. This policy if implemented would create huge distortions in the competitive market with unintended consequences. The idea that a judgement could be made on a British Gas social tariff on the basis of how it relates to a product of a competitor, who might have completely different costs, capabilities and commercial strategies to us is an extremely odd concept in a competitive market. This would be the equivalent of setting some sort of (moving?) external benchmark against which suppliers must operate to deliver social support, regardless of their own costs or commercial priorities.

Why this particular lowest tariff should be worthy of being such a focal point for the regulator and other suppliers is not explained. It would mean that one supplier's tariff would provide a constraint on how other suppliers act in determining their social tariffs. The benefit of the concept is unclear. And even if benefits are articulated, are there really no other ways of delivering those benefits without distorting the commercial decisions all other suppliers make?

Even making a judgement on the basis of how a supplier's social tariff relates to its own lowest tariff at a particular time would clearly not achieve what its proponents would like. Naturally we and other suppliers would then be reviewing the commercial viability of our lowest tariffs, if the effect of having them is to change the value attached to our social tariffs by the regulator. Suppliers would simply have reduced incentives to offer cheaper products.

We understand the desire of front line agencies to have confidence that they are referring customers to the best deal available. But it would be counterproductive to have rules which then lead to less choice and product innovation for all customers, including the fuel poor, who most need the competitive market to work well for them. If a policy of this type was implemented, it would indeed be simpler for the agencies to work out the best deal for the customer but only because there would (in the long run) be less cheap deals and less innovation reflected in the products on offer.

Ofgem notes in 2.8 how it is important to know whether "it is better to provide a little help to many or more help to a few". It is however equally important to think about how social tariff customers *and all other customers* are affected by Ofgem's approach. All other customers are of course paying for the social tariffs enjoyed by others. At a time of substantial increases in energy prices, many fuel poor people will be among those who will not be eligible for social tariffs. They will however be contributing to paying other people's energy bills as well paying their own.

All these factors highlight why Ofgem needs to give more thought to why this (albeit well-intentioned) policy proposal may actually seriously damage the interests of *all* customers if it is taken forward. Even those who directly benefit from social tariffs may not be better off in the long run if the effect of the policy is introduce regulatory distortions which interfere in an arbitrary way with normal commercial decisions.

Question 4: Do you agree with our proposed approach to including rebates as part of suppliers' social spend?

Yes, we agree. A monetary rebate, when applied directly against a customer's energy bill is an effective mechanism of delivering tariff relief to the customer. On this basis we agree that rebate schemes should continue to be included as part of a suppliers social initiative.

Question 5: Do you agree with our proposed approach to including PPM equalisation as part of suppliers' social spend only where it is targeted at fuel poor customers?

In principle, yes. However, our view is that there must be some form of additional benefit to a fuel poor customer in order for this to qualify.

We fully support the view expressed within 3.16 that a blanket approach to PPM equalisation would be a poorly targeted approach. Since the majority of fuel poor customers do not use

prepayment meters, equalising prepayment meter tariffs to, for example monthly direct debit would not actually mean that the majority of the fuel poor customers – those not on prepayment meters – would end up paying more for their energy. This is because it would become more costly for energy suppliers to offer such low direct debit and standard credit prices as they currently so if they were forced to offer the same price to prepayment customers also (given the higher costs of serving prepayment meter customers).

However, if PPM equalisation is applied in a targeted and quantifiable way for example as we have done with our Essentials Social tariff and providing predefined qualification criteria is adopted at customer level then it may be considered as fuel poverty measure.

In the scenario where a supplier has equalised PP rates for all customers irrespective of circumstance, we do not agree that the supplier should be able to pull out and claim “credits” for that proportion of their customers who they believe to be fuel poor. To qualify for a “credit”, there must be some form of “financial additionality” to the fuel poor customer that is over and above what is generally available to all customers. Simply identifying customers who are potentially fuel poor customers; whilst not providing additional benefits should not be regarded as a fuel poverty/social initiatives scheme.

Question 6: Do you agree with our proposed approach to including trust funds as part of suppliers' social spend?

When assessing a supplier's contribution to a Trust Fund it is important to reflect the set-up and nature of the Trust.

For example, where the Trust has charitable status and therefore is independent from their donor companies as is the case for the British Gas Energy Trust and EDF Energy Trust, then the full amount donated by the donor company to the Trust should be recognised as being part of their CSR spend.

For example, the British Gas Energy Trust has been established with full charitable status, operationally independent from the donor company. The decision as to how its budget is applied (be it administration or funding) is a decision for the Trust only and is made within the framework of their charitable status. On this basis, full recognition should be given to the amount donated from the donor company to the Trust.

However, where the Trust is not independent but is administered by the donor company, then our view is that donations made to the trust should not be included given the high level of flexibility the company would have over application of funds, or changes to funding levels over time. If to be included, then only direct customer support should be included. Furthermore, stringent, prescribed and auditable qualification criteria should be put in place, and monitored by OFGEM.

Question 7: Do you agree with our proposed approach to including other categories of spend towards suppliers' social spend targets? In particular our proposed approach to energy efficiency initiatives, debt prevention initiatives and operational costs?

Yes, we agree.

For the review to be of value it's important that it takes into account, and recognises the full range of initiatives and support suppliers offer their fuel poor and vulnerable customers. We have long advocated the need for flexibility to be built into any such review so that it enables suppliers to continue to develop innovative schemes that provides help to customers in a targeted and appropriate way. To purely focus on social tariffs, rebates and trust funds would effectively disincentise suppliers to develop "niche" schemes and partnership approaches which are just as effective in delivering the long term objectives to the "harder to reach" customers, but by their very nature are unlikely to impact large volumes of customers.

We specifically agree that the costs of providing Benefits Health checks should contribute towards a supplier's social spend. We would suggest that Ofgem collaborates with suppliers in order to set rate card values to cover the fulfilment costs of supporting benefit health checks etc (and therefore identify what is meant by "efficient" costs).

In addition we believe further thought should be given to having in place some criteria to quantify the benefits to the consumer, and providing some form of recognition of the financial benefits achieved. Whilst it is important to reflect the extent of support provided to provide the checks, the actual increase in income obtained by the customers must surely be one of the core measurements of success.

Question 8: How do we ensure robust and true additionality in suppliers' calculations of their energy efficiency spend above their statutory obligations?

We agree with the principle of including energy efficiency initiatives within a suppliers social spend targets, if additionality can be demonstrated above their statutory obligations.

To avoid double-counting each proposal should be judged on a case-by-case basis. Where for instance, suppliers are supporting a Warm Zone, there must be clear transparency of the proposed expenditure on statutory obligations e.g. CERT, and that on social initiatives, to avoid cross subsidisation. Ofgem will need to determine that the cost of carbon abatement on the CERT element is consistent with prevailing market rates to avoid any manipulation of the social spend element.

Suppliers should also have flexibility to support measures for fuel poor households that would not otherwise be cost effective under the CERT programme, for instance solid wall insulation. Only measures accredited under CERT, with clearly defined energy savings should be permitted. To avoid double counting, Ofgem will need to assess the level of CERT funding that would normally apply to these products; this could be calculated at Defra's forecast cost of carbon abatement within the Priority Group (£24.70 tCO²). Additional spend associated with this activity, which is above this level, would be permitted against supplier's social spend target at this pre-defined rate.

Question 9: Do you agree with our approach to include efficient administration costs where they relate to specific projects involving joint working across industry?

Yes, we agree. In particular we welcome the views expressed within 5.24 that current collective initiatives such as the ongoing support of the Home Heat Helpline; the current pilot with EAGA and winter mail-outs etc will be included. These are all valuable initiatives which would otherwise not have been delivered if purely undertaken on an individual supplier basis. We are please that the costs incurred by the energy suppliers in establishing and administering

protocols and operational processes etc will be included.

Question 10: Do you agree with our proposed approach to calculating suppliers' contribution towards their social spend targets?

We agree and support this being the methodology for calculating the spend

Our agreement to the voluntary approach was, and always has been conditional upon this remaining the methodology. We therefore seek an explanation as to the comment within paragraph 6.9 that "target spend level may be revised for 2008-11".

Question 11: Do you agree with our proposed approach to setting the baseline spend?

We agree in principle.

Question 12: Do you agree with our proposed approach to include analysis on suppliers' overall tariff and pricing strategies?

We seek confirmation that this relates purely to the analysis presented of the benefits available to consumers rather than determining the benefits to the customer and therefore the contribution to the target.

Question 13: Do you agree with our proposed approach to our monitoring role?

Yes, we agree.

Question 14: Do you agree with our proposal to require assurance from the Board of each supplier to ensure data accuracy?

We do not believe that this approach is necessary, but propose that Ofgem adopts the same model followed by CERT.