first:utility

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Dear Andrew

Addressing Unfair Price Differentials Consultation

Thank you for the opportunity to respond to the above consultation.

First Utility fully supports the principals identified in the Energy Supply Probe with regard to tariff price differentials. We believe that there needs to be greater transparency in the provision of optimum tariff and supplementary billing data that clearly disaggregate charges for customers.

The pricing strategy used by ex-incumbent suppliers is a major obstacle to a small supplier's ability to grow since it potentially allows an incumbent to sell at below cost to those customers that are most likely to switch. It's clear that subsidisation could occur when 75% of the profit earned by the big six suppliers is obtained from their ex-incumbent customers, which only account for, on average, 45% of their customer base.

We have deliberately not identified a preferred implementation model, as we believe that this is for Ofgem to agree directly with the suppliers affected. However we would urge Ofgem to build on the momentum for change that already exists in this area by making a swift decision that allows for rapid implementation. These decisions could have an immediate benefit to the in-area customers of ex-incumbent suppliers, as they would receive fairer and reflective tariffs, rather than potentially subsidising out of area growth.

There are a diminishing number of small independent suppliers and yet our input is critical if Ofgem is to achieve a balanced and effective set of remedies to address the shortcomings identified in the probe. First Utility welcomes the opportunity to work with Ofgem to help ensure that measures are introduced that will have the desired impacts and act in the benefit of customers and the market as a whole.

Please contact me if you require any further information, or if you believe we can be of further assistance.

Yours sincerely

Leyton Jones
Commercial and Regulation Manager

Addressing Unfair Price Differentials

Chapter 2

Q1 The Ofgem Energy Supply Probe report has exposed the way in which the incumbent suppliers offer better prices to those customers who are active switchers than they do to customers that are reluctant to switch. This allows for an effective cross-subsidy which permits sales to active switchers at, or below, cost and, thereby, represents a major barrier to new entrants who can only grow significant market share through the acquisition of customers prepared to switch supplier.
The unfair price differential should concentrate on customers in the PC1 & 2 categories, as domestic customers are most at risk from high prices due to apathy in switching, or misplaced loyalty to their incumbent supplier.
It's also vitally important that any mechanism agreed upon is easy to operate and manage. Otherwise it will become a pointless exercise to manage.

Q2 The extreme situation would be to provide a complete breakdown of all costs found in the unit and standing charge e.g. DUoS, wholesale energy, losses etc. However, this could possibly fall under the category of a laborious system for OFGEM to police and may not be the best route to take.

Bad debt (as an example) could be factored into the prices by customer category profile i.e. domestic, SME & HH; ensuring that domestic customers do not get apportioned with a debt incurred by commercial and industrial customers.
PPMIP costs should be recovered from this customer group, especially as these customers are not always obligated to have a pre-payment meter, but often chose this payment method from a budgeting standpoint. However, SMART meter roll-out to these customers could significantly reduce these costs and also allow customers using pre-payment as a budgetary option to have a real alternative, without the expense associated with PPMIP.

Q4 There's no point in having a proportionate materiality threshold, as this just allows suppliers to push the boundaries and slowly increase their prices/margins until told to stop. Based on agreeing the measuring of a breach, **any** breach should be penalised by the regulator.

Q5 Any enforcement should cover the retrospective changing of domestic tariffs as is allowed under clause 23.3 of the terms of the supply licences. Therefore, any mechanism has to allow for pricing changes which are backdated, as well as changes notified for the future.

Q6 Any proposals should only affect the six largest suppliers, as they are the incumbents with existing customer bases, which has historically, and continues to provide them with a major competitive advantage over any new suppliers in the market. 75% of the incumbent suppliers' profits come from customers located in-area, although this only equates to 45% of their customer base. This conclusively proves that incumbent customers are subsidising customer base growth outside of the supplier's historical DNO area(s). This has been proved recently by the loss of two of the larger independent suppliers in Bizz Energy and E4B.

Apathy or lack of understanding (especially among vulnerable groups such as the elderly) has led to customers remaining loyal to these incumbent suppliers. Therefore the groups most at risk of unfair pricing are the in-area customers of the incumbent supplier.
Smaller suppliers don't have the luxury of the incumbent customer base and therefore have to make additional margin to sustain the business during the formative months and years. To compete, smaller suppliers frequently offer more innovative services, often at a premium, so they should be able to offer contracts to reflect additional costs. Asking small suppliers to adhere to a set of fiscal rules when pricing would seriously diminish

their ability to compete with the larger suppliers and add yet another barrier to entry for new suppliers. The energy market needs new entrants and new entrants will only emerge if they have a reasonable prospect of achieving profitable growth.

Q7 Yes, but this should be dependent on a review of whether any changes have stimulated serious competition from smaller suppliers and allowed new entrants to come into the market.

Chapter 3

Proposal A

Q2 PPM charges should be capped at a fixed % above the standard rate. This should be shown as an additional extra charge on the bill (full disaggregation of difference in charges between standard and PPM tariff).

Proposal B

Q3 Any discounts based on payment should be shown as an additional line on a bill and should not be reflected in the units rates/standing charge.

Q4 Switching sites should be made to show comparisons based on the unit and standing charge and also a separate comparison to include any payment and dual fuel discounts.

Q5 Any discounts for dual fuel should be shown separately to allow complete transparency between a single fuel and dual fuel offering, as any discounts would be shown separately. Competition in the market will then deal with the cross subsidy issues, as customers will have clear transparency of single and dual fuel offerings.

Proposal C

Q6 It would be very difficult to set a 'benchmark' for the relative price control, as it would entail knowing the exact make-up of the units.

Q7
- i) in-area versus out of area
- ii) dual fuel versus single fuel
- iii) direct debit versus credit payment

Q8 Benchmarks would be better defined by area, as the make-up of the tariff DUoS, TNUoS & losses can differ to a material level between areas.

Proposal D

Q13 Stop dual fuel discounts! Why are dual fuel discounts offered? Apart from the ability to collect 2 reads in one visit there are no other synergies, as the majority of suppliers provide separate bills (no consolidated billing) and use different call centres; therefore no common system.

Q14 Under the current regime where many dual fuel discounts are applied as lump sums or percentage rates on the total bill, how would OFGEM know that a cross subsidy had occurred?

Q15 Yes, the advent of Smart metering will see electricity meters become a more important piece of hardware than the gas meter, as they will be used to transmit reads back to the office. It may therefore become important to retain the electricity meter and there would then be an incentive on the supplier to provide preferential rates on this supply as opposed to the gas one.

Appendix 2:

Q1 A proposal, or a combination of proposals, needs to reflect proportionate regulatory effort and careful consideration is required when agreeing what information is going to be required from suppliers. If the proposal is too onerous it will be easy for suppliers to extend the time it takes to collate information, or refuse to provide data based on the sensitive nature of hedging strategies.

Q2 Regulation will not only be beneficial for vulnerable customers in society, but also all in-area customers who believe they have shown loyalty to their incumbent suppliers by continuing to receive their electricity and gas from them. For these customers, regulation would see a reduction in charges to reflect the costs incurred by the incumbent suppliers. The loyalty shown by these customers would then be repaid in the form of fairer and reflective charges, as they're currently subsidising the acquisition of out of area customers on cheaper tariffs.

Q3 Any transparency of charges can only aid competition, as it will provide the customer with all the information required to make an informed decision regarding their choice of supplier. However, smaller suppliers need to be protected to ensure that they are given the opportunity to provide further competition to the six large suppliers and provide additional alternatives to customers. It's currently clear that the pricing strategies of the incumbent suppliers make it impossible for smaller suppliers to undercut their prices, even though they have significantly cheaper costs to serve.

There desperately needs to be a real number of alternatives to the big six to truly allow competition to work in the energy markets. Without new and innovative companies we will still be discussing issues of this nature in another five years, whilst customers continue to be disenchanted and frustrated by poor service and unreflective prices from their suppliers. Any onerous regulation of smaller suppliers would have an adverse affect on this aspiration and the ability to have a truly competitive energy market. If businesses such as first:utility are allowed to blossom then the competitive dynamic in the market will ensure that these benefits will quickly become available to all customers and transformational change will have been achieved. We believe that this is a goal that policy makers should be striving to achieve.

Q6 If wholesale regulation is mandated for all suppliers then this could inhibit competition further, as it will have an adverse affect on smaller suppliers relative to the big six. It may inhibit new entrants into the marketplace, as they would be restricted in the setting of their tariffs and the choice to customers. This would severely limit any growth for the current small suppliers and limit future new alternatives to the current major suppliers.