RWE npower

By e-mail only

Ms S Piggott
Social and Consumer Affairs
Ofgem
9 Millbank
London
SW1P 3GE

Name Paul Tonkinson
Address 1 Bridgwater Rd, Worcester, WR4 9FP
Phone 01905 340501
Fax 01905 340710
e-mail paul.tonkinson @npower.com

12 June 2008

Monitoring suppliers' social initiatives – proposed reporting framework

I refer to the Ofgem document of 30 May.

Introduction

As the document indicates, given the increase in, the importance of, and the greater weight placed on, suppliers' social expenditure, it is vitally important that this is correctly and properly measured, while allowing for a transparent and meaningful comparison between suppliers and preserving a diverse approach to dealing with fuel poverty.

As you may recall from conversations and correspondence we have sent you, we maintain that there is scope for measuring not just the inputs of any measure, but also the outputs. While this may be harder, it does identify what has worked best from suppliers' suite of initiatives. In the light of the intention of to continue with an inputs based approach, it is pleasing to see that there will be some attempt to assess the impact of different measures.

We also support the comments made by other respondents to the open letter that in order to ensure that suppliers can spend the money most effectively there needs to be a degree of flexibility regarding expenditure committed within each year. Our proposals to address this are outlined in the response to question 10. As per paragraph 8.9, we welcome Ofgem's indication that it intends, before publishing the annual report on suppliers' social programmes, to raise any concerns the latter have in meeting their social spend with BERR for further consideration.

Below, we answer the questions asked in the order and by reference to the section headings under which they appear in the document.

RWE npower

Trigonos
Windmill Hill Business Park
Whitehill Way
Swindon
Wiltshire SN5 6PB

T +44(0)1793/87 77 77
F +44(0)1793/89 25 25
I www.rwenpower.com

Registered office:
RWE Npower plc
Windmill Hill Business Park
Whitehill Way
Swindon
Wiltshire SN5 6PB

Registered in England
and Wales no. 3892782

Social Tariffs

Q1 What should the qualifying criteria be for a social tariff? Do you agree with the proposed approach?
Q2 Do you agree with the changes we have proposed to calculating suppliers' contributions from their social tariffs?
Q3 What are the potential implications of assessing a supplier's social tariff against the lowest available for that payment method

You propose that a social tariff can be called such where it is at least as good as an individual supplier's direct debit tariff. From a npower perspective, we believe that a social tariff should only be categorised as such if it is below the direct debit rate of the supplier offering it. The main purpose of a social tariff is to ameliorate the impact of the rise in fuel prices for those least able to pay. Intuitively therefore, it seems right that this particular group ought to get more than other customers who choose to pay by direct debit. Otherwise those customers who are not in fuel poverty get an equally good deal simply by paying by direct debit.

It ensures all fuel poor customers who pay by standard direct debit will receive additional help, because, at present, those who pay by monthly direct debit obtain no benefit through a social tariff from some suppliers. People who fall into fuel poverty do so not because of how they pay for their energy; they do so for many reasons irrespective of their payment method. We estimate that 35 - 40% of fuel poor customers pay by monthly direct debit. The proportion is broadly similar for the overall group of customers who are in fuel poverty. As such, we believe that fuel poor direct debit customers should be able to benefit from a supplier's social tariff.

While the some elements of this argument may apply for online tariffs, the proportion of fuel poor customers accessing these products is far smaller. As you recognise in paragraph 2.7, the prices for these change frequently and so to link a social tariff to this would, in all likelihood, be administratively difficult. The prices for standard direct debit offerings remain more stable for a longer period of time than online tariffs. Pricing below standard direct debit preserves the competitive market between suppliers, but offers a distinct proposition for qualifying fuel poor customers.

We do not believe that a social tariff should be lowest available for that payment method regardless of which supplier the customer is with (paragraph 2.5). What this appears to be alluding to is some form of equalised tariff across the board that is, in effect 'supplier blind', and that this will be dictated by whichever supplier has the lowest payment method. As you state, this could create confusion for customers as well as practical problems for suppliers and customers alike. As you state, such an arrangement could be construed as de facto interference in, and essentially taking qualifying customers out of, the competitive market with all the ramifications attached to that.

We agree that there should be transparency in comparing suppliers' social tariffs with other offerings to highlight the benefits for customers.

Turning now to suppliers' contributions from social tariffs. It is our experience that fuel poor customers use more fuel than the notional figures quoted of 3,300kWh for electricity and 20,500kWh for gas and which Ofgem used for its calculations. It must be the case that the savings customers make on a social tariff together with the cost to suppliers in providing it are based on actual consumption.

We therefore agree with the proposal to use average actual data for social tariff customers along with the split across payment methods. It is also pleasing to see that you propose to collect more information about E.ON's Staywarm tariff. It is only on a like-for-like basis that suppliers should be compared, and while diversity of approach is to be welcomed, it should be transparent.

Rebates and other discounts

Q4 Do you agree with the proposed approach to including rebates as part of suppliers' social spend
Q5 do you agree with the proposed approach to including PPM equalisation as part of suppliers' social spend only where it is targeted at fuel poor customers.

We agree that rebates are an important part of suppliers' social offerings for the reasons stated: particularly to provide flexibility, given that suppliers have to achieve a year-on-year level of spend against a backdrop of external constraints. However suppliers should be required to demonstrate the measures taken to ensure that the rebate was targeted towards fuel poor customers. This will ensure that rebates are an efficient form of spend and is not simply a means to disburse unallocated expenditure.

Like Ofgem, we do not believe that rebates impact on competition and prevent customers from switching. They have been an integral part of the domestic competitive gas and electricity markets since the latter's inception. Rebates are often a simpler proposition for customers to understand than general tariff comparisons as they are completely transparent.

In respect of spend to equalise PPM prices with other payment methods, we agree, for the reasons stated, that this should be counted against suppliers' targets for fuel poor customers who may benefit from a social tariff. Primarily the reason being that the majority of PPM customers are not fuel poor.

Trust Funds

Q6 Do you agree with our proposed approach to including trust funds as part of suppliers' social spend?

Paragraph 4.3 states that some commentators see trust funds as a means of writing off debt that would be unrecoverable anyway and recycling the funds back into the company. In npower's case as part of a our day-to-day business as usual activity we do not write off any live debt. Any debt that is deferred or eventually written off via a trust fund is therefore solely for the benefit of the consumers concerned, not the company.

As the document recognises, trust funds are an integral part of suppliers' offerings. While counted as part of these, their status means that they are not within direct control of the suppliers; funds dispensed are the responsibility of trustees. There are also timing issues as to when money is actually spent - as opposed to committed or donated spend - which do not take account of notional dates. See our comments under 'Calculating suppliers' contribution' below for a more detailed explanation.

In addition, some trust funds, for example npower's Health Through Warmth (HTW) leverages a far greater amount of expenditure than the sums dispensed. As well as this, HTW provides a crisis fund which is used as a last resort. This enables us to provide in excess of £10 of benefit for every £1 contribution made by npower. A transition to a target based upon money spent in year, rather than that committed, would undermine this model and create perverse incentives to spend the crisis fund. In our letters of 13 March and 6 May to Ofgem, we suggested that outputs should be measured as well as inputs. See our comments under 'Ofgem's monitoring role' below for a more detailed explanation.

Other categories of spend

Q7 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?
Q8 How do we ensure robust and true additionality in suppliers' calculations of their energy efficiency spend above their statutory obligations?
Q9 Do you agree with our approach to include efficient administration costs where they relate to specific projects involving joint working across industry?

We agree that a diverse approach is to dealing with fuel poverty is to be encouraged, not least that one of the sub-themes of the recent Fuel Poverty Action Programme was to get suppliers to share best practice of targeting their social programmes. The implication being that a 'one size fits all' approach is not likely to be as successful as utilising different approaches and learning from one's peers.

The costs of all initiatives which benefit vulnerable customers and which are not a direct statutory or licence obligation should be included within the expenditure reported. As we have stated before this would include, for example, expenditure on the Home Heat Helpline (HHH), the EAGA trial and DWP mailings.

Taking each heading identified in the Ofgem document in turn

<u>Partnerships</u>
We agree that partnerships and other initiatives' spend continues to be counted towards suppliers' targets.

<u>Benefit entitlement checks</u>
In the case of benefit entitlement checks (BECs), there is reference to suppliers being allowed to count expenditure of *'the efficient costs of providing them'*. What does this mean in practice and how does Ofgem propose to assess this? We agree that the provision of BECs should count towards suppliers' targets.

<u>Energy efficiency initiatives</u>
Regarding non-CERT energy efficiency measures expenditure counting towards suppliers' social spend targets. It is pleasing to see Ofgem is supportive in principle that this should be included where it is additional to the CERT statutory obligation. Expenditure here does benefit customers and should be recognised as such.

Debt advice and suppliers debt prevention strategies

We do work with and fund outside agencies and we welcome the view that this funding for these bodies should continue to be counted towards our expenditure.

Operational and administrative costs

It is a pity that Ofgem does not accept the principle of including the operational expenditure (opex) of suppliers providing all their social initiatives (other than for BECs – see above). An opex based initiative that is additional to any statutory or licence backed requirement (for example, HTW) can deliver outputs for customers that are comparable to social tariffs or trust funds.

All suppliers' funding of the HHH should count towards their social spend targets, as well as the opex cost of the EAGA pilot. With the latter, it is assumed that the £10 per customer fee that EAGA charges for the hand-off of each referral will also count. Equally. the opex costs of dealing with the referrals should also be allowable against suppliers' expenditure. It is pleasing to see that Ofgem does not rule out being able to include the costs of providing similar initiatives if a clear and compelling case can be made.

Calculating suppliers' contribution

Q10 Do you agree with our proposed approach to calculating suppliers' contribution towards their social spend targets?
Q11 Do you agree with our proposed approach to setting baseline spend?

Given the large sums of money Government is requiring suppliers to spend, then there needs to be a degree of flexibility to ensure that suppliers can spend the money most effectively.

We believe that the proposal to count only those monies which have been spent in a defined period rather than committed or accrued will have the impact of reducing effectively the help that customers might have otherwise received. If a customer has been promised assistance in one reference year, but this is delivered and the money spent in the next, it is not clear under the present proposal that this would be counted in either year.

If suppliers, in order to maximise the recognition for their expenditure, are expected to spend money in a particular calendar year, this may well result in an inefficient use of resources by suppliers for which they and, ultimately, consumers may not benefit. It would also seem to run counter to the requirement for the spend having to be *'efficiently incurred and effectively targeted at fuel poor customers '*, the criteria against which the Board will have to sign off data submitted to Ofgem (paragraph 8.7 refers).

This could be resolved if there was a means to allow a carry over of demonstrably committed or accrued expenditure which cannot be recalled or recast, but where the consideration does not take place until a later date. Conversely, early spend of a future year's allocation should be allowed to prevent eligible customers from - potentially - being turned away because the year in question's expenditure has been reached. CERT allows for this in the carry over of excess energy savings where they have been provided in one year, with the target having been reached within that year.

This is important for social expenditure for this year (2008-2009) because the framework on what can be counted will not be finalised until, effectively, half way through the year.

As you have implied we would ask that this is raised with BERR for further consideration

Related to this, we would ask that you explain what you mean by the statement in paragraph 6.9 about the September 2008 report that Ofgem will publish which will *'..clarify the baseline figure of suppliers' social spend and any revisions to the target spend levels for the 2008-2011 period.'* It was our understanding that the amounts committed to by suppliers had been agreed.

Suppliers' overall pricing strategies

Q12 Do you agree with our proposed approach to include analysis on suppliers' overall tariff and pricing strategies?

It is helpful to have a context within which to compare suppliers' social tariffs to both each one's other tariffs and each other's offerings. However, it has to be recognised that this may cause confusion or may not present a complete picture as there are subtle but, nonetheless, distinct differences in the applicability of the comparator tariffs used.

Also, as you recognise, there are a range of deals on the market which, while limited by geography or time, may provide a better option for particular customers. Excluding these, again, may skew results accordingly.

In paragraph 7.6, you detail how you propose to quantify the impact of suppliers' pricing strategies on fuel poor customers using the same methodology as in the October report last year. It was not clear then what the resulting graph was meant to show. A simpler and easier to understand methodology would be to show the average dual fuel bill of a fuel poor customer for each supplier, based on an acceptable payment method mix of fuel poor customers. An example of how this might look is given in the table below.

A fuel poor customer's dual fuel bill based on each supplier's average national prices as at 1 April 2008[1]

Company	npower	BG	E ON	EDF	Scottish Power	Scottish & Southern
Average GB dual fuel bill (£)	1,046.86	1,049.16	1,041.89	1,000.95	1,048.63	1,004.75
Rank	4	6	3	1	5	2

This, shown either in tabular form or graphically, should give a fairer indication as to the effect of suppliers' current pricing strategies. It is recognised however that any pricing summary such as this is clearly explained so that people using the document are

1 The table is for a dual fuel bill, based on average national prices, notional consumption and a payment method mix of 30% direct debit, 47% receipt of bill and 23% pre-payment with prices as at 1 April 2008.

aware that suppliers' relative competitiveness will vary over time, by region, payment method and consumption.

Ofgem's monitoring role

Q13 Do you agree with our proposed approach to our monitoring role?
Q14 Do you agree with our proposal to require assurance from the Board of each supplier to ensure data accuracy?

We currently complete a joint BERR/Ofgem questionnaire and we are happy to continue to do this. As is recognised, it may require changes to take account of the enhanced expenditure and any revisions to the monitoring framework to which this letter is a response.

It is a pity that Ofgem has demurred on the possibility of using an outputs based approach. While it is more difficult to establish an inputs and outputs measure, once done, assessing the impact of a particular measure or set of measures in relation to the cost of their provision can give a more complete picture of their effectiveness and value for money.

We agree that the Board should sign off on the data submitted to Ofgem for the purposes of monitoring suppliers' social spend. As mentioned above, you state that you '*..will require assurance on behalf of the Board that that the spend has been efficiently incurred and effectively targeted at fuel poor customers..*'. In addition to our comments above on flexibility and carrying over of spend, we would welcome clarification as to what this statement actually means; it would be unfortunate if a whole new regime of compliance and auditing arose as a result.

I hope you find the comments above helpful. Please do not hesitate to contact me if you require clarification of any of the points made in this letter.

Yours sincerely,

Paul Tonkinson
Economic Regulation