

ADDRESSING UNFAIR PRICE DIFFERENTIALS - an Ofgem Consultation

OVERALL VIEWS OF NATIONAL RIGHT TO FUEL CAMPAIGN

1. NRFC welcomes the opportunity to respond to this consultation document. There are several issues we would like to highlight here with regard to the issues that have been raised. Our comments are driven first by what we consider most likely to provide consumer protection, particularly for low income and vulnerable consumers. Issues relating to competition are of secondary concern since experience shows that it has not been an effective means of delivering consumer protection.
2. First, in terms of the regulatory options that have been raised given the information available from the consultation document and within the partial impact assessment, it was difficult to choose which option was likely to protect the interests of consumers most effectively. NRFC believes that an enhanced option C – the imposition of relative price controls with an independently assessed and audited baseline tariff to ensure cost reflectively is the best means of consumer protection. This option would require substantial commitment from Ofgem and will require it to be proactive in its monitoring of suppliers. We are concerned by the notion of actively building in headroom at a time when there is even less likelihood of new entry than there has been for the past 10 years. We also believe that option B would be an effective means of protecting consumers from unfair price differentials.
3. Second we have a significant concern regarding Ofgem’s approach to sunset clauses within licence conditions. It is our strong view that the general approach should be that a case should be made for their removal rather than their retention.
4. Third we are worried that Ofgem’s view that it will only take action for breaches that are “substantial, extensive and persistent” provides a very low compliance threshold for companies and provides little incentive take this issue seriously. We are surprised that Ofgem would give this message to companies and it clearly undermines its commitment to consumers.

CHAPTER 2

Question 1 – in proposing action, are the overall aims set out appropriate? Are there other issues we should focus on in taking a decision on the best way to proceed in this matter?

5. Ofgem’s overall aims focus too heavily on the “development of competition” as the end in question rather than the protection of consumers. It may be the case that Ofgem’s statutory duty is to “protect the interests of consumers...wherever appropriate by promoting effective competition”. After 12 years of competition it is still not effective and it is increasingly apparent that it is not the appropriate means of protecting consumers.

Question 2 – what is the appropriate approach to cost allocation?

6. We accept that Ofgem’s general approach to cost allocation is appropriate as set out in paragraph 2.5. Our issue is with compliance with the approach, particularly in terms of the non-directly attributable costs. While Ofgem is concerned with avoiding a compliance burden, it will be necessary for it to be proactive in understanding the policies and practices of companies in this regard, so as to protect the interests of consumers by ensuring that costs are being allocated fairly.

7. NRFC believes that in the first instance it is important to assess whether or not the proposed costs of bad debt are sufficiently efficient before considering how the costs should be allocated. It is clear also that there should be different approaches for debt incurred by credit consumers who do not have a prepayment meter installed and those consumers that go on to have a prepayment meter installed (whose debt recovery costs we believe will be lower) We also believe that where debt has been incurred as a consequence of hardship or through vulnerability there is little to be gained by increasing the costs of those consumers through higher prices.

Question 3 – are social or environmental issues appropriate to consider in relation to objective justification? How might these exceptions be captured in either licence conditions or guidelines?

8. It is appropriate to consider social issues as an objective justification for price discrimination. However NRFC believes that mandatory guidance as to the detail should be provided by Government under its requirement to provide social and environmental guidance to Ofgem. We recognise that this may require an amendment to primary legislation. Once this was in place we would expect Government to issue Regulations and that suppliers would have a licence requirement to comply with the regulations (the comparison being with CERT requirements)

Question 4 – would it be beneficial to give clear indication of materiality thresholds either on the face of any licence conditions or in guidance?

9. NRFC believes that Ofgem should not at this stage give indication of materiality thresholds to suppliers. The notion of materiality can also be described as approval for price discrimination up to the level outlined in the thresholds. It may be the case that Ofgem wishes to consider issues of proportionality in relation to the regulatory burden placed on suppliers by companies however NRFC strongly believes that the fact that this additional regulation has been required as a consequence of the market failures identified in the probe should mean that no view is given on materiality to suppliers.
10. We are exceptionally concerned with Ofgem's view that breaches need to be "substantial, extensive and persistent" to warrant action by Ofgem. It is difficult to imagine then the circumstances in which Ofgem will take any action at all.

Question 5 – Would it be beneficial to introduce a new enforcement process? If so, should this process be of the form set out in this document? Are there any other considerations in relation to the detail of how such arrangements might work?

11. NRFC believes that it would be beneficial to introduce the new compliance process as long as it is embedded in the conventional compliance and enforcement process. It would be wholly inappropriate for example if Ofgem were to issue a "notice of objection" only to then have to pursue the company through a separate enforcement process to be able to levy a fine for a breach or non-compliance. The process will also need to be able to provide speedy resolution otherwise there would be no benefit from the additional burden of this process –either in terms of regulatory certainty, consumer confidence and ensure that detriment is suffered no longer than is absolutely necessary. NRFC believes that it would be appropriate for other agencies to bring potential cases to Ofgem in this regard using their super complainant status for example.

Question 6 – should the proposals for licence requirements set out in this document apply to all suppliers active in the market for domestic consumers or only to a subset of these suppliers, such as the big six?

12. NRFC believes that licence requirements should apply to all suppliers of domestic consumers.

Question 7 – Would a sunset clause be appropriate for any licence conditions? What would be a suitable time period before any review of the market?

13. We believe that in certain circumstances sunset clauses are an appropriate regulatory tool. However experience of their use is chequered. NRFC is concerned to see in this consultation the view from Ofgem that as a matter of principle a case should be made for the retention of licence conditions. We believe that, given the experience of competition in the domestic market, this is wholly inappropriate and it should be that a case be made for the removal of licence conditions. Any case should be made based on clear and transparent indicators of the success or otherwise of competition and its ability to protect the consumer interest better than regulation.
14. We believe that there could be no case for reviewing whether or not a case could be made for the removal of licence conditions before they have been in place for 4 years. This would allow for 1 year start up, 2 years in place and 1 year for review.

CHAPTER 3

15. The following section sets out our views on the different proposals and addresses some but not all of Ofgem's questions. Our comments are driven first by what we consider most likely to provide consumer protection, particularly for low income and vulnerable consumers. Issues relating to competition are of secondary concern since experience suggests that it is not a particularly effective means of delivering consumer protection.
16. **Option A** appears to involve the least intervention and would therefore provide the greatest regulatory certainty and have least impact on innovation of the 4 proposals. However it only relates to payment methods and would not include in/out area and online tariffs. Consequentially NRFC does not believe that this option will provide the greatest level of consumer protection.

Option B is about preventing undue discrimination and so is much wider than the first option. NRFC shares the view given by Ofgem that this proposal has greater regulatory risk than option A because it will be open to significant variation of views and interpretations. While Ofgem may issue guidance as a means of alleviating risk, in practice it can be seen as a starting off point for bright pricing analysts and regulatory advisers in companies to find loop holes.

Option C would provide for the reintroduction of relative price. This option would appear to provide similar consumer protection as option b in that it determines clearly what the price differentials can be from one tariff to another. An additional benefit of this form of action will be the contribution it will make to improved customer communication since consumers will clearly understand the difference between one form of payment method (or locational price) and another. This option also requires a substantial commitment from Ofgem and will require it to be proactive in monitoring suppliers' tariffs.

17. NRFC believe that this option would help improve customer communication, certainly within a supplier's offerings.
18. NRFC has difficulty reconciling the discussion of cost reflectivity, undue discrimination and relative price controls with the notion of the provision of "headroom" to encourage new entrance. This would seem to encourage suppliers to charge more either more than their costs or more than a reasonable profit. This is another example where competition is promoted more as an end in itself than as a means of delivering consumer protection which it has failed to deliver over the past 12 years during which time there has been no significant new entrance into the domestic energy market.
19. **Option D** is preventing cross subsidy between gas and electricity. Given the evidence from the probe, this appears to be a sensible proposal.

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