



**Consumer
Focus**
Campaigning for a fair deal

Consumer Focus response Ofgem consultation on Promoting Smarter Energy Markets

March 2012

About Consumer Focus

Consumer Focus is the statutory consumer champion for England, Wales, Scotland and (for postal consumers) Northern Ireland.

We operate across the whole of the economy, persuading businesses, public services and policy makers to put consumers at the heart of what they do.

Consumer Focus tackles the issues that matter to consumers, and aims to give people a stronger voice. We don't just draw attention to problems – we work with consumers and with a range of organisations to champion creative solutions that make a difference to consumers' lives.

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Promoting Smarter Energy Markets consultation

Consumer Focus welcomes the opportunity to respond to this consultation on 'Promoting Smarter Energy Markets'. We believe that smart metering has the potential to radically change the energy market and customers' experience and engagement with it. It is appropriate that Ofgem is proactive in taking steps to not only protect customers, especially the most vulnerable, but also to promote their interests by developing a regulatory environment which maximises the benefits to consumers.

Outlined below are our initial high level thoughts on the strategy to shape market development from the platform of smart metering. We are supportive of the development of an implementation plan for reforms and look forward to continuing to work with Ofgem as this work progresses. As part of this process we urge the regulator to actively seek the views of the widest possible range of stakeholders. We have had some concerns to date that the views of potential new entrants in the energy products, services and data markets have been under represented in wider discussions on smart metering. It is important that the incumbent energy players are not given a competitive advantage in these emerging markets if the consumer benefits are to be fully realised.

Consumer Focus expects to see increasing convergence of different retail sectors in the future. The introduction of Green Deal has the potential to further facilitate this. Customers are likely to be offered services that combine energy supply with energy efficiency, micro-generation, home security, water efficiency, in-home displays, and telecommunications for example. At present regulatory responsibility for these areas sits across a number of bodies. If the needs of customers are to be properly represented in a smarter world, it will be essential for Ofgem to proactively work with Ofcom, Ofwat, and the Office of Fair Trading (or its equivalent) in particular. The recent creation of the Energy Efficiency Deployment Office is a reflection of the growing recognition of the need for a more joined up approach in policy making in the area of sustainability. We hope that as part of its strategy for promoting smarter markets, Ofgem will take the lead in bringing together the different regulators and their approaches, to identify gaps, areas of inconsistency and where a joint approach could be of benefit. This is particularly important regarding sales and marketing, consumer redress, complaint handling, and financial transparency and accountability.

Our response focuses on domestic consumers, but we are mindful that much more work is needed to engage with and understand the needs of small businesses in this changing world. We hope that Ofgem will take this forward.

Historically, the competitive market has not always been effective in meeting the needs of vulnerable and low income consumers who may be a high debt risk, and have limited purchasing power. It is therefore particularly important that Ofgem ensures that this group of customers is protected and benefits from the introduction of smart metering. We strongly support the commitment to carry out a distributional analysis of the impact of time of use tariffs but this should to be extended to include demand response in the widest sense, including critical peak pricing, automation and seasonal tariffs. Linked to the latter, the distributional impact of moving to more cost reflective pricing and potentially more localised charging also needs to be fully understood before regulatory changes are made.

To date, little work has been carried out on the potential *benefits* to low income customers of new technologies. We would urge Ofgem to carry out research in this area to actively identify opportunities. For example, could load limiting enable the provision of a life line of electricity to prepayment meter customers as an alternative to self-disconnection? Will suppliers be better placed to monitor self-disconnection and target social assistance at those most in need? Are key decisions being made on the Home Area Network likely to preclude or restrict innovation in the provision of remote health care services? What regulatory arrangements are needed in this area to facilitate competition? Suppliers have a number of environmental and social obligations that have developed in an ad hoc, piecemeal way. Consumer Focus continues to believe that these could be delivered much more efficiently and cost effectively with a more joined up approach and greater use of data matching. We strongly urge Ofgem, as part of its strategy for promoting smarter markets, to review the regulatory framework around social and environmental obligations to see how suppliers might tackle fuel poverty and help vulnerable consumers in a smarter way.

Collective switching

Consumer Focus believes that collective switching initiatives may represent an opportunity to increase consumer engagement. We have initiated a dialogue with a service – iChoosr – that has successfully developed and rolled out a collective switching model in Belgium, Netherlands and Germany. It offers a platform that sits behind trusted community and civil society organisations as well as local authorities who act as the consumer-facing element of the service to tackle lack of trust and therefore engagement in the market. Consumer Focus has facilitated a meeting between iChoosr and a range of GB organisations and local authorities interested in rolling out this model. We are happy to meet with Ofgem to discuss the regulatory implications of these kinds of initiatives.

Enabling retail market development

Question 1: Do you agree with the propositions set out in this Chapter.

Question 2: For each proposition, have we identified the elements of the current market arrangements that could help or constrain the realisation of benefits to consumers?

Question 3: For each proposition, have we identified the range of issues, such as timescales for any changes to market arrangements?

Question 4: Are there additional opportunities for the development in retail energy markets that we should include in the scope of our work?

Time of use tariffs

Proposition 1: Time of use (TOU) tariffs should help many customers lower their energy costs, but improved engagement will be needed to help all consumers make informed choices.

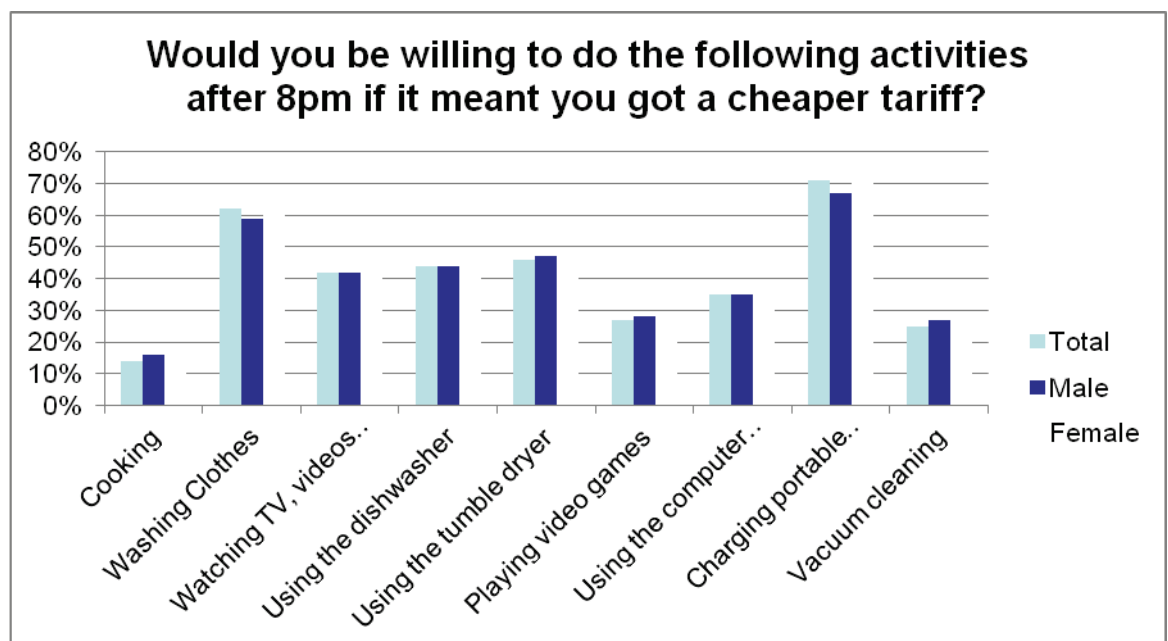
- We agree that some consumers may be able to benefit from relatively lower cost energy if they are able to use their electricity at off-peak times.

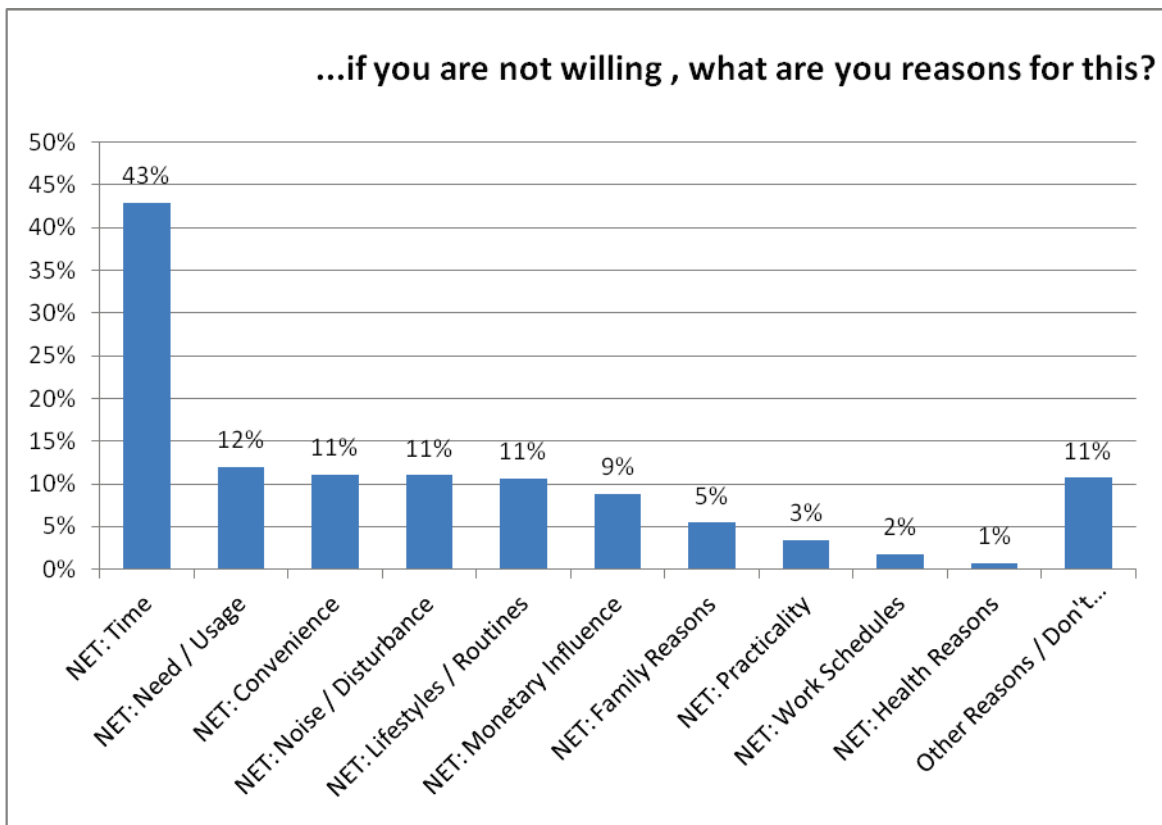
- More work is needed to understand who the winners and losers of these new deals will be, and to quantify the impact and benefits of this. DECC's latest impact assessment on smart metering recognises that '*Bill savings for some customers may be offset by bill increases for other customers as the cross subsidy unwinds*'¹. As a result, TOU is now listed as an industry, rather than a consumer, benefit.
- The assumption is that shifting consumption to off peak times can benefit all customers indirectly by helping to lower the costs of generating and transporting electricity. We query how cost savings will be passed on to consumers and what mechanisms will ensure this is delivered. Given that Ofgem's own research into the subject suggests that 40-60 per cent of customers are 'sticky' and have never switched suppliers, there may be insufficient incentives for suppliers to pass on these cost savings to all of their customers. Rather, suppliers may well only pass on the cost savings to those customers who are engaged enough either to be able to change their usage pattern, or to switch supplier if they see a better deal elsewhere.
- We welcome the recognition that new tariffs could create further market complexity, potentially making it harder for consumers to find the best deal for them. We do not believe that the Retail Market Review proposals will address barriers to consumer engagement with regards to demand response and time of use. The proposed recommendations to simplify tariffs could just result in customers on the proposed new simple deals, also in practice being on the most expensive tariffs. In particular, more work is needed on tariff design. We advocate for a limited number of time bands, so that customers are able to compare TOU tariffs on a like for like basis. For example, if one TOU deal classifies 'off peak' as 9.30am to 12pm, and a different TOU deal classifies 'off peak' as 10am to 1pm, it would make it very hard to compare.
- The National Audit Office report on smart metering suggests that low income customers in particular may not be able to engage in the market to be able to access the cheaper deals which smart will facilitate². This could result in the costs and benefits being unevenly distributed. We share this concern.
- We agree that not all consumers are likely to be *able* to take advantage of these deals eg those whose consumption coincides with higher cost, peak times. In Victoria, Australia concerns have been raised that certain groups of consumers such as low income working families would not be able to use their energy at off-peak times and have little discretionary load. There is therefore a risk that some customers who are unable to shift their usage will be paying significantly more.
- We welcome Ofgem's commitment to carry out a distributional impact assessment of TOU – this is an important piece of work. There has been much debate about the impact of these kinds of offers on low income and vulnerable consumers. It has been asserted that low income customers have flatter load profiles so are more likely to benefit from TOU. In practice it will depend on the type of customer and the tariff structure. Fuel poor consumers are not a homogenous group. The analysis will need to carry out detailed segmentation to be meaningful. This should include the impact on different payment types, social group, age and income groups, household types, fuel type and different regions. We seek clarification on the timescale for carrying this out – it is long overdue.

¹ DECC Impact Assessment: Smart meter rollout for the domestic sector (August 2011), page 55

² National Audit Office report on 'DECC Preparations for the roll-out of smart meters', June 2011, <http://bit.ly/uVXXvM>

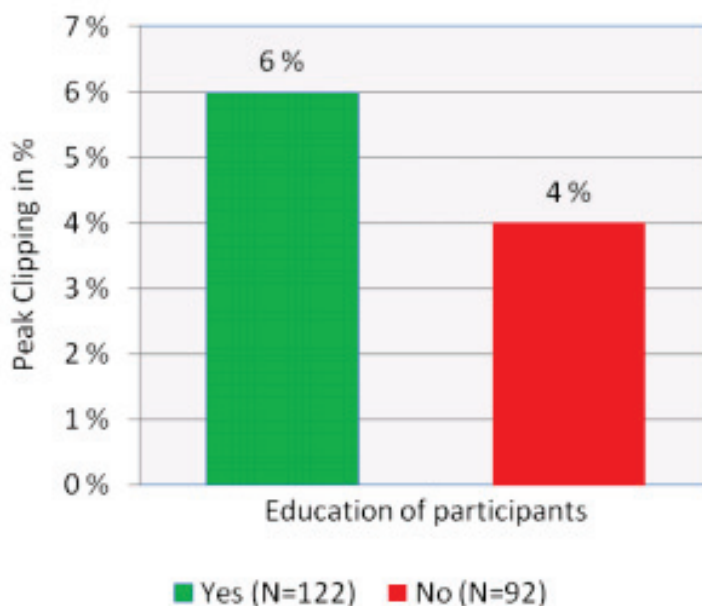
- Consumer Focus is currently carrying out qualitative and quantitative research into the experience of existing customers on basic TOU tariffs (such as Economy 7). We hope that this can inform decisions. This will be published in the early summer.
- More work needed to understand the potential for gas TOU in the GB context.
- Research is needed around customer willingness to shift load and their ability to do so.
- Further consumer protections will be needed. Consideration should be given to requiring suppliers to provide customers with projected energy costs in the same way they do with mortgage advice before selling them the deal. The customer could then be given projected costs based on their existing usage profile, examples of savings if lifestyle changes are made and customers switch to off-peak at key times. This should be based on actual consumption patterns over a number of seasons including the winter.
- There is likely to be an increase in long-term contracts as suppliers bundle supply with products such as in-home displays (IHDs), where they recoup the costs of the product over time. Ofcom has reportedly taken action to restrict contract length with regards to mobile phones, because of the negative impact on competition. Ofgem should make clear its expectations in this regard in advance.
- There is a risk that standard IHDs will not meet the needs of TOU customers. This should be addressed in the minimum specification. We recommend that Ofgem carries out work to understand the information needs of TOU customers and how these can best be met.
- More work is needed on consumer interest in and acceptance of different types of demand side response propositions. Our March 2010 online survey (Base 2,048) found some interest in shifting load, if customers were given a price incentive but also potential barriers to engagement (see below).





- The VaasaEET/ESMIG ‘Empower Demand Study’³ (2011) found that participant education was an important factor in ensuring that customers got maximum benefit from their time of use tariff. More work will be needed in this area and ensuring that pricing is fair and transparent.

Figure 25 : Influence of education on peak clipping in TOU trials



³ <http://bit.ly/wkDOIN>

Demand-side response

Proposition 2: More efficient use of demand-side response can lower overall energy costs, but this will need co-ordinated changes to regulatory and commercial arrangements

- We agree with the proposition. To facilitate demand-side response (DSR), changes to the regulatory and commercial arrangements will be needed. As noted, different parties are interested in using different types of DSR and their interests may not always be aligned. Similarly one party's use of DSR can have knock on impacts for other parties throughout the system. We would welcome flexibility in arrangements to allow networks and third parties to offer DSR to open up competition and help engage customers.
- We recognise that international evidence in particular suggests that customers responding to price signals can result in peak load shift and overall energy reduction. But, before facilitating DSR, Ofgem should be clear of the potential for load shifting in the GB context, and fully understand the distributional impact and benefits, and what protections will need to be put in place. We recommend Ofgem carries out a detailed impact assessment including analysis of the potential for demand response. This will help inform decisions on the regulatory framework.
- We anticipate that in addition to TOU tariffs where the customer is charged a different amount depending on when during the day or week they use energy, there could also be seasonal tariffs, dynamic pricing (critical peak pricing, off peak rebates) and automation (direct load control or remote control of appliances within the home). Each of these propositions poses new risks to consumers that need to be addressed with new consumer protections. For example new regulation may be needed around what are fair terms and conditions. Will there be penalties if the customer overrides direct load control? How will customers get a reliable signal for critical peak pricing (CPP)? What are appropriate number and lengths of CPP periods?
- As with TOU more research is needed on customer attitudes towards new offers and whether unlimited innovation should be permitted. The Irish TOU trial found that tariffs that were more expensive in winter were unacceptable to customers. Customers were also not interested in automation where they were penalised if they chose to over-ride the remote control.
- The same issues for TOU identified above also apply with regard to consumer engagement, distributional impact and distribution and passing on of cost savings.
- More work is needed to explore the potential for automation. Automation could result in savings without customers having to change their lifestyle on an on-going basis. Lower customer involvement is required than TOU – the customer only needs to sign up to the deal and purchase or have installed the appliance. There is also an element of choice, as the customer could select which appliances react to price signals which may appeal to some consumers. We would welcome Ofgem carrying out further research in this area. This kind of DSR also provides greater certainty for industry as it enables an immediate response as needed. However, we have concerns that key decisions on the home area network (HAN) and wide area network (WAN) solutions could impede competition in this area by precluding market entrants (see below).
- The Empower Demand report suggested that automation with dynamic pricing 'can double or even quadruple the amount of load shift' with potential to increase the amount that customers save on electricity bills.

However, further consideration will be needed as to whether Critical Peak Pricing should be permitted given the increased risks to consumers and the regulatory changes that would be needed to facilitate this.

- Ofgem should review existing demand programmes to establish lessons learnt, and be cautious of international comparisons.
- We urge the regulator to use the Low Carbon Network Fund projects to gain learning about the customer experience of different demand response propositions and what is needed to help consumers engage. To date the focus has been on the network needs. The opportunity to understand the consumer experience should not be missed.
- The assumption is that smart metering will remove a key technological barrier to DSR by recording half hourly data, thanks to two-way communication and load switching. While the minimum specification for Smart Metering Equipment Technical Specification (SMETS) 2 is expected to include this functionality, we are unclear if this is the case for SMETS 1 or other advanced meters that are currently being introduced and may not have to be replaced. This could mean that some consumers are not technically able to access these deals because of the type of 'smart meter' they had installed. We are seeking clarification from DECC as to the minimum functionality of exempt meters, and the potential numbers of households that could be impacted. We hope that Ofgem is actively engaged in this debate to ensure the minimum functionality is fit for purpose. This issue could not only have an impact on the individual's access to DSR, but also on the potential savings that could be achieved an aggregate level.

Energy services

Proposition 3: Innovation in energy services would increase the consumer benefits of smart metering and can happen without major changes in the regulatory framework.

- We disagree with the proposition. While we recognise that innovation in energy services could provide consumer benefits, we strongly believe that regulatory changes will be needed to facilitate this. This includes energy sector specific regulation around data access and use⁴ and requirements to ensure that third party products and services can easily use the HAN selected by suppliers.
- The Smart Energy Code (SEC) and BIS MiData proposals must also be developed in a way that not only protects consumers but maximises competition and consumer benefits. We have concerns that decisions are not on track to facilitate this, eg it is not currently proposed that personal data inventories will be machine readable.
- As mentioned, new protections will also be needed to prevent customers suffering detriment due to bundled propositions and longer-term contracts. While Ofgem does not regulate the provision of energy services directly, it will need to work with those regulators that have responsibility to ensure that customers are safeguarded and that there is a joined-up approach.
- Consumer Focus believes that the rollout of smart metering could help improve competition, encouraging new entrants into the market, as opportunities arise for companies to compete not only on price of supply, but also a more diverse range of smart and energy efficiency products and services. Accenture research indicates that 68 per cent of UK customers would consider purchasing their electricity, energy-efficiency products/and or related services from general

⁴ <http://bit.ly/xrljLu>

retailers, phone companies, cable providers or online sites⁵. Younger people in particular were more likely to consider alternatives to their utility company to supply their electricity.

- Encouraging non-utilities into the energy services market is also arguably particularly welcome as research has consistently shown low levels of trust in energy suppliers. Consumer Focus research for example found that only 26 per cent of customers trusted their electricity supplier to help them save money on their energy bills and go green, with confidence in gas companies even lower at 23 per cent⁶. This compared to 31 per cent of customers trusting online price comparison sites. Similarly Accenture's 2011 research found that only 16 percent of UK customers trust their utility to inform them about actions they can take to optimise their electricity consumption, down from 17 per cent the previous year. There may therefore be particular advantages, in terms of consumer engagement and behaviour change from encouraging new entrants into this emerging market. Given that £4.6 billion⁷ of the customer benefits from smart metering are meant to come from consumers using smart data to reduce their energy consumption, this is significant.
- We agree that increased uptake of energy products and services has the potential to improve engagement in the wider energy supply market. We welcome the recognition that bundling of energy services with energy supply contracts will impact the way the supply market operates and that new consumer protections will be required. In particular, as mentioned, the need for up-front investment could deter take up of some energy services, such as home automation. Vulnerable customers in particular may be unable or reluctant to find these costs. There is the risk that disengaged consumers will not achieve the same benefits and that developments in the energy services market could widen the difference in outcomes for engaged and disengaged consumers.
- We do not have confidence that Green Deal will address financial barriers to taking up energy efficiency improvements.⁸
- It is unclear if customers will have to pay to access data that could benefit them, and if so at what level of detail. Consumer Focus's investigation into the small business market found that microbusinesses were charged to access to their own energy consumption data – in one instance, 52p a day for data via an online portal – and therefore face barriers to accessing the energy efficiency benefits of smart metering. We think this is unacceptable.
- More work is needed to ensure that consumers can compare smart deals on a like for like basis to ensure they can access the best deal for them. We do not believe that the Retail Market Review sufficiently addresses these concerns. Our full position is outlined in our consultation response.⁹
- As noted, further consideration is needed as to how switching sites will accommodate TOU tariffs and bundled services and how this is reflected in the Confidence Code.
- Under DECC's original proposals third parties would potentially have access to data via three routes: the Data Communications Company (DCC), via the customer physically contacting them with information (eg web, telephone, letter, face to face), or via a bridging device direct from the smart metering system.

⁵ Revealing the values of the New Energy Consumer. Accenture end-consumer observatory on electricity management 2011. P.11

⁶ Ibid P.14

⁷ DECC Impact Assessment: smart meter rollout for the domestic sector (August 2011)

⁸ For more information on Consumer Focus' work on the Green Deal, including our detailed policy positions, please go to: <http://bit.ly/w27DZu>

⁹ <http://bit.ly/xtA0Pc>

All of these require some initial action and engagement by the consumer which immediately puts the third party at a disadvantage. How much of a disadvantage will depend on how easy and fast the process is via each of these routes. The greater the number of steps needed by the customer, the greater the disadvantage to the third party; the slower and more onerous the process the customer has to go through to get what they want (whether a quote for a better tariff or on-going energy efficiency advice) the greater the chance the customer will lose interest and disengage along the way. Certainly if the customer has to purchase a bridging device upfront this will act as a barrier to engaging in that service.

- We have special concerns about access to data pre-DCC. In order for the customer to switch to a basic tariff, for example, they can access the key information they need about their overall energy consumption from their annual statement, bill or even their IHD if they have one. They can acquire price comparison sheets from Consumer Direct, call a switching site or go online. But for more complex tariffs, such as TOU, more detailed data will be required. As we understand it, at present, the customer would have to go via their supplier for this kind of information. Experience in the mobile phone market highlights that where the incumbent provider is the data controller this can act as a barrier to competition. Ofcom introduced new regulation as they found that the customer needing to go to the incumbent for their Porting Authorisation Code (PAC) before they switched resulted in mobile companies reserving their best deals for customers about to leave, and stalling on the provision of information the customer needed to switch, so they gave up moving provider.
- Contrary to the vision outlined, it is now also uncertain if some customers will be able access their energy data locally at all even post-DCC. Recent Government proposals for exemption may mean that not all 'smart meters' are required to store 13 months data in the meter. If this is the case, some customers may not have local access to more than a few months energy information that they can access themselves or share with third parties. This is a real concern and could effectively kill competition in the energy services market. We hope that these issues will be addressed. We strongly urge the Smarter Markets team to get more actively involved in this debate and discussions around MiData to ensure that the benefits are realised.
- We also have concerns that suppliers will select in-home communications solutions that could result in technical barriers to new entrants that use data or the HAN. For example we understand that the frequency and protocols around ZigBee are such that product innovation around the home area network (HAN) could be limited, as appliances such as iPhones and HTC phones do not contain ZigBee chips.
- Third parties will also need to be accredited to protect consumers from cowboy operators. Any third party accessing data via the DCC will need to sign up to the Smart Energy Code (SEC), but it is unclear what safeguards will be in place for other parties. Requirements around the SEC should not be unduly onerous for small companies and new entrants. It is particularly important that the governance arrangements around the DCC do not favour incumbent utilities' interests.
- Energy suppliers already have an unfair competitive advantage in the energy products market, given their obligations under the Carbon Emissions Reduction Target and the upcoming Energy Company Obligation. The proposal to allow suppliers to be able to sell during the face to face visit will further exacerbate this.
- Potential third party service providers report that in order to provide energy efficiency products and services in particular, you need economies of scale, ie

hundreds of thousands if not millions of customers. Suppliers already have this advantage because they have a ready-made large customer base, while any third party would need to gain customers or enter into partnerships. Indeed while arguably not serious commercial propositions, the challenges of third party entrance are perhaps illustrated by Google's withdrawal of its PowerMeter¹⁰ and the discontinuation of the Microsoft Hohm service¹¹. Both of these aimed to help consumers to better manage their energy use and both reportedly were withdrawn because lack of scale, ie not enough consumers subscribed to their services.

- Given the challenges therefore and the potential benefits in terms of product innovation, lower costs, greater choice and improved customer service that could stem from effective competition, it is essential that every effort is made to ensure a level playing field in terms of data access and use. Consumer Focus does not therefore support suppliers having default access to half hourly or more detailed data (appliance level data, real-time information) for value added services including tariff propositions, energy efficiency services, as well as smart products and home appliances. This would give incumbents a further unfair advantage. This should be reflected in sector specific regulation outlining regulated duties.

Payment methods

Proposition 4: Consumers will have more payment options, without changes to regulatory arrangements beyond those that are envisaged as part of the smart meter rollout.

- We are unclear about this at present. We hope that smart metering will facilitate consumers getting access to a greater range of top-up options – over the phone, via the internet, at a cash point – which will provide greater choice and convenience. We are told that new technology will also enable customers to combine regular payments with ad hoc top-ups, but we are unclear to what extent this kind of innovation is smart dependent or can be done anyway.
- We believe that smart metering could provide a rare opportunity to help revolutionise the Pay As You Go (PAYG) energy market and remove historical barriers to competition in Great Britain. If no additional costs to serve are added (such as for separate displays or key pads), it should not only reduce the cost of prepayment tariffs but also help tackle barriers to consumer interest in this payment method. This is because in theory the customer's meter will no longer have to be exchanged if they move to, or from, prepayment. As mentioned consumers should also get access to a greater range of top-up options.
- Greater choice of PAYG energy products should also reduce the stigma associated with this payment method. All these factors in turn could open up the PAYG energy market and further drive down prices and improve customer service.¹²
- Consumer Focus has concerns that potential benefits for prepayment meter (PPM) customers are not on track to be realised. Few suppliers have conducted trials of smart prepayment and there is a risk that suppliers may leave PPM customers to the later stages of rollout. In practice, innovation in this market could be slow to develop without incentives or regulation.

¹⁰ <http://bit.ly/iq3LD8>

¹¹ The company reported that "The feedback from customers and partners has remained encouraging throughout Microsoft Hohm's beta period. However, due to the slow overall market adoption of the service, we are instead focusing our efforts on products and solutions more capable of supporting long-standing growth within this evolving market" <http://www.microsoft-hohm.com/>

¹² *Cutting back, cutting down, cutting off – Self-disconnection among prepayment meter users.* Consumer Focus, July 2010, <http://consumerfocus.org.uk/g/4lx>. Annex 4.

- Consumer Focus is working with Accenture to understand how we can best realise the consumer and industry benefits of smart prepayment and address barriers to rollout. We will be happy to share the findings with Ofgem in early summer.
- As noted, suppliers must be able to objectively justify price differentials between payment methods. In a smart world differential charging may arise within prepayment, depending on how the customer tops-up. For example, will it cost more to top up online than by cash? What difference will it make for customers who top up small amounts on a regular basis? There may be a role for Ofgem in ensuring that charging is fair and doesn't result in consumer detriment.
- We would also welcome clarity as to where the cost will fall of making prepayment safe and practicable in a smart world. For example the cost of hardwiring a display, adding a separate key pad or moving the meter to an accessible location. In the case of those struggling to pay their energy bills it would be particularly unacceptable for this cost to be borne by the individual customer as it could potentially push them into debt and add to their hardship. Any charge, particularly an up-front fee, may also discourage people from allowing the supplier to address the problem, potentially putting their health in danger if they are reliant on a supply of energy to stay well. This needs to be reflected somewhere in the protections.
- It is particularly important that PPM customers see wider benefits of smart metering as it is likely that these customers will not achieve the same energy savings as those on other payment types, yet they will still be required to foot the bill. DECC's impact assessment for example estimates that gas prepayment meter customers will achieve average savings of 0.5 per cent compared to 2 per cent for gas credit. It is therefore crucial that they get other benefits.
- At present DECC's proposed minimum standards for IHDs and smart meters do not adequately consider the needs of PPM customers. For example, as we understand it, on Quantum PPM meters, the consumer has to press a button over 30 times to access account information. In our qualitative research into attitudes toward prepayment¹³, none of those interviewed were aware that this information was available on their meter. These kinds of usability issues should be addressed.
- Low credit warnings could also be provided via the display – at present where a meter is located outside of the property, for example, in a basement, low credit warnings cannot be heard and it can be particularly difficult for customers to keep track of their energy use. This means they can unwittingly self-disconnect. This is not currently proposed.
- We welcome the Smart Metering Installation Code of Practice requiring all suppliers to provide information to consumers on how to top up their smart meters when operating in PPM mode, but more research is needed on the information needs of this group of customers more generally.
- Consumer Focus March 2010 survey indicated that at least a third of consumers would be interested in PAYG energy if the price was comparable with Direct Debit and it was easy to top-up.¹⁴

¹³ *Cutting back, cutting down, cutting off, Self-disconnection among prepayment meter users.* Consumer Focus, July 2010, <http://consumerfocus.org.uk/g/4lx>. Page 12. This is the biggest ever study of PPM energy customers. The study explored attitudes to this payment method, and the extent to which PPM customers self-ration or self-disconnect.

¹⁴ ICM online survey for Consumer Focus of 1,839 customers, March 2010. This indicated that at least a third of energy consumers may be interested in a pay-as-you-go energy tariff (as with mobile phones) if the price was competitive with Direct Debit and they could top up easily. Experience in Northern Ireland where semi-smart meters have been introduced suggests that pre-pay is the payment method of choice for many consumers. Around 30 per cent (230,000) of all

The Government's decision that all smart meters should have prepay installed as a standard feature would facilitate this. However, given recent proposals around SMETS 1 and exemptions, we are unclear what proportion of meters will now not have this functionality and the impact of that on both individual households and wider market innovation and competition.

- We welcomed the introduction of new protections around remote functionality. We are also monitoring the effectiveness of these.
- We are supportive of the proposed measures to facilitate commercial interoperability but it is clear that there will continue to be very real barriers to switching for customers with smart meters in prepayment mode/smart prepayment meters. We welcome Ofgem's commitment to monitor developments and introduce further protections if needed.
- Suppliers with more than 50,000 domestic customers have an obligation to offer choice of payment methods to customers. Ofgem should consider whether this should be extended to small suppliers to prevent customers being locked into prepayment where they have a smart meter installed by one of the smaller energy companies. The regulator should monitor customer experiences in this area.
- Smart metering is likely to facilitate the introduction of credit limiting. Thus a customer may only be allowed a certain allocation of energy before they have to pay their bill eg £100, £50 or less depending on their credit rating. We understand that at least two suppliers are considering this option, with customers who fail to pay their bills being load limited. Ofgem will need to monitor developments in this area to ensure that low income and vulnerable customers in particular do not suffer detriment as a result.
- More work is needed in understanding the needs of small businesses and in particular their experience of remote disconnection and switching. There is potential for increased use of pay as you go in the small business sector as flexibility of payment top up increases.

Improving market processes

Settlement arrangements

Proposition 5: Settlement arrangements should use actual daily (gas) and half hourly (electricity) meter reading data in order to improve their accuracy and efficiency.

- *Innovation*
More accurate settlement may lead to scope for product innovation, but it should be noted that product innovation is an activity rather than a public good in its own right (or to put it another way, innovation can lead to good *or* bad consumer outcomes. Apple and Amazon are very innovative – but so were Enron and Lehman Brothers). A wide range of research, much of it conducted by Ofgem, suggests that consumers find existing tariffs confusing and that this can lead them to make bad choices. Ofgem will need to consider the trade-off between cost-reflectivity and simplicity as with facilitating developments in energy services.
- *Demand forecasting*
The current system of settling non half hourly (NHH), based on profiles, leaves suppliers partially insulated from the consequences of unexpected blips in

electricity consumers were using the keypad prepayment meters by mid-2009 with new connections continuing at a rate of 2,000 per month. About 58 per cent are on low incomes but 32 per cent are middle or higher incomes including 17 per cent who are 'wealthy achievers' (Acorn classification).

demand or unusual events, because their imbalance position is based on their consumers' profiled consumption rather than their actual consumption. This insulation comes at a price; the need for residual balancing by National Grid as System Operator, which is directly socialised across market participants and indirectly socialised over consumers. However, shifting risk back on to suppliers is not free either.

- Settling on half hourly (HH) exposes suppliers to increased forecasting risk. Some of this may be manageable; one would expect that suppliers will have a reasonable understanding of their customers and that this understanding will grow with smart roll-out. But some of this risk may be unmanageable; unexpected and/or infrequent events (such as TV pick-ups during major sporting tournaments or tragedies) may result in increased imbalance exposures when compared to settling based on profiles. The core question is whether the net benefit to society is greatest where forecasting risk is managed by suppliers or by National Grid. The presumption in this proposition is the former. We think this is plausible but not self-evident.
- There may also be economies of scale that mean that increasing the forecasting risk that suppliers face favours larger parties (for example; that the cost of forecasting systems will not be linearly related to the number of customers served, or that large players may be better able to support a 24/7 trading function to close out imbalances). It may be more cost reflective to make suppliers face these costs, but it may also hamper market entry – Ofgem will need to make a judgement call on where the balance lies.
- *Credit*
We think one benefit that can be added is credit. Suppliers currently have to lodge credit cover against 29 days¹⁵ of trading charges, in part to reflect the lag time before 'billable' quality data is available in the Settlement Final Run. The monthly Trading Operations Report (chart 3.02) suggest that this results in substantial over-collateralisation; at any given time the amount of excess credit cover lodged is typically somewhere around the £400 million mark, despite daily market indebtedness exposures running in the single digit £millions. Mandatory HH settlement could get billable quality data into settlement quicker, allowing the first payment run to take place sooner and a contraction in the credit window. This could bring a range of benefits:
 - Reducing the amount of collateral tied up as credit cover, the financing costs of which are borne by consumers
 - Reducing barriers to entry by decreasing the amount of working capital that needs to be tied up as credit cover. This is likely to be of particular benefit to smaller players who tend to lodge credit in the form of cash rather than letters of credit
 - Reducing market wide exposure to the risk of bad debts, because the volume of liabilities incurred but not yet settled would decrease. The cost of bad debt is ultimately borne by consumers
- *Reducing back-billing windows – and sorting out problems faster.*
There could be potentially significant consumer benefits if the ability to get accurate data in to settlement earlier can be used to increase the accuracy of consumer invoicing. This would benefit all customers, but may be of particular benefit to small businesses that may currently be back-billed for periods of up to six years.

¹⁵ Notionally, although given that Credit Default provisions kick in when a Party's Credit Cover Percentage exceeds 80 per cent (rather than 100 per cent), and that Parties may build in further headroom because the main imbalance cash-out price is inherently volatile, it is likely that the credit lodged by short Parties will equate to significantly more than 29 days of typical charges.

Our research suggests that many back-billing problems are a direct result of problems with metering or meter reads. We see little justification for allowing back-billing for up to six years even in a pre-smart world; it should be possible for suppliers to identify and resolve all problems much more quickly than this. But in a post-smart world, the justification for allowing back-billing for up to six years becomes even weaker still.

- *The performance assurance regime.*
We think it would be worth giving consideration to whether there would be any impacts on the performance assurance regime. There are potential benefits and costs here, the balance between the two being unclear. In the medium to long term, smart meters could increase the quality of data in settlement and improve the reporting and resolution of errors in so far as this can be automated. In the short term, it may increase the amount of assurance activity required as the process of switching out millions of meters is likely to identify (and possibly cause) large numbers of data errors. Are you making any assumptions on whether the cost of the assurance regime will change, and over what periods?
- *Reduced number (and cost) of settlement runs?*
In principle, smart metering may allow final settlement of liabilities to happen earlier, and possibly with the need for fewer intermediate settlement runs before the RF run. We imagine there would be some cost savings associated with this.
- *Migration issue 1: Cherry-picking sites during the transition period?*
The proposition implies that there may be a transitional period where settling domestic sites with smart meters on a half hourly basis will be optional, prior to it being formally mandated. Allowing suppliers a choice of two settlement outcomes in relation to a single metering point may create gaming opportunities, because there is bound to be a difference between the two outcomes. You should consider whether protections are needed to prevent market abuse.
- *Migration issue 2: Legacy systems.*
The Government's ambition is for all consumers to have a smart meter by 2019. However, consumers will be able to opt out, and experience from international trials and roll-outs suggest that there are a wide range of technical, economic and social constraints that may make reaching every single home extremely challenging. It would therefore be prudent to consider the extent to which legacy systems will need to be maintained and how they will be integrated with DCC activities.
- *Migration issue 3: Displaced error*
Settlement error is currently smeared through Group Correction Factor (GCF). As the number of NHH sites decreases a smaller number of sites will be subject to the smearing process. One would expect that the volume of error would also decrease. If these two reductions are broadly correlated, it may well be that the effect of GCF on the energy volumes of those sites that are still NHH will be relatively stable throughout the transition period. However, if the correlation is weak, this may mean that the impact of GCF ramps up, or ramps down, during the transition period. From a consumer perspective, GCF is only of interest insofar as it has any impact on consumers. If changes to its level were sufficiently large to result in differential charging for smart and non-smart sites that consumers saw we would have concerns about this.

Change of supplier process

Proposition 6: The change of supplier process should be reliable and fast, so that customers can confidently switch supplier on a next day basis.

- We agree that the change of supplier process should be fast and reliable. Consumer Focus is carrying out face to face survey research in March which will seek to understand customer preferences in this area.
- Before supporting same day switching we would seek assurances that administration could be done sufficiently carefully in this dramatically reduced timeframe, and if suppliers which wished to object could do so within this time. This would save consumers from a situation in which they think a switch has been successful and then find that it has not, and to ensure that a much faster turnaround time does not lead to increased error.
- For domestic customers we query how a 24 hour switch would sit alongside requirements to allow consumers a seven-day cooling off period; if the proposal is to abolish the cooling off period then we would not support the proposition as it stands.
- We agree that fast and reliable switching could encourage competition and help consumer engagement in the market. It would also bring energy markets in line with other sectors, such as mobile phones and banks, where customers have come to expect that they can switch provider quickly with little effort or risk.
- We recognise the benefits in terms of improving accuracy of the change of supplier meter reading and reducing erroneous transfers. This should result in reduced costs as these processes are often manual.
- We would suggest that switching times should also be reduced for consumers not on smart meters if this can be done at reasonable cost. However, we would not see the longer switching time as one of the major disadvantages of not having a smart meter, unless suppliers began offering better deals to consumers who could switch onto them sooner.

Data processing and aggregation

Proposition 7: Electricity data processing and aggregation services should be procured centrally in order to reduce costs and support faster switching.

- We welcome any steps that can reduce costs, deliver greater efficiency and improve the customer experience. We are unclear whether this would best be achieved by the central procurement of data processing and aggregation services.
- There are concerns about increased privacy and security risks which would need to be addressed. The impact of a security breach would arguably be greater if data for all consumers was held by a single operator. There is also a reputational risk to the smart metering programme if the DCC is perceived as a central database holding customers personal information. This could lead to consumer backlash.

Code consolidation

Proposition 8: The Smart Energy Code should be used as a vehicle to consolidate existing industry codes dealing with retail issues in gas and electricity to facilitate market development and reduce administrative burden.

- In principle we support this proposition and have advocated for this to some extent in discussions regarding the SEC. It is not clear that this is something which DECC itself sees as a priority. Discussions led by DECC regarding the SEC, for instance in the smart metering working groups 1 and 2, have not mentioned a wider SEC which would cover other industry arrangements. We will respond more fully in the upcoming SEC consultation.



Consumer Focus response to Promoting Smart Energy Markets consultation

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