

**Minutes of a Special Meeting of the  
Gas and Electricity Markets Authority  
Thursday, 5 March 2009 at 12.30 pm  
9 Millbank, London SW1P 3GE**

**Introductory remarks by the Chairman**

1. The Chairman welcomed Members to a special meeting of the Authority which would be devoted, in the main, to issues arising from the Probe into retail energy supplies. Apologies for absence had been tendered by Robin Bidwell, Judith Hanratty, Miriam Greenwood and Michael Brocklehurst. There had been no declared conflicts of interest in respect of the agenda items.

**Report from the MD Networks**

2. The Authority considered two matters relating to independent gas and electricity network operators. A company had made a request to the Authority to be allowed to grant a floating charge to their funding banks over their network assets. The Authority decided that this would not be appropriate where this led to risk of interference with the Special Administration arrangements in place to protect customers in the event of the financial failure of a network company. Another company had written to the Authority seeking confirmation and guidance on matters relating to the overall regulatory framework governing the independent networks. The Authority discussed the matter and asked the MD networks to carry out some further analysis before responding to the company's request in detail.

**Direct Debit arrangements**

3. On this item, the Authority considered a further report, following its discussions at its February meeting, into suppliers' direct debit arrangements. The analyses of suppliers' arrangements and procedures had not been a straightforward matter given their generally opaque nature. However, the evidence did not show that direct debit payments were being systematically increased in order to advance cash flow by more than could be justified; or that there were widespread errors in the calculation of payments requested from individual customers. Price volatility, changing patterns of usage and the impact of estimated meter readings had to some degree magnified some of the difficulties of calculating new direct debit contributions and in their analysis.
4. The Authority, recognising these factors, concluded, however, based on the evidence presented, that the explanations given by suppliers to their customers were, in most cases, inadequate; and that they provided no firm basis for customers to understand how revised direct debit payments were arrived at. The proposals put forward by the Energy Retailers Association to develop self regulatory standards by way of a new Statement of Intent linked to the present billing code - to deal with some

of the communication issues - was not seen as an adequate response to the problems, nor one capable of effective enforcement. It had been suggested by the ERA that the focus would be on improved generic, rather than individual explanations to customers. The Authority agreed that there was a need to prescribe clearly what was expected of suppliers in informing their customers about direct debit arrangements and revised payments. Equally, since it may well prove necessary to carry through a number of licence changes to underpin improved communication, there would be merit in working up proposals for consultation, along with the key findings of Ofgem's investigation.

### **Probe: price differentials**

5. The Authority was presented with a paper proposing ways forward for addressing the concerns identified in the Probe into retail supply prices in respect of unfair price differentials. The Authority had taken a decision, in December 2008, to consider further the resolution of some of these issues through new licence conditions, leaving open the alternative approach of a reference to the Competition Commission. A consultation exercise, with an accompanying draft impact assessment, outlining four possible approaches on a collective licence modification, had recently been completed. The Authority was provided with the results of the consultation and the views of some 34 stakeholders, and a further draft of the impact assessment. The Authority also had before it a personal note prepared by Prof Yarrow commenting on the approach of addressing price differentials in the retail energy market through licence conditions.
6. Introducing the discussion, the Chief Executive provided an overview of the key issues and considerations before the Authority, and noted the views of some of the main energy companies. The Authority considered the pros and cons of action on approaches to a collective licence modification approach with conditions summarised as follows:
  - Option A: a requirement for cost-reflective pricing between payment methods (for example, the differentials between pre-payment tariffs and those for direct debit arrangements must reflect the underlying cost differences of these payment methods).
  - Option B: a prohibition on undue price discrimination (for example, the differential between pre-payment tariffs and DD tariffs, or in-area or out-of area tariffs must be objectively justifiable on cost or other grounds).
  - Option C: relative price controls (i.e. the approach of *ex ante* price controls).
  - Option D: a prohibition of cross subsidy of gas supply (such that the margins on electricity and gas supply would be required to be broadly similar).
7. The Authority also noted that there was a need in any event to clarify requirements under EU Directives (Annex A to Directives 2003/54/EC and 2003/55/EC) that differences in payment methods be cost reflective.

8. Having reviewed the issues and the consultation responses, the Authority rejected Option C since it was the most intrusive and would re-introduce a form of *ex ante* price regulation into retail energy markets and because there was almost no support from respondents, including some consumer groups. The proposals in option D which would control relative margins between gas and electricity supply were seen as disproportionate and potentially difficult to implement and were also rejected by the Authority.
9. There was extensive discussion and debate about the benefits and potential risks associated with the recommendation to pursue Option A and Option B. On Option A, the Authority noted the widespread support from consultation responses and concluded that the licence condition should be introduced to reflect the requirements under EU Directives (Annex A to Directives 2003/54/EC and 2003/55/EC).
10. On Option B the Authority acknowledged the clear benefits of the proposed condition to provide greater consumer protection by addressing a range of concerns that had been highlighted through the retail probe. There was discussion about whether the extent of price discrimination found by the Probe was materially different to those seen in other effectively competitive markets and whether the proposal could have unintended effects - such as reducing competitive intensity between suppliers, or raising average prices. The Authority concluded that the condition was necessary, appropriate and proportionate to protect customers' interests in the light of the Probe's findings and to give the other information remedies identified in the Probe - to improve the effectiveness of competition through greater customer engagement - sufficient time to work. The Authority therefore concluded that a "sunset clause" should be introduced such that the condition would cease to have effect after three years. One Member of the Authority did not support the conclusion on pursuing Option B because of the risk of unintended adverse effects on competition and on consumers.
11. Many respondents to the consultation referred to the importance of the enforcement guidelines and the drafting of the proposed licence conditions. As a result, the Authority agreed, as the next step, to consult on these specifically.
12. The Authority noted that, should it not be possible to agree a collective licence modification to give effect to the proposed prohibition on undue price differentials, a reference to the Competition Commission of either the specific licence amendment(s), or for a Market Investigation Review by the Commission, would remain as options.

### **Date of next meeting**

13. The Chairman confirmed the date of the next meeting as **19 March at 8.15 am.**

### **Those present**

The Lord Mogg, KCMG	(Chairman)
Alistair Buchanan	(Chief Executive)
Sarah Harrison	
David Harker	
Jim Keohane	
Jayne Scott	
Steve Smith	
Andrew Wright	
John Wybrew	
Prof George Yarrow	

### **Those attending**

Charles Gallagher	(all items )
David Ashbourne	( " )
Maxine Frerk	(Direct debit arrangements)
Dr Tony Burne	(Secretary to the Authority)