



Inveralmond House
200 Dunkeld Road
Perth
PH1 3AQ

Claire Tyler
Senior Manager, GB Markets
Ofgem
9 Millbank
London
SW1P 3GE

Telephone: 01738 456410

Facsimile:

E:mail: katherine.marshall @
scottish-southern.co.uk

Our Reference:

Your Reference:

Date : 11 July 2008

Dear Claire

Ofgem Open Letter: Prepayment Meter Customer Switching

Thank you for the opportunity to respond to Ofgem's open letter of 30 May in which a number of questions are posed regarding the issue of customers switching to more expensive suppliers.

We have attached a paper setting out our detailed comments.

All of the options proposed have been made on the basis that there is a problem for prepayment meter customers and that this requires this customer group to be treated in a particular way compared to customers who use other payment methods. We do not believe that there is a fundamental problem with competition in this segment of the market and we would therefore strongly urge Ofgem to consider all the facts before taking any additional measures, including those proposed in the open letter.

Within the energy market, the most effective sales and acquisition mechanism continues to be doorstep sales activities. As part of our internal processes to ensure compliance with the marketing licence condition and the AES Code we have a robust sales verification process in place. When we acquire a customer via this sales route the agent contacts our customer service centre and the customer service advisor takes the customer through a series of questions to ensure amongst other things, that the customer is aware that they have agreed to switch to SSE, of the package that they have signed up to, the tariff that they are on and the payment method. This process, we believe, is robust and provides assurance that we are operating in a responsible way in the competitive market environment.

We have serious concerns with Ofgem's proposal that one remedy to address the perceived problem would be to alert prepayment meter customers when they are switching to a more expensive deal. This is fundamentally unworkable and risks

making direct sales impossible for prepayment customers. For example, the requirement would result in all direct sales staff needing to have up-to-date comparison information for all rivals' products and at all consumption levels. They would need to be trained in making such comparisons, monitored in terms of compliance and procedures would have to be written for cases where a supplier was not the cheapest.

We believe that the additional costs of compliance would undermine direct selling as an economically viable route to market for prepayment customers. As a consequence, Ofgem needs to consider carefully the implications that this could have on the competitive market: it could stifle innovation and lead to a reduction in the number and variety of products offered to prepayment customers. It also risks segmenting one particular customer group to the detriment of those customers. In short, we believe there is a considerable risk that this regulatory requirement would significantly reduce, if not remove altogether, competition for prepayment meter customers.

Furthermore, we know of no other competitive market where there is a requirement to advertise the prices/products of rivals. We do not see how this could be capable of being policed in a dynamic and competitive sales environment.

Any remedy, must be proportionate and should not create unnecessary or expensive additional burdens on suppliers or be detrimental to the efficient operation of the competitive market. We therefore welcome Ofgem's approach to seek to avoid new licence conditions and to explore alternative actions. If Ofgem considers that further bureaucracy is required in this area, we could support a minimal requirement on suppliers to alert all customers to the importance of checking that the product is best for them and where to obtain impartial advice.

We are firmly of the view that if any actions are identified they should be targeted at all customers, irrespective of payment type. We do not believe that prepayment meter customers should be particularly "singled-out" for special treatment by suppliers or other organisations. This merely serves to perpetuate the myth that prepayment meter customers are in some way disadvantaged compared to customers using other payment methods. This risks segmenting the market to the detriment of competition and customers.

Fundamentally, we do not believe that regulatory action is required to address the issues raised. Where evidence has been provided of mis-selling or other inappropriate activities, we consider that Ofgem already has the appropriate powers to take action against the company or companies concerned.

If you like to discuss any of the points made above or in the attached paper in further detail, please give me a call.

Yours sincerely



Katherine Marshall
Regulation Manager

SSE Response to Ofgem's open letter 30 May 2008: Prepayment Meter Customer Switching

Requirement on suppliers to provide a written statement of the savings that will be available to the customer from switching provider

This sounds like a simple enough concept, but there will be practical implementation issues. For example, at what point in the sales and transfer process would such a statement be provided. SSE has a verification system as part of its sales processing arrangements. Customers have the right to a cooling-off period; during this period of time the customer could exercise their right to change their mind and cancel the transfer. Ofgem needs to ensure that any new requirement is proportionate and is not detrimental to the effective operation of the competitive market.

We are concerned that this is not a practical or feasible option on a customer by customer basis. First, suppliers would need to have access to up-to-date information about each of their competitor's products and at all consumption levels. Whilst this information is generally available and, indeed, required by licence condition to be provided on request to anyone that requests it, it places an onus on all suppliers to update the information on an ongoing basis. This is simply not a practical proposition in a competitive market where doorstep sales is still the major means by which suppliers acquire customers.

Second, such a requirement does not take account of the fact that each customer has a unique usage pattern and therefore may not fit in to the "typical" domestic consumption levels. Customers and indeed the sales agent may not know for certain whether the customer meets one profile or another. At the extreme, such a measure could potentially require suppliers to invest in complex IT systems to ensure that the agent has access to the most recent information. Furthermore, there could always be the potential to mislead whenever another supplier changed its prices. As soon as a rival supplier launched a new product the information would need to be constantly updated.

A requirement on suppliers to provide the customer with pricing factsheets (for example those prepared by energywatch) at the point of sale which show each supplier's offerings based on average consumption

Again, we believe that there are practical implementation issues associated with this option. Suppliers offer many tariffs and average consumption levels vary depending on the individual customer's circumstances.

Whilst it is true to say that we do monitor competitors' prices and product offerings, the literature would need to be presented to customers in a user-friendly way and we are not convinced that it would add extra value. It is not clear whether the requirement would be to list all rival products or just a selection of basic tariffs.

In order for this information to be truly meaningful to customers it would need to be constantly updated with the inevitable additional costs and administrative burden on suppliers. Sales staff would also need to be trained in making comparisons. This would have consequences for existing participants and could also be a potential burden on new entrants.

Furthermore, because of regional variations in consumption patterns there are additional factors to consider. For example, a household with an electricity only supply which uses electricity as its primary source of heating will have a completely different consumption pattern and energy bill to a household with a dual fuel supply using gas as its primary source of heating but with poor insulation and an inefficient boiler.

We are concerned therefore that there are inherent risks associated with the provision of such information, which would have to be heavily caveated. We are not convinced that providing this additional information would achieve the desired outcome, namely to enhance customers' choice and enable them to make informed decisions about changing supplier.

A requirement on suppliers to alert customers to the importance of checking that the product is best for them and to provide details of where to obtain price comparison advice

If Ofgem considers it is necessary to impose additional obligations then we could support this proposal, which is similar in concept to arrangements in the financial sector. It could be relatively simple and quick to introduce as a step in the sales verification process or to develop a standard information leaflet, which could be provided to the customer at the point of sale.

However, we do believe that Ofgem should bear in mind that at the fuel poverty summit commitments have already been made by industry to initiate improvements in the general information and advice that is made available to customers. In this regard, SSE has already engaged with a variety of stakeholders and is including partnerships with organisations such as Citizens Advice Bureau and Money Advice Trust. Educating trusted intermediaries about the competitive market is an effective way of helping to raise awareness of the benefits of competition for all categories of customers.

In addition, the switching sites have signalled their intention to provide additional services to customers who are unable to access their services online. Furthermore, we understand that the new NCC will take on responsibility for maintaining the pricing information factsheets and the confidence code when it replaces energywatch in October.

It is important to give these initiatives the opportunity to play out before further action is taken.

A requirement on suppliers to alert customers at the point of sale where they are switching to a more expensive supplier

We have concerns that this approach could potentially be misleading and assumes that customers make decisions only on the basis of price.

First, it would be difficult for a supplier's sales agent to make that statement categorically unless the individual has access to point of sale competitor information. All direct sales staff would therefore have to carry up-to-date information for all rival

products and at all consumption levels and be trained in making comparisons and explaining them to customers. It would also create a need for additional monitoring and compliance procedures for the direct sales force. The sales agent would need to be able to deal with cases where a supplier was not the cheapest. These points, coupled with the other practical implementation issues we have outlined above make the proposal fundamentally unworkable and risk making direct sales uneconomic for suppliers, to the detriment of competition and customers.

Furthermore, such an approach ignores the fact that customers are influenced by a range of factors when making a decision about their supplier. Some customers may knowingly elect to switch to a more expensive product offering, for example because of a partnership arrangement or to support environmental credentials. We know of no other competitive market where certain criteria are imposed on the customer as part of the decision-making process. Customers should be allowed to make an informed choice of supplier based on their own criteria.

A requirement on suppliers to alert customers as part of the follow-up contact (under SLC 25) where they are switching to a more expensive supplier.

Again, this approach raises the same issues as outlined above unless the advisor has access to accurate competitor price information. One option could be for the sales verification process to be adapted to remind the customer that they should check that the product is best for them and how they can access impartial advice.

Win-back activity

Win-back activity, whilst relevant, is not, in our opinion, where attention should be focused, unless there is questionable conduct surrounding the use of the right to object. Win-back activity is legitimately carried out by suppliers once they have received notification that the customer is transferring. There could be merit in suppliers conducting win-back activities seeking to establish why the customer has decided to leave the supplier and where there have been any incidents of inappropriate sales activities to refer the case.

Additional comments on Ofgem's analysis and the extent to which it suggests there is a problem which needs to be addressed to ensure PPM customers are getting the best deal

With regard to customers moving to a more expensive supplier, we can state with a high degree of confidence that for the first three months of the year, any customer switching to SSE from another supplier would be paying less.

We note Ofgem's analysis and recommendations on tariff differentials from June 2007. At that time, Ofgem indicated that costs to serve PPM compared with direct debit and standard credit were £85 and £60 respectively for a dual fuel customer.

In terms of tariff differentials for different payment methods SSE firmly believes that the cost differentials we have are fair and justified. We are less certain that those of our competitors are, particularly some internet tariffs. The only tariffs we currently

offer which are not cost-reflective are designed not to be: our tariff for electricity prepayment meter customers and our social tariff.

In support of this we have already provided Ofgem with a paper setting out detailed analysis of the costs associated with serving customers on direct debit, standard credit and prepayment meters. It would be helpful to understand how this compares with the detailed analysis that Ofgem has undertaken and what Ofgem has included in its costs to serve, particularly given that this differs from the figures presented by Government in last year's Energy White Paper.

Ofgem's analysis indicates that the premiums paid by PPM and standard credit customers over direct debit have on average significantly risen in recent years. This may be true for some of our competitors, but for SSE this is simply not the case. In fact, since we aligned our electricity PPM prices in January 2007 in response to calls from consumer groups, the differential for gas PPM customers vs standard credit has narrowed slightly and is now approximately £41 which we consider to be reflective of the underlying costs associated primarily with the provision of the meter and infrastructure.

To conclude, therefore, that differentials are widening is simply not the case for SSE.

If we look at our competitors, it is true to say that PPM vs Direct Debit differentials have widened in recent years, particularly online direct debit differentials. We understand that Ofgem is looking into these issues as part of the retail market probe and await with interest its initial findings.

Notwithstanding this, however, Ofgem itself has stated that only around 20-25% of customers are fuel poor and therefore fall into the category of vulnerable. It is important to note that prepayment meters are used and indeed chosen by a variety of customer types and therefore it would be inappropriate and misleading to assume that all PPM users in the country are vulnerable and therefore do not possess the confidence, knowledge or wherewithal to obtain additional information to help them make a good choice about changing supplier. In fact, vulnerable and fuel poor customers are more likely to pay by direct debit or standard credit arrangements than PPM.

We do agree, however, that vulnerable customers are likely to be reactive rather than necessarily proactive switchers and therefore it is vital that, irrespective of payment method, such customers know how to access information to help them make an informed choice. Initiatives have already been launched to address concerns raised as part of industry discussions on fuel poverty and these should be given the chance to take effect before further action is taken.

We do not believe that PPM customers deserve any special attention. We do consider however that any initiative which explains the benefits of switching supplier, the questions that a customer should ask or things to look out for would be helpful. This is why SSE is already participating in a variety of initiatives with trusted intermediaries to help improve customers' understanding and perception of the competitive market.

Such perception is not helped by accusations by energywatch amongst others that the market is not working, which may actually be detrimental to the interests of customers if it deters them from changing supplier.

Compliance with existing legislation

As we have outlined above, we have robust procedures in place to ensure compliance with the marketing licence condition, the AES Code and our other legal and regulatory obligations.

Ofgem recently consulted on whether the current marketing licence condition should be retained and we agreed with Ofgem's conclusion that it should remain for at least another year.

We agree that additional protection is also afforded to customers via the CPUTRs and look forward to receiving some guidance on their application in the energy sector. In addition, the energy Ombudsman now has a remit which includes sales activities.

We are firmly of the view that there are already in place sufficient safeguards to ensure that customers are protected and that Ofgem has at its disposal appropriate remedies where breaches have been identified. At this stage whilst Ofgem is still carrying out its investigation into npower it is difficult to comment. Depending on the outcome of that enquiry we are confident that if necessary Ofgem will use the full range of powers it has available.

We are aware that it could be possible that suppliers are not misleading customers but nevertheless customers may be making ill-informed decisions. As we have set out above, we believe that the solution to this is to ensure that customers have access to clear and transparent information about suppliers' offerings. The most obvious route to this is via trusted intermediaries such as advice agencies, switching sites and Ofgem.

One area over which we do have some concern is suppliers' advertising which clearly has the potential to mislead customers. It can create an impression about a company which is completely unfounded. For example, recently, British Gas has been advertising that "for every £1 spent on the fuel poor, 66p is spent by British Gas." We have complained to the ASA about this statement because we consider it to be highly misleading for customers.

We await with interest the outcome of the further research Ofgem is carrying out into consumer behaviour and to see what factors may have influenced customers to switch to a more expensive supplier.

Options for new licence obligations

As we have stated above, we are firmly of the view that additional regulation is not necessary or appropriate at this stage until the outcome of Ofgem's investigation into npower's activities are known. We are sure that Ofgem has already taken steps to find out from the other two "more expensive" suppliers the reasons why they have gained so many customers and the research that Ofgem has commissioned will help inform that piece of work.

Within the highly competitive supply environment there is a real balance to be struck between providing customers with sufficient impartial, reliable information and advice on the one hand, and letting market forces determine what is of most value to customers. The most successful suppliers will be those that have the best price, service and product combination which meets the needs of their existing and prospective customers. Suppliers will continue to innovate to gain and retain customers. Against this backdrop, it is important to recognise that customers' behaviour is not always predictable or logical. Provided the customer has not been misled, and that sufficient remedies are available to punish those suppliers who have misled customers, we feel confident that customers do have sufficient protection in the energy sector.

We are interested in Ofgem's statement that PPM customers are "typically" on lower incomes. It would be useful to understand what has informed this view.