Ofgem Supply Market Probe

Written response submitted on behalf of the Government's Fuel Poverty Advisory Group for England (FPAG) by Derek Lickorish (Chair)

FPAG welcomes the opportunity to respond to Ofgem's consultation regarding the Supply Market Probe.

1. FPAG Context

- **1.1 Fuel Poverty Figures**. FPAG estimates some 4 million households in **England** to be in fuel poverty as at September 2008. This compares with 5.1 million in 1996, 3.4 million in 1998 and 1.2 million in 2004. The reduction of 3.9 million between 1996 and 2004 was due to a mix of falling energy prices, energy efficiency and increased incomes. Of the 3.9 million reduction, some 2.92 million (75%) was due to the improvement of incomes. Meanwhile, average domestic duel fuel bills (Gas & Electricity) have increased from £572 to £1,287 (+125%!) between January 2003 and September 2008

- **1.2 C. 4M in fuel Poverty**. Of the estimated 4 million fuel-poor households, over 50% are pensioners and overall some 80% can be categorised as vulnerable.

- **1.3 Non gas areas.** Some 2.1M homes in England do not have mains gas, of these circa 630,000 (30%) are fuel poor customers. **No** dual fuel discount and exacerbated by space and water heating costs using kerosene or LPG being respectively 60% and 100% higher than those for mains gas.

- **1.4 Prepayment meters.** Circa 440,000 (11%) fuel poor households use prepayment meters

- **1.5 Standard Credit.** Circa 2,440,000 (61%) fuel poor households pay by standard credit.

- **1.6 Conclusion.** The majority of fuel poverty customers are adversely affected, over and above very high fuel prices, by the initial findings of Ofgem's 'Probe'. The potential for the numbers of pre-payment customers to significantly increase, following this winter's period of very high bills, is also a further and serious cause for concern.

2. Promoting more active engagement of consumers in the market

- **2.1 An annual statement for all customers.** The annual statement should identify the following: – 1. the tariff options and costs associated with paying by different methods – 2. the supplier's social tariff and eligibility criteria – 3. the basis for the direct debit calculation and refund criteria – 4. Warmfront eligibility criteria. The information also to be available via the internet; the statement should contain the necessary detail to facilitate internet access. This would then also enable trusted 3rd parties e.g. CAB etc to access the data on an individual's behalf.

- **2.2 Promote confidence in switching sites.** All sites should be required to submit themselves to a rigorous, comprehensive and independent audit process to ensure consumers can have confidence in the services they provide. The sites should then be regularly monitored by Consumer Focus and, should any fall below the code standards, they would risk having their accreditation withdrawn. In addition, suppliers should be required or encouraged to have commercial arrangements with only accredited sites.

3. Helping consumers to make well informed choices

- **3.1 Reform of suppliers' sales practices.** It is unlikely that a customer would willingly change supplier for a more expensive deal and even more so for the already disadvantaged pre-payment customer. The revelation from the probe findings that some 45% of pre-payment customers are changing supplier for a worse deal raises a very serious concern. In the absence of any available data to contradict that information, FPAG asserts the view that this is a symptom of mis-selling. This is likely to be caused by a lack of information and process rigour of the pre-payment proposition at the time of sale. Furthermore, the modus operandi of pre-payment metering does not easily reveal the financial consequences of the poor information given at the time of the sale, unless some subsequent and detailed analysis is undertaken. In view of this serious issue, FPAG recommends that a licence condition be imposed for pre-payment customer acquisitions only. Whereby the potential new supplier is required to advise the potential new customer, in writing, they will be paying more than their existing deal should the transfer proceed. Some suppliers will raise concern about more costs, hurdles and system issues. However, from an FPAG perspective, it is difficult to judge how any voluntary solution or requirement for further signatures against particular clauses in the sales contract is going to overcome this serious problem. There does not appear to be any significant current down side for the acquiring Supplier. Post this proposal, should problems persist, then the licence condition should be extended to all sales; this threat should provide a significant incentive for suppliers to get it right.

- **3.2 Easy to understand price metric.** FPAG supports this concept and recommends a simple kWh price of energy plus transmission & distribution. This would, therefore, exclude the suppliers' fixed cost to serve for each product type and should be shown separately.

- **3.3 Smart Meters.** FPAG welcomes Ofgem's declaration of intent to actively engage with government, suppliers and others to facilitate an efficient roll out of smart meters. FPAG is similarly keen to engage in this process and seek the opportunity for the pre-payment customer to be made a priority for smart meters. Investment in new technology appears to be the ultimate resolution of the inequity endured by existing pre-payment customers. However, the indicative timescale of 2010 to 2020 to complete a roll out should trigger a prioritisation for those most in need. Smart meters could also facilitate a whole new approach to debt and credit management with disconnection and load limiting only as a very last resort

4. Reduce barriers to entry, expansion and customer safeguards

- **4.1 Accounting separation** FPAG welcomes the proposal to require separate accounting of the suppliers' generation and supply businesses. This will provide a greater degree of transparency than hitherto and provide ongoing opportunities to give consumers confidence through regulatory oversight of the prices being charged.

- **4.2 Address liquidity issues in power markets.** Although FPAG welcomes this objective, it is far from clear how this issue can be effectively tackled. The complexity created by different political interests and the implication of territorial boarders, both European and non European, does not bode well for a speedy resolution.

- **4.3 A mandated social tariff.** The potential for price volatility, both in the short and long term, is a very real risk for customers in general and for the fuel poor in particular. It is for this reason FPAG asserts that, in addition to a requirement for Ofgem to facilitate clarity of Supplier social programmes, it should also be required to explore the pros and cons of a Social Tariff. It should be funded through an explicit Fuel Poverty Levy (FPL) and explored at a range of percentages, for all MWhs and Therms sold. Meanwhile, FPAG does acknowledge that suppliers' social tariffs and programs have made progress, but their offerings are still considered to be unclear and invisible to the many in need and also to the various agencies that assist fuel poor consumers. In addition, the gravity and risk posed in the current context compared to the relief on offer, is judged by FPAG to be inadequate.

5. Address concerns over unfair price differentials

- **5.1 A requirement for cost reflective payment differentials.** FPAG views the introduction of such a requirement as essential. In doing so the regulatory oversight would also facilitate the 'driver' that would appear to be missing in the suppliers businesses to reduce some costs. For example, are suppliers pre-payment costs being efficiently incurred as mentioned in the probe? From the limited analysis FPAG is able to undertake, the initial findings reveal a number of inconsistencies that should be explored by Ofgem. For example, one supplier charges over £45 for a lost Powerkey meter key, yet another supplier makes no charge at all. The cost to a supplier for a 'call out' to attend a pre-payment or credit meter issue reveals a range between £27 to £50 during 'callout period 1' and for 'period 2', a range of £47 to £250. Finally, there appears to be more than a 6 fold difference between the costs to a supplier of an electricity pre-payment transaction compared to its Gas equivalent. These wide variations and the implications for a customer when seeking to choose the best deal also reinforces the need for a simple kWh metric as already mentioned in 3.2. Turning now to the Northern Ireland, it would appear that the NI pre-payment solution does not incur these additional costs, and hence there is only a 1.5% tariff differential between pre-payment and direct debit.

- **5.2 Is a ban on undue price discrimination appropriate?** It is apparent from the structural market issues to do with suppliers' margins and the significant differentials revealed in charges incurred by some suppliers for pre-payment activity, that a mechanism to ensure customer equity is required. The evolution of the competitive market whereby suppliers appear to be sacrificing their gas margin in all areas and lesser electricity margins out of area creates an inequitable situation for non-gas customers in particular and latent electricity customers in general. Whilst FPAG recognises that 'in area' legacy gas customers do have the opportunity to take up a dual fuel deal, there remains for many vulnerable customers their inability to do so and for a range of reasons. These customers must be protected from this unforeseen structural issue that has been allowed to develop. With regard to an appropriate mechanism, a return to price controls would seem initially as undesirable. A lesser step would be to require suppliers to harmonise their 'in and out of area' prices over and agreed period and for a relationship parameter between electricity prices of different products to be developed. Meanwhile, FPAG is interested to understand the impact a correction to the market would create following the recent and seismic increases in suppliers' prices.