SCOTTISHPOWER

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David Hunt
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Dear David,

THE RETAIL MARKET REVIEW (RMR) – UPDATED DOMESTIC PROPOSALS

Thank you for the opportunity to comment on Ofgem's updated proposals to reform the domestic market. The aim of the RMR – to encourage and equip customers to engage effectively so that they can get the best deal from the energy market – is a positive one and one that we share for our customers. We have made a significant number of improvements in this area over the last 12 months, but we do think that there is more that we can do to support our customers and help to build greater engagement.

In defining our service offering, we continue to listen to what our customers tell us, which is that they want choice, clarity and control over their energy bills. Our key concern throughout the RMR process has been the impact that the proposals could have on competition and our ability to deliver what our customers want. We have therefore been reviewing Ofgem's revised proposals in light of this.

As you know, we shared the strong concerns of some stakeholders about the impact that some of the previous tariff proposals would have had on competition. We are pleased that Ofgem has recognised those implications and responded with some alternative proposals. We have summarised our high level position on each of the revised proposals below:

- **Simpler Tariffs.** We remain concerned that the net result of the restrictions may be to weaken competition and innovation to the detriment of consumers. Simplifying the choice of tariffs could mean that more consumers are willing to switch for a given saving, but overall switching rates (and hence competitive pressure) may still reduce if there are fewer special offers in the market and smaller potential savings – concerns which have been raised by a number of academic and market commentators. Given this divergence of views, we welcome Ofgem's intention to monitor the market impacts of RMR and conduct an *ex-post* policy evaluation, but we believe that the evaluation should be complemented by a sunset clause on the tariff restrictions. This will counter the risk that, if the restrictions do not achieve the desired result, they are overlaid with yet more regulation when the correct course would be to remove them.

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We also think that there are significant advantages to any cap being set at five tariff types rather than four. With only four tariffs, the ability to make innovative or niche offers such as our discounted "Help Beat Cancer" product would be severely constrained.

- **Fixed Term Discounted Tariffs.** We do not think it is in the best interests of consumers for Ofgem to prohibit tariffs with a time limited fixed discount relative to the supplier's standard tariff. Such tariffs can help reward switching and may have wider benefits (such as our Help Beat Cancer tariff). We see no reason why such introductory fixed discounts should be incompatible with consumer protection legislation, nor do we consider that a prohibition is a proportionate response to the risk that some customers may misunderstand them. In any event, customers on such products are unequivocally better off than customers on a standard product, receiving a cheaper price for a defined period of time, and are subject to the same protections if prices increase.

- **Clearer Information.** We agree that clearer, more consistent information will be of benefit to customers and the information remedies should drive increased engagement in the market, assuming that they are implemented correctly. We were slightly surprised by the level of prescription proposed around some information remedies and are concerned that these are too text-heavy, which could actually hinder engagement. We welcome signals from Ofgem that there is some flexibility in formatting and presentation here and have suggested some alternatives in our response.

- **Market Cheapest Deal Pilot.** We have concerns about the proposed 'market cheapest deal' pilot. As a general rule, regulatory interventions should seek to replicate practice in fully competitive markets, and we can think of no competitive market in which companies alert their customers to rival's cheaper prices. Ofgem is effectively asking suppliers to undertake the role of market intermediaries such as comparison sites, and such distortions of market behaviour carry a risk of unintended consequences. Furthermore, we can see significant practical implementation difficulties, and potential risks for some customers, for example if a customer in receipt of the Warm Home Discount moves to a small supplier and can no longer receive it. If Ofgem proceeds with a pilot, the target group should be narrowly defined to minimise distortions, and careful consideration should be given to the various practical difficulties.

- **Tariff Comparison Rate.** We welcome the overall concept of a Tariff Comparison Rate (TCR) for customers to refer to. However, we do think that careful consideration is needed to ensure that it does not mislead or confuse customers, either through the way in which it is calculated or the way in which it is presented. We strongly object to the proposed methodology for calculating a national average, which we believe would put ScottishPower at an unfair competitive disadvantage.

- **Standards of Conduct.** We support the principle of mandatory Standards of Conduct and the intention behind Ofgem's bespoke enforcement approach that suppliers should look to their customers rather than to Ofgem in deciding what conduct is expected of them. However, it remains the case that Ofgem will be the arbiter of first instance[1] of a wide and subjective licence condition, and further reassurance is needed with regard to the enforcement approach. If there is regulatory uncertainty over how the concept of 'fairness' will be

[1] Subject, of course, to the possibility of review by the courts

interpreted, this will inhibit innovation and investment and deter new entrants from entering the market.

- **Transition**. It will be critical that the transitional arrangements are well thought through, to ensure minimum customer disruption. We believe that all existing fixed term tariffs should be allowed to run their course, assuming that the customer is then moved to the relevant standard evergreen tariff at the end of these in line with the proposals. Given that the aim of the RMR package is to increase consumer confidence in the market, we also believe that Ofgem should seek to minimise the extent to which suppliers are required to impose adverse variations on their customers.

Annex 1 to this letter sets out our more detailed thoughts on each of the proposals and any Licence drafting considerations that we think are relevant at this stage. Annex 2 includes brief answers to the consultation questions.

For each of the proposals, the detailed Licence drafting will be of critical importance and we understand that there is still much work to be done in taking this forward. Ofgem's timescales for creating final Licence Conditions are ambitious and we would anticipate an intensive period of Licence drafting and review in early 2013. We think it is vital that proper consideration is given to how the detailed Licence drafting meets Ofgem's final policy decision once this is agreed, and that all stakeholders are fully consulted as part of this process.

Once the Retail Market Review proposals are implemented, their success will need to be reviewed and assessed on an ongoing basis. We understand that this is Ofgem's intention and that the market will be subject to closer monitoring and scrutiny as a result. Before commencing any further market monitoring, we would urge Ofgem to work with stakeholders to consider what success in the retail market might look like and how Ofgem would propose to track this. Customer switching activity is still a key indicator of the level of competition in a market, but it is not sufficient by itself to assess the wider context of the market and levels of customer satisfaction that surround this.

We would be pleased to discuss any of the points made in this response in further detail. Please contact me on the details above if you would find this useful.

Yours sincerely,

Rupert Steele

Rupert Steele
Director of Regulation

Annex 1

RETAIL MARKET REVIEW – UPDATED DOMESTIC PROPOSALS
SCOTTISHPOWER RESPONSE

Executive Summary

1. The issues raised by Ofgem in relation to its Retail Market Review (RMR) are important and it is clear that the industry needs to take action to address these. We have agreed with this throughout the development of the RMR proposals and continue to believe that this is important.

2. Overall we consider that the revised proposals are a significant improvement on the previous proposals. However, we consider that much of the detail behind the proposals still needs to be refined and there are numerous questions around the practicality and overall impact of the individual proposals which need to be considered. It is of critical importance that the process and timescales for implementing the proposals are designed in a way that minimises any adverse impacts on customers.

Diagnosis of the problem

3. While we agree with Ofgem's overall conclusion that there are problems with the current market that need to be addressed - particularly around the high level of consumer distrust in the market and the capacity, or reluctance of customers to actively seek a better deal - we disagree with key aspects of Ofgem's diagnosis, particularly with regard to the effectiveness of competition. For example, claims that suppliers are focused on retaining customer numbers at a steady level to keep generation and supply demand at equilibrium[2], and that suppliers seek to avoid competing on price to gain customers[3] are contentious and unsubstantiated.

4. Ofgem's proposed package of measures does have the potential to address some of the current market problems of mistrust and disengagement, if managed appropriately. But the proposals do nothing to address other problems which contribute materially to consumer distrust, such as the widespread consumer perception that rising prices are due to supplier profiteering. This needs greater consumer education and awareness – in which suppliers, Ofgem and Government all have a part to play.

Tariff restrictions

5. The revised tariff restrictions are an improvement on the December 2011 proposals and are welcome in that respect, but still represent a radical and potentially disproportionate intervention in the market. We support the goal of improving clarity and transparency for consumers, but we remain concerned that the net result of the restrictions may be to weaken competition and innovation to the detriment of consumers. Simplifying the choice of tariffs could mean that more consumers are willing to switch for a given saving, but overall switching rates (and hence competitive pressure) may still reduce if there are fewer special offers in the market and smaller potential savings - concerns which have been raised by a number of academic and market commentators. In particular, the proposals might strengthen the hand of the

[2] Retail Market Review – Updated Domestic Proposals, Ofgem, October 2012, Chapter 2,para 2.44
3 Ibid, para 2.53

largest suppliers (British Gas and SSE), allowing them to pursue a defensive, high margin strategy, with limited competitive pressures.

6. Although Ofgem acknowledges these concerns in its impact assessment, it discounts them without detailed analysis. Given this divergence of views, we welcome Ofgem's intention to monitor the market impacts of RMR and conduct an ex-post policy evaluation, but believe the evaluation should be complemented by a sunset clause on the tariff restrictions. This will counter the risk that, if the restrictions do not achieve the desired result, they are overlaid with yet more regulation when the correct course would be to remove them.

7. We think it would be wise to consider increasing the cap to five core tariffs. If the cap is set at four, suppliers are likely to use the four slots for relatively mainstream tariff types, sidelining more specialist or niche offers such as Green tariffs or ScottishPower's "Help Beat Cancer" tariff. Increasing the cap to five would make it easier to accommodate such tariffs and would also allow more room for experimentation and innovation. This will be particularly important as we head towards a Smart-ready market and seek to realise the benefits of behavioural change and reduced energy demand.

<u>Prohibition on fixed term discounted tariffs</u>

8. We do not think it is in the best interests of consumers for Ofgem to prohibit tariffs with a time limited fixed discount relative to the supplier's standard tariff. Such tariffs can help incentivise switching and may have wider benefits (such as our Help Beat Cancer tariff). We see no reason why such introductory fixed discounts should be incompatible with consumer protection legislation, nor do we consider that a prohibition is a proportionate response to the risk that some customers may misunderstand them. In any event, customers on such products are unequivocally better off than customers on a standard product, receiving a cheaper price for a defined period of time, subject to the same protections if prices increase.

<u>Transition issues for tariff restrictions</u>

9. It is important that the tariff proposals are introduced in a way that causes minimum upset to consumers and gives suppliers a reasonable time to minimise the impact on their business. In particular, we think it is vital that customers who are on existing fixed term tariffs at the time the conditions come into force, should be allowed to remain on those tariffs until the end of their current deal. We also think that customers on No Standing Charge Evergreen tariffs should be allowed to remain on these tariffs (within the context of the rules around 'dead' tariffs).

10. We would also note that we are currently undergoing a tightly-controlled migration to a new Fully Integrated Billing and Service SAP platform, taking a staged approach which will see customers migrated over to the new system over the course of 2013. This will involve significant investment and ongoing system development over the next 12 months. We do not consider that this will be a barrier to implementing the proposals, but we would welcome the opportunity to have an ongoing conversation with Ofgem as our migration proceeds and we are able to better assess the approach necessary to implement the proposals.

<u>Information measures</u>

11. We agree that providing better information to customers will bring wider market benefits. If we are to excite and engage customers who are currently disengaged

from the market, the information provided to them needs to be accessible and useful. We have some concerns about the level of text and formatting of some of Ofgem's prescriptive proposals and we look forward to working with Ofgem to develop this in a format that works best for consumers.

Tariff Comparison Rate

12. While we welcome the concept of the Tariff Comparison Rate, we think that establishing the correct methodology for calculating it will be vital. We strongly object to the proposed methodology for calculating the national average since it will place suppliers who have a high number of customers in areas with high network costs at an unfair competitive disadvantage (and may provide some consumers with a misleading ranking of suppliers). We consider it would be more appropriate to have either a flat average or weighted average based on the total number of meter points in each region, thereby providing consistency across suppliers. We also believe much more thought needs to be given to how the TCR will be used in marketing materials (which can vary in scale from customer leaflets to billboards to customer leaflets) and the amount of supporting information that would need to be provided with this.

13. It must be recognised that it will be impossible to calculate a perfect national TCR; some level of approximation and risk of misleading some customes must be accepted. The alternative would be to look at a regional TCR, though there would then have to be simplifications about when and how it was used. A careful balance must be struck here.

Transparency

14. In terms of transparency, one of the main reasons for customer mistrust in the industry is the perception that prices are rising as a result of profiteering, rather than due to investment or the costs to supply. One of the main reasons for rising energy prices is the increasing costs of distribution and transportation, and social and environmental obligations. It is important that customers understand what makes up their bill and the impact that these costs have on the bill. We would like to work with Ofgem to develop new and innovative ways to help customers engage with their bills in such ways.

Implementation issues for supplier cheapest tariff

15. We have particular concerns about the implementation of the supplier cheapest tariff requirements, specifically the cost and time required to do this on all bills. Currently we provide personalised savings information to customers on some more targeted communications, such as End of Fixed Term Period notifications. However, the costs and impacts of providing this detail on more routine communications is not yet clear.

16. In particular, the biggest constraint in this case is the technical challenges associated with implementing a solution to deliver such detailed information to customers. While not impossible to implement, at a technical level this is not a straightforward, or low cost, change. We would therefore encourage Ofgem to take this under consideration in developing the final proposal.

Market Cheapest Deal

17. We have concerns about the proposed 'market cheapest deal' pilot. As a general rule, regulatory interventions should seek to replicate practice in fully competitive

markets, and we can think of no competitive market in which companies alert their customers to rival's cheaper prices. Ofgem is effectively asking suppliers to undertake the role of market intermediaries such as comparison sites, and such distortions of market behaviour carry a risk of unintended consequences. Furthermore, we can see significant practical implementation difficulties, and potential risks to vulnerable consumers, for example if a customer in receipt of the Warm Home Discount moves to a small supplier and can no longer receive it. If Ofgem proceeds with a pilot, the target group should be narrowly defined to minimise distortions, and careful consideration should be given to the various practical difficulties.

Standards of Conduct

18. We support the principle of mandatory Standards of Conduct and the intention behind Ofgem's bespoke enforcement approach that suppliers should look to their customers rather than to Ofgem in deciding what conduct is expected of them. We already aim to provide a service that meets our customers' needs and is based on our assessment of those needs and we think that the Standards, if managed effectively, can help to provide a robust basis for this.

19. However, it remains the case that Ofgem will be the arbiter of first instance[4] of a wide and subjective licence condition, and further reassurance is needed with regard to the enforcement approach. If there is regulatory uncertainty over how the concept of 'fairness' will be interpreted this will inhibit innovation, investment and deter new entrants from entering the market. These concerns are all the greater given the highly political nature of the energy market and the scope for Government intervention in regulatory policy.

20. We continue to think that there is a strong case for a two-stage enforcement process, but failing that, we would like to understand how Ofgem intends to document and manage the bespoke enforcement process, and how it will eliminate subjectivity. Beyond this, the drafting of the Standards merits discussion, particular the scope and definition of 'fair' within this context, to ensure that it does not inadvertently prevent suppliers from taking justified action. For example, blocking a transfer due to debt (in accordance with the rules) would benefit the supplier and be detrimental to that particular customer, but ought not to be considered unfair within this context.

Monitoring and evaluation

21. In developing a suite of successful remedies, Ofgem needs to ensure that it has a clear vision of how it will measure the success of those remedies for customers. We welcome proposals for increased market monitoring to determine the success of the remedies. A robust suite of measures - including measuring the numbers of customers who have changed tariff with their current supplier and customers who have ever taken a non-standard product - will be essential in helping Ofgem to fully understand and assess the operation of the market.

Chapter 2 Assessment – Why the Market Needs Reform

22. In Chapter 2 of its consultation document, Ofgem sets out an assessment of the market and some of its perceived failings, leading to the need for reform. While we continue to agree that the market could do a lot to improve customer trust, we

[4] Subject, of course, to the possibility of review by the courts

consider that some of the statements in that aspect of the consultation document should be challenged. This includes allegations that there is no evidence that energy companies seek to minimise controllable costs[5], that the number of passive customers is increasing and that current engagement levels are insufficient to support effective competition in the market going forward[6], and concerns that suppliers follow their competitors' prices rather than looking to compete directly to gain market share[7]. We believe that many of these points are unfounded.

23. As a first point, a fundamental reason for the lack of trust in suppliers – which is also borne out by Ofgem's own research – is the perception that the rising price of energy is solely or mainly due to supplier profiteering. Research commissioned by ScottishPower[8] found relatively low spontaneous awareness of component costs amongst the general GB population responsible for household energy bills. The majority of respondents (52%) stated they did not know what components made up their energy bill. Of those who did mention specific components, these were reasonably well identified, however, the contribution of 'supply company profits' to the bill was substantially over-estimated.[9]

24. Although the consultation document makes reference to rising domestic margins the evidence presented shows that margins remain low as a proportion of the average bill.[10]. Indeed our most recent price rise was primarily due to substantial increases in non-energy costs, over which we have no control. Therefore, a key issue of trust in the market is based on perception rather than reality and we think that more can and should be done to address this issue. None of the proposals set out later in the RMR document specifically seek to address this misconception that rising bills are due to profiteering.

25. We therefore believe that Ofgem, the Government and industry need to work together to increase consumer awareness of the impact of these externally driven costs and the effect that they can have on customer bills. Increased transparency of bill components is a key part of this. As customers become more familiar with the make-up of their bill this could pave the way for tariff innovation. For example, more savvy consumers might be willing to opt for tariffs which track externally measured indexes of energy and non-energy costs – in the same way that businesses often opt for energy price tracking tariffs at present.

26. Ofgem cites the concern that the number of passive customers in the market is increasing and that current engagement is too low to maintain sufficient market competition. Whilst we acknowledge that switching rates have fallen from previous years, rates of switching in the domestic supply markets are still comparable with those of other competitive markets in GB, such as phone or broadband and are still relatively high when compared to energy markets in other countries[11]. In the World Energy Retail Market Rankings Report for 2012, it is noted that the market in Great Britain remains active with characteristics including high levels of customer awareness, powerful online switching and comparison services, active media and retail price volatility. However, the authors also note that switching has fallen significantly following the discontinuation of door to door marketing.

[5] Retail Market Review – Updated Domestic Proposals, Ofgem, October 2012, Chapter 2,para 2.51
[6] Ibid, paras 2.32 – 2.37
[7] Ibid, para 2.55
[8] Source: YouGov Omnibus survey for ScottishPower, February 2012[8]
[9] Based on a weighted average of responses, profits were thought to contribute to 21% of the bill.
[10] Retail Market Review – Updated Domestic Proposals, Ofgem, October 2012, para 2.65
[11] Source: The World Energy Retail Market Rankings Report 2012 by the Utility Customer Switching Research Project (UCSRP) (published by VAASA ETT, Global Energy Think Tank)

27. This suggests that the customer churn rate between suppliers is not enough on its own to base a full assessment of the competitiveness of a market. Other relevant considerations include the improved trend noted by Ipsos MORI in the number of customers switching tariffs or payment methods with their current supplier. Our own customer activity supports this, with around 15% of our customers switching tariff or payment method every year.

28. Ofgem considers that "incumbent suppliers still retain a high proportion of the customers which they inherited at privatisation" and that incumbents therefore retain a significant competitive advantage over other suppliers, particularly small suppliers, who are less able to offer prices to meet those of the incumbents[12]. We believe this overstates the position. Firstly, Ofgem's own analysis of the impact of SLC 25A showed that the differentials between incumbent and non-incumbent prices have reduced as a result of the implementation of SLC 25A, and any advantage is unlikely to be material. Secondly, smaller suppliers have an inherent advantage in that they do not have to bear the increasing costs of social and environmental obligations that larger suppliers have to recover through their prices.

29. Ofgem also states that research done during the Probe indicates that suppliers often wait for other suppliers, particularly the regional incumbent, to move before making their own price change. Firstly, the regional element of this suggestion does not seem to make sense in that suppliers tend to move prices simultaneously GB-wide, rather than making piecemeal price moves in individual areas depending on the when the various incumbents move. Secondly, the fact that suppliers take account of any prior competitor price movements in finalising their own tariff changes is entirely consistent with a competitive market; it is a sign of ineffective competition if a company can price independently of the actions of its competitors. The impression of 'leader-follower behaviour' may be more pronounced in the energy market because price changes are widely publicised and expensive to implement (and therefore occur relatively infrequently). This greater visibility does not mean that there is a problem with competition or any detriment to consumers..

Proposal 1 – Simpler Tariffs

30. We continue to be fully supportive of measures to improve tariff comparability, provided that these are targeted at the right level to ensure the most efficient and competitive market for consumers. Although Ofgem's revised tariff proposals are an improvement on the December 2011 proposals, we think they still represent a radical intervention in the market which is likely to have an adverse impact on competition.

<u>The case for a sunset clause</u>

31. Although the tariff cap (and other tariff restrictions) will simplify the choice of tariffs and therefore make it easier for consumers to engage, it is likely that they will also lead to convergence between tariffs and a reduction in the savings available to switchers. This is for two reasons: suppliers may no longer be able to offer the deeply discounted tariffs which are typically used for customer acquisition; and there

12 Ofgem, Op cit, para 2.32

is a risk that greater transparency will make it easier for suppliers to track each others' prices leading to 'coordinated' pricing behaviour[13].

32. There is a wealth of evidence that consumers' propensity to switch is strongly dependent on the available saving[14], which means that any positive impact on switching from increased simplicity may be outweighed by the negative impact of reduced switching incentives. These trade-offs are acknowledged by Ofgem in its draft Impact Assessment:

> "We recognise the possibility that our proposal could lead to a short-term reduction in the availability of deeply discounted deals. However, over the longer term, a more engaged consumer base should help to increase competitive pressure on suppliers and force suppliers to look for efficiency savings."[15]
>
> "We recognise that there is scope for "coordinated effects". Firstly, with fewer tariffs in the market coupled with the TCR and other simplification measures, suppliers may find it easier to monitor each other's prices and/or bundled products and services. Over time, it might be that this greater transparency allows suppliers to respond more easily to rivals' strategies, thereby reducing the differentials that exist between them. ... On balance, we consider that a more engaged consumer base will help to reduce these effects and will outweigh any incentive for firms to co-ordinate their actions." [16]

33. Ofgem clearly believes that the balance lies in favour of the tariff restrictions, and we cannot disprove this hypothesis. However, we would note that in their commentary on the Government's tariff proposals (which closely mirrored the RMR proposals), financial analysts generally played down the risk that this would lead to increased competition and lower profits for suppliers – indeed they suggested it would work to the advantage of larger suppliers such as Centrica and SSE who would have less need to defend their customer base from aggressive pricing by smaller competitors (see Box 1).

Box 1: Reactions of industry analysts on 20 November 2012 to the Government's intention to require energy suppliers to put their customers on the lowest tariff and limit the number of tariffs to four (emphasis added):

JP Morgan: "We await the details of the proposed Government legislation to see how it will tackle such things as regional differences due to different network charges, different costs associated with different methods of payment (prepayment, direct debit etc) and internet based tariffs. We are also interested in how any new legislation will incorporate time of use tariffs which will become more prevalent as the penetration of smart meters increases. **Our initial view is that any legislation will lead to even lower gross churn in the industry through the removal of discounts for new customers and as such play to the advantages of the larger suppliers such as Centrica and SSE.**"

Merrill Lynch: "Our view remains that this is unlikely to be a major concern for the companies, who are already simplifying tariffs in response to Ofgem's Retail Market Review. SSE and Centrica have already overhauled their product range. The RMR

[13] For further explanation, see 'Economic appraisal of Ofgem's domestic tariff proposals - An appropriate intervention to increase consumer engagement?, Report prepared for ScottishPower', Oxera, March 2012, http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Scottish%20Power%20Oxera%20report.pdf
[14] E.g. see ScottishPower response to previous RMR consultation, chart on page 30, http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Scottish%20Power%20response.pdf
[15] Impact Assessment page 39, para 4.12
[16] Impact Assessment page 38, paras 4.9 to 4.10

already provides for suppliers to offer only 4 tariffs depending on how customers want to pay, in order to make increase transparency and make it easier to compare prices. **The move would outlaw predatory pricing and could actually reduce competition as well as churn rates**. **Companies will simply adjust overall tariffs in order to recover a reasonable overall profit.** Last week, SSE welcomed the possibility of such legislation."

Nomura: "If implemented, these proposals appear to be stronger than those put forward by Ofgem as part of its retail market review, which only required the inclusion of information on cheaper tariffs within customer bills. If there are customers that are not on the cheapest tariffs, which suppliers are obliged to move across, the initial impact could be negative on the margins for these supply businesses (such as those for Centrica, SSE). **However, over time it could result in tariff convergence and a reduction in competition.**"

34. This view is supported by Professor Littlechild who commented on the Government proposals as follows:

> "Such proposals are effectively a tax on competition. They would drive the lowest prices out of the market. Over time this reduction in competitive pressure would increase prices and profit margins across the board. All customers would be worse off, including those the policy is designed to help.
>
> ... The proposals have no counterbalancing advantages. The only potential beneficiaries would be the major energy suppliers, which would be able to enjoy quieter and more profitable lives, unhindered by retail competition.
>
> ... The longer-term consequences are even more serious. When such policies deliver less competition rather than more, and higher prices rather than lower, is it likely that the government will repeal them? More likely, it will say that the policies did not go far enough. There will be a demand for direct controls on profit margins, on wholesale transfer prices and on final retail prices. And if a competitive market has failed so comprehensively, what is the case for continued private ownership?"[17]

35. Ofgem may argue that, even if there is a weakening of competition (and hence an increase in average prices), this is nevertheless justified on the basis of 'fairness' and protection of vulnerable consumers: if the gap between sticky and engaged consumers is reduced, this will tend to benefit vulnerable consumers who are more likely to be sticky. However, as Catherine Waddams points out in a recent article on RMR[18], this trade-off between average prices and protection of vulnerable consumers is one that ultimately needs to be made by Government:

> "Vulnerable consumers could be protected by regulation, though this would probably involve higher prices across the market because of the inefficiencies of any regulatory process. The final judgement, in the UK with its long experience of deregulated markets, and elsewhere where competition is just beginning, must lie with governments. They cannot eat their cake and have it, enjoying the benefits

[17] '*Simpler energy tariffs will lead to higher bills and less competition'*, Stephen Littlechild, City AM, 29 November 2012, http://www.cityam.com/forum/simpler-energy-tariffs-will-lead-higher-bills-and-less-competition

[18] 'Retail Energy Markets: Does competition offer enough protection?', Catherine Waddams, http://competitionpolicy.ac.uk/documents/107435/107588/CCP+Research+Bulletin+Issue+24+Autumn+2012.pdf/1bb33b0d-e5ff-4292-b27c-6bb61be0b965

both of competition and protection; in making the choice, they would do well to recall that the road to hell is paved with good intentions."

36. Given the wide range of views as to the likely outcome of the proposed tariff restrictions, from highly positive to highly negative impacts on consumers, we welcome Ofgem's intention to monitor the market impacts of RMR and conduct an ex-post policy evaluation. However we strongly believe that this monitoring should be complemented by a sunset clause on the tariff restrictions, such that the restrictions automatically lapse after (say) three years unless positive steps are taken to extend them. This will counter the risk that, if the restrictions do not achieve the desired result, they are overlaid with yet more regulation when the correct course would be to remove them. Such a sunset clause would also be consistent with the Coalition Government agreement, which recognises the need for incentives to regularly review key regulations in order to build a fairer and more balanced economy: "*We will impose 'sunset clauses' on regulations and regulators to ensure that the need for each regulation is regularly reviewed*."[19]

Transition arrangements

37. The proposals are likely to mean significant adjustment to some suppliers' tariff portfolios and the impacts on customers could be significant if not managed correctly. We understand from discussions with Ofgem that the proposal is to ensure that, from a certain date, all customers are *offered* a choice of no more than four core tariffs per fuel and meter type, and that customers on existing fixed term offers will be allowed to remain on those offers until they have run their course. We would welcome confirmation of this point, as it is a fundamental factor in allowing us to be comfortable with the proposals.

Tariff cap should be five not four

38. We think it would be wise to consider increasing the cap to five core tariffs. Four tariffs might allow the market to deliver the more mainstream or in-demand tariff types, but is likely to mean that more specialist or niche tariffs will be overlooked, and the scope for innovation will be constrained.

39. Different suppliers will reach different commercial judgments on preferred tariffs within any cap, but an illustrative scenario is that a supplier might choose the following under the proposed four core tariffs limit:

a) a standard variable, evergreen tariff;
b) a fixed term, fixed price one year tariff;
c) a fixed term, fixed price longer term tariff[20]; and
d) a cheaper online fixed term tariff.

40. Increasing the tariff cap from four to five would make it easier to accommodate green tariffs, which can help to support Government aims to deliver a low carbon economy, or niche tariffs that support special interests and have a wider societal benefit, such as charity support. For example, on the assumption that ScottishPower wanted to offer the four tariffs described above, we would no longer be able to offer our Help Beat Cancer tariff nor our Simply Green tariff. Our Help Beat Cancer Discounted

[19] 'The Coalition: Our programme for Government', The Cabinet Office, 2010, page 10, http://www.cabinetoffice.gov.uk/sites/default/files/resources/coalition_programme_for_government.pdf
[20] While some customers will opt for a one year fixed price tariff, in a climate of rising prices there are other customers who would prefer the security of a longer term fixed price tariff at a slightly higher price.

Tariff offers customers a 4% discount against our standard prices until February 2015. As part of this tariff, customers also contribute to Cancer Research UK, through donations which we make on their behalf, across the lifetime of the offer. This tariff has already raised substantial sums of money for Cancer Research UK.

41. Increasing the cap would also allow more space for innovation and experimentation. It is a natural feature of a competitive market that suppliers use small scale experiments to test new products with customers, in order to understand what works best in terms of engaging customers. With a cap of four tariffs, such experimentation would be severely curtailed. This will be of particular concern as the market attempts to become Smart-ready. However, it is not just smart metering where tariff innovation may be needed. As an example, suppliers may in future wish to offer a form of tracker tariff in which customers agree to pass-through of certain externally driven costs in exchange for cheaper up-front costs. We are already seeing a move to tariffs of a pass-through nature in the SME market and some European domestic markets – though it is likely to require a greater level of consumer engagement and understanding before there is significant demand in the GB market.

42. In a similar vein, we think that the proposed exception to the tariff cap for collective switching tariffs is a sensible one, provided that the concept and scope of the exemption can be appropriately defined. Collective switching schemes have the potential to increase consumer engagement and raise the possibility of switching in a secure way to customers who have previously been unaware or wary of switching. Schemes such as iChoosr, which seeks to work with community leaders to encourage customers, particularly those who have not switched before, to switch to get a better tariff for them, have the potential to help achieve the RMR aims.

43. We note, though, that 'collective switching' in this context has not been defined. We would consider a 'collective switch' to be one where a group of consumers (i.e. more than one), or a body representing such a group, agrees a tariff which all of the members of that group can access during a defined time period. We would also suggest that suppliers should be free to restrict the availability of 'collective switching' tariffs to a specific set of customers (e.g. those signing up with the collective switching provider) – which would mean that those tariffs are exempt from inclusion in supplier cheapest tariff messages.

<u>Fixed Term Tariffs</u>

44. We do not agree that it is necessary to introduce a ban on tariffs that offer a discount relative to the supplier's standard tariff, provided that the discount is offered as a fixed amount[21] which stays constant[22] for the duration of the fixed term period (hereafter 'discounted tariffs').

45. Banning such tariffs will not be in the best interests of consumers. It will contribute significantly to the problem of tariff convergence, which, as we have highlighted above, could lead to lower switching rates and weaken competition between suppliers. It will also constrain innovation and potentially lead to the withdrawal of tariffs with wider societal benefits. A case in point is ScottishPower's Help Beat Cancer Discounted Tariff, which offers a customer a 4% discount against our standard prices until February 2015. As part of this tariff, customers also contribute to

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[21] At present such tariffs are typically expressed as a fixed percentage discount to the standard tariff, but in accordance with Ofgem's proposed prohibition on percentage discounts, they could alternatively be expressed as a fixed p/kWh discount relative to the standard tariff.

[22] We have no objection to a prohibition on fixed term products offering a *variable* discount against a supplier's standard tariff. Such products typically guarantee a discount of 'at least x%' but are offered at an initial discount which exceeds x% .

Cancer Research UK, through donations which we make on their behalf, across the lifetime of the offer. This tariff has already raised substantial sums of money for Cancer Research UK.

46. We struggle to see how discounted tariffs can be considered to be detrimental to consumers. Consumers on such tariffs are always better off than if they were on a supplier's standard variable tariff and enjoy exactly the same safeguards in respect of adverse price variations. Provided that appropriate safeguards exist at the end of the fixed term (which are the subject of separate Ofgem proposals) consumers cannot suffer any obvious detriment.

47. We understand that Ofgem's rationale for this proposal is threefold:

    a) some customers do not understand such products and mistakenly believe that prices are fixed;

    b) there is little consumer appetite for such products;

    c) such tariffs may be contrary to general consumer protection legislation.

    We consider each of these points in turn.

Consumer understanding of discounted products

48. Ofgem argues that fixed term discounted products are potentially confusing for consumers, citing previous research findings that consumers often equated fixed duration with fixed price, and in some cases assumed that fixed duration meant they were locked into the contract for the duration.[23]

49. We agree that the marketing of discounted tariffs needs to be particularly clear to ensure that consumers understand the nature of the tariff and are fully aware of the terms under which they operate, and accept that more could be done by suppliers to improve the clarity. However, we do not believe that a ban on such products is a proportionate response to such misunderstandings.

50. Given the widespread lack of interest in energy products and low levels of consumer engagement, it is not surprising that the research revealed some consumer confusion with respect to discounted products – particularly bearing in mind that the experimental conditions may not have described the products with the same care as suppliers would aim to achieve in an actual sale. Our experience of selling discounted products reveals a high level of customer awareness and very little (if any) evidence of complaints relating to such misunderstandings.

51. We suspect the proportion of customers affected by such misunderstandings is very low in practice, and that the associated detriment is also very low. Accordingly, we think a more proportionate response would to tighten up the rules around end of fixed term conversions to avoid any detriment (as is already proposed) and if necessary tighten up rules around marketing of such products.

[23] 'Tariff Comparability Models, Volume 1 - Consumer qualitative research findings', Creative Research, 11 October 2011, page 42

Customer appetite for discounted products

52. Ofgem also argues that consumers have little appetite for discounted products, citing research which suggests that consumers broadly prefer fixed term fixed price tariffs[24] and questioning whether consumers have a strong expectation to see non-fixed price fixed term tariffs in the market.[25]

53. These findings are at odds with our own research and experience in the market, and appear to be the result of poorly designed experiment. At a time when energy prices are generally expected to be on the increase, a rational consumer would expect to pay a premium for a fixed price product. In the experiment which Ofgem refers to, consumers were simply asked whether they would be likely to choose fixed price, variable price or tracker tariffs[26]. In the absence of any explanation that fixed price tariffs would be more expensive than variable tariffs, it is unsurprising that more consumers opted for fixed price tariffs.

54. Research conducted for ScottishPower in 2009[27] showed that broadly similar proportions of consumers found fixed term discounted tariffs appealing as found fixed term fixed price tariffs appealing. This is borne out by our experience of the market. We have a large number of customers on discounted tariffs (circa 11% of our domestic customer base), including a significant number on our Help Beat Cancer Discounted Tariff (see above). Customers will generally have opted for such tariffs in preference to fixed or capped price products also offered by Scottish Power, confirming that many customers prefer to pay a lower price now, and run the risk that tariffs may rise in future[28]. A similar range of preferences is observed in other markets, such as mortgages.

Consumer protection law

55. Ofgem says it is concerned that fixed term products which permit the supplier to make adverse price changes are ‘not in alignment with’ general consumer protection legislation (e.g. 2009 Gas and Electricity Directives, and the Unfair Terms in Consumer Contracts Regulations 1999) and the provisions of SLC 23.[29]

56. We have taken external legal advice which confirms that fixed term discounted products offering a fixed level of discount are not unlawful, or inconsistent with the Third Package Directives or general consumer protection law.

57. The closest reference we can find to a prohibition on adverse variations is in the Unfair Terms in Consumer Contracts (UTCC) Regulations 1999, which implement the Unfair Contract Terms (UCT) Directive[30]. These contain a list of examples of terms that may be regarded as unfair, including:

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[24] Draft Impact Assessment, para 3.26, citing ‘Consumer reactions to varying tariff comparability, Quantitative Research conducted for Ofgem’, Ipsos MORI, October 2011..

[25] Draft Impact Assessment, para 7.17

[26] When asked which they would probably choose, 47% of consumers tested chose fixed, 9% chose tracker and 6% chose variable price tariffs

[27] 73% of customers found a fixed term discounted tariff to be appealing, of which10% found it very appealing; 70% of customers who found a fixed term fixed price tariff to be appealing, of which 31% found it very appealing (Source: ICM Omnibus 782 (Respondents with joint or sole respondents for energy bills). 30th October – 1st September 2009)

[28] The relative preferences does of course vary over time, and in recent months, we have seen particularly strong demand for our fixed price products

[29] Condoc para 9.24

[30] Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31993L0013:en:HTML

j) "*enabling the seller or supplier to alter the terms of the contract unilaterally without a valid reason which is specified in the contract;"*

however, this is

"without hindrance to terms under which a seller or supplier reserves the right to alter unilaterally the conditions of a contract of indeterminate duration, provided that he is required to inform the consumer with reasonable notice and that the consumer is free to dissolve the contract."

58. In applying this provision to Fixed Term Supply Contracts, it is necessary to recognise that 'fixed term' does not necessarily mean the *contract* is of fixed duration. The 'fixed term' relates to the period over which certain features of the price are guaranteed (e.g. a discount relative to standard tariffs or a fixed price), and in some cases, the period during which the customer may be liable to an early termination penalty. However, in every case that we are aware of, the contract continues indefinitely thereafter, typically reverting to a standard evergreen tariff, or whatever other tariff may be specified in the contract[31]. In such cases, the contract is therefore of indeterminate duration and qualifies for the 'without hindrance' exemption (subject to the tests associated with that exemption).[32]

59. There is already a general requirement under SLC23[33] to inform the consumer with reasonable notice of any unilateral change in the terms and conditions of an energy supply contract, and to allow them freely to dissolve the contract in the event of such change. As a result of this condition, consumers are made aware at the time they enter a fixed term discounted contract that they may terminate it without penalty if there is any adverse unilateral price change, and they are reminded of this opportunity at the time they are notified of the price change. The two tests of the 'without hindrance' exemption are therefore met in every case (or if they are not, the product is in breach of SLC23[34]). We therefore conclude that fixed term discounted products are not caught by example (j), and in any event are not contrary to the provisions of UTCC/UCT.

60. Finally we would note that most, if not all, consumer protection legislation is targeted at contract terms (or other behaviour) that cause (or have the potential to cause) detriment to the consumer. As argued above (paragraph 46), we can see no reason why fixed term discounted products should give rise to any consumer detriment, since the consumer is unequivocally better off than they would be under the standard evergreen tariff against which the discount is pegged.

Simplify Tariff Structures

61. While we generally support proposals to simplify tariff structures, we believe that careful consideration has to be given to how customers on existing evergreen No

[31] Under proposed SLC23C.3(e)(iv), the contract would be required to revert to the Relevant Cheapest Evergreen Tariff unless the customer has opted for another fixed term period.
[32] Even if the contract did not count as being of 'indeterminate duration', the relevant terms would not necessarily be considered unfair. However, if Ofgem merely wished to ban fixed term discounted products which also had a fixed contract term, we would have no objection, but that is not how the current proposals are expressed.
[33] '**23.3** If, in accordance with the terms of a Domestic Supply Contract with a Domestic Customer, the licensee unilaterally varies a term of the contract: (a) to increase the Charges for the Supply of Electricity to a Domestic Premises ...the licensee must give Notice of that variation to the customer in accordance with paragraph 23.4. **23.4** The Notice referred to in paragraph 23.3 must: (a) be given either in advance of the date on which the variation has effect or no later than the end of 65 Working Days after the date on which the variation has effect; (b) inform the Domestic Customer that he may end the Domestic Supply Contract if the variation is unacceptable to him'
[34] Ofgem implies that certain fixed term discounted products may not currently be observing the provisions of SLC23. If so, it would be open to Ofgem to take enforcement action under the existing licence condition.

Standing Charge tariffs will be managed. Currently 44% of our domestic customer base is supplied on a No Standing Charge tariff and we have customer research which indicates that, if given a choice and an explanation between the different options, around a third would prefer a No Standing Charge option.[35]. This supports our view that customers like a choice over how they manage their energy and that No Standing Charge options are seen by many as preferable to a Standing Charge. It is important that any changes in this area are handled sensitively, to ensure that customers who have actively selected this offer are not unnecessarily upset, which could taint the public reaction of some customers to the proposals more generally.

62. We understand from discussion with Ofgem that existing Fixed Term tariffs will be allowed to run their course, so no immediate change is needed for those customers on fixed term No Standing Charge tariffs. Those customers will simply be moved to the cheapest evergreen Standing Charge tariff at the end of the current fixed term. However, a key question is whether suppliers will be required to automatically move all customers who are currently supplied on existing evergreen No Standing Charge tariffs to the closest equivalent Standing Charge tariff.

63. Based on initial analysis of our current customer base, we estimate that around 63,000 households would be disadvantaged by moving from a No Standing Charge tariff to a Standing Charge tariff at an average cost of around £70 per annum (based on a customer with both gas and electricity on No Standing Charge tariffs). Removing the No Standing Charge option for these customers will therefore mean imposing an adverse unilateral contract variation on them, equivalent to a price increase. Indeed, we may conclude we would need to treat removal of the No Standing Charge option as an adverse variation for all customers because of the possibility that their circumstances might change.

64. Whether the adverse variation notices need to go to the broader or narrower group, they are likely to cause a natural level of concern and customer complaints, including from some customers who will be upset at losing the choice of a No Standing Charge tariff. In this scenario, it will be important to ensure that customers fully understand the reason for the change and why a No Standing Charge option is no longer available to them. We think that the level of customer upset that would arise from this latter approach merits allowing customers to remain on these tariffs as ‘dead evergreen’ tariffs, or at least giving suppliers a longer window over which to move customers off these tariffs. We welcome confirmation from Ofgem over this point.

65. We would also be keen to understand how cash back offers would operate with the simplified tariff structures. We understand that potentially these would be treated as discounts – although practically, we do not think that this works in light of the current Licence drafting. However, there may be cases where a supplier is able to realise cost savings, e.g. via a particular sales channel, and it is only fair to customers that they should be able to realise some of these cost savings. For example, a third party website promotes a supplier’s tariff at no cost to capture (as in the case of some collective switches), then customers signing up to that tariff through that particular route would result in cost savings for the supplier. It would seem sensible then that the supplier should be allowed to pass that saving on to the customer in the form of cash back. The current proposals however, do not seem to allow for this scenario.

[35] 33% of customers would prefer a No Standing Charge option; a further 32% did not have a preference, with 18% preferring a Standing Charge. Figures are from YouGov Plc. Total sample size was 2,064 adults. Fieldwork was undertaken between 21st - 23rd August 2012. The survey was carried out online. The figures have been weighted and are representative of all GB adults (aged 18+).

66. Similarly, there may be tariffs which make a donation to a charity or other organisation on the customer's behalf, such as with our Help Beat Cancer tariff, through which we will donate up to £45 to Cancer Research UK over the lifetime of the product. We would welcome comfort that tariffs such as this, with an additional benefit or feature that is not applied to the customer's account would not be inhibited by the new Licence proposals.

67. We would also appreciate clarification on the application of payment method differentials to the core tariffs. We expect that this would be calculated as a £ per year figure based on industry average consumption and then scaled across the consumption bands accordingly. As there are some cost differences that scale with competition, such as bad debt costs, it will be important to ensure that these can remain as an aspect of the payment method differential in order to achieve true cost reflectivity. However in the current proposals, it is not apparent that payment method differentials can be calculated in a way that captures both fixed and scalable cost differences, which would otherwise be truly cost reflective. We consider that there may be tensions with SLC 27.2A that we think need to be acknowledged here and we would welcome further guidance or discussion with Ofgem on this point.

68. As a final point in relation to tariff structures, we think that it will be impracticable for all of the charges listed in Schedule 22B of the draft Licence Conditions to be displayed as a pence per kWh or pounds per annum figure. Many of the charges listed in the Schedule are ancillary charges that are likely only to arise at a particular point in the customer's association with ScottishPower. For example, disconnection or warrant charges will only apply to a minority of customers, and the final charge that applies will depend entirely on the stage within the warrant process that the customer reaches. It will be impossible to make statements that charges of a set amount will apply, particularly if that amount is required to be expressed as an annual amount.

<u>Removing dead evergreen tariffs</u>

69. A very small number[36] of ScottishPower customers are currently on a dead evergreen tariff and the majority, if not all of these, are likely to be cheaper than our current standard evergreen tariff. Therefore, we are broadly comfortable with plans to protect customers on dead evergreen tariffs and to conduct an annual review, applying the same logic. Some care will be needed with the definition of the cheapest evergreen tariff to which customers on dead evergreen tariffs are switched. For example, affinity deals may not be suitable if the customer has no or even a negative affinity with the cause in question.

70. We do not see a strong rationale for derogations for any dead tariffs at this point in time. The only exception may be for preserved meter tariffs in some areas; however we consider that the number of affected customers is likely to be small.

Proposal 2 – Clearer Information

71. We fully support proposals that are designed to bring customers more clarity and information on their energy supply, therefore we think that Ofgem's intention and, broadly, approach here is the right one. We do however consider that more work is needed on the formatting and content of the information, to ensure that it truly is valuable and accessible for customers.

[36] Less than 1,000 (0.03%) of our domestic customers

Tariff Information Label

72. We support the concept of a tariff information label which summarises the key terms and features of a tariff in a user-friendly format. Indeed, as an interim measure we have created our own label, which we have been using on all tariffs from July 2012. We recently tested our own version of a Tariff Information Label with our ScottishPower Tell the Energy People Panel. This Panel consists of around 7,000 customers and its main aim is to provide a regular view of customer satisfaction at a quantitative level and a deeper understanding of why customers score satisfaction the way they do. It also helps us to identify and understand areas for improvement across our business.

73. Overall, the Panel findings showed that customers responded well to the revised information format, finding the information to be user-friendly and trustworthy. Customers particularly liked the clear and simple table format within which the information was presented, and found that the bulleted information style allowed for ease of comparison across tariffs. The Panel did express confusion over the need for repetition in the table, for example in the original version of the Label we included the tariff end date within the descriptor of the tariff and in a separate section. Customers also expressed a preference for pricing information to be displayed in £ per year terms, along with unit price information.

74. In summary, we concluded from this research that customers like the Tariff Information Label and want it to be presented in a clear table format, with unit price information, bills expressed in a £ per year figure and a removal of repetitive information where possible. Based on this, we agree that Ofgem's proposed Tariff Information Label is based on the correct principles.

75. There are, however, some practical points of implementation and presentation that we believe still need to be considered. In particular, it is important that we consider the format and presentation of the Tariff Information Label in light of the spacing and sizing of the Annual Statement, as the Label will be used on that Statement. At a practical level, it is key that the Label is able to fit on to the Annual Statement. We think that this might be a particular issue for customers with multiple rate meters, some of which can span up to 7 rates. The numbers of customers that this would impact is likely to be small, but we consider it important to address this. Perhaps a solution would be to design an alternative Tariff Information Label format for such customers, which would also translate more effectively to the Annual Statement.

76. We are comfortable with the presentation of estimated annual costs across the different consumption bands, but have a real concern about also including an estimated monthly amount. We feel that this has the potential to be confused with monthly Direct Debit amounts, which are unlikely in reality to be directly relatable to the monthly figure in the Tariff Information Label.

77. We feel that some of the explanatory information, particularly around the Tariff Comparison Rate is currently fairly weak and in isolation may not mean much to a customer. This will obviously form part of the wider consideration of the methodology and presentation of the TCR (see our comments below) and any other education or support for customers that accompanies the wider RMR remedies.

78. In terms of implementation, our biggest concern would be the interaction with the re-design of the Annual Statement and the practical challenges that this would present

for our new SAP system integration. As with all IT changes, a reasonable amount of time is needed

79. Overall, we support the approach to the Tariff Information Label and would be happy to agree to implement this format without the need for a Licence mandate. This would help to remove some complexity from the supply Licence, provided that all suppliers would agree to this approach.

Information on Bills

80. As with other information remedies, we understand and appreciate the rationale for prescribing the summary box on bills. We are however keen to ensure that this new requirement is appropriately specified and that it is accessible to customers, in order to deliver the benefits to customers that Ofgem envisages. We currently consider that the prescribed content and format of the bill summary box is too word heavy and therefore likely to deter some customers –potentially those that Ofgem most aims to target – from reading or engaging with it.

81. In its latest 'State of the Nation' report[37], the National Literacy Trust concludes that one in six people in the UK struggle with literacy, meaning that their literacy level is below that expected for an eleven year old. In addition, the Leitch Review[38] published in 2006, found that more than 5 million adults lack functional literacy, the level needed to get by in life and work. It is reasonable to assume that these are exactly the types of customers who are reluctant to engage in the energy market. As such, this must be an essential consideration in developing ways to provide information to customers, and to ensure that the presentation of information is accessible.

82. In the first instance, we know that consumers like clear, simple information, preferably presented in table or bullet form. This follows our feedback from customers on the format of our bills and statements and more recently on the Tariff Information Label tested through our Tell the Energy People Panel. We therefore consider that the text-heavy summary box should be reviewed, as it requires thorough reading for customers to understand the message, plus it runs the risk of making the front page of the bill appear more complex, which could cause customers some concern or distress. We would advocate a more modern, simple format and presentation, preferably in bullet form. We would also recommend that the tone of the messaging be reviewed, as it is currently negative, and unlikely to help foster trust in the messaging or with the supplier.

83. Beyond this, placement of information on the bill is important, to ensure that the main purpose and function of the bill does not get lost. We have made significant investment in designing and testing our current bill format in conjunction with customers, in order to ensure that the format and style works to help customers understand the primary messages – their account balance and what action they need to take. This investment has recently been recognised by Which?, who awarded ScottishPower the top score of 5 stars for billing and account management practices[39]. The Which? review found that ScottishPower stood out for the clarity of bills, particularly the way that key information was easy to find on the first page. We consider our bill to be a key interface between us and our customers, and we are

[37] Literacy: State of the Nation, The National Literacy Trust, January 2012
[38] Prosperity for all in the Global Economy – world class skills, Leitch Review of Skills, December 2006, Published by the Department for Employment and Learning
[39] http://www.scottishpower.com/PressReleases_2372.htm

keen to retain control over the content and format of this, to ensure that it remains clear and accessible to customers.

84. We understand that Ofgem feels it is appropriate to include particular information for customers on the bill and has attempted to take account of spacing issues in doing so. We think that much of the information needs to be accommodated together on the bill in order to provide the most value for customers. We are concerned that there is insufficient space on page 1 of the bill for this information to be grouped there, particularly in the case of a Dual Fuel bill, where much of the information for the customer would be doubled. Further, if the TCR is to be presented as a p/kWh figure, this will need to be clearly segmented from the specific unit rates and Standing Charges, to ensure that consumers are not confused by the varying messages on the bill.

85. We would therefore propose an alternative approach which focuses on principles rather than prescription and which would allow suppliers to present the information in a clear, well-spaced and accessible format, all in one place on the bill. Under this alternative option, the supplier would be required to put a clear, simple and prominent message on the front page of the bill directing the customer to where in the bill they can find the personalised information on what this means for them. The supplier could then present the information in that location on the bill, depending on their existing bill format, in a way that made it accessible for customers. We also believe that we should look for opportunities to simplify the messages to customers where possible, including presenting information to customers on a Dual Fuel basis where the customer has previously selected this option for account management.

86. This would mean that the customer has a clear prompt on exactly where the information is, it is in a consistent information across suppliers, so easily comparable, but will be presented with relevant information together and without fundamentally impacting supplier bills (the scale of which will depend on the customer's billing option and meter type) or the customer's existing account management choices.

<u>Annual Statements</u>

87. Similarly to the presentation of information on bills, we consider that care is needed around the level of text and presentation of information on Annual Statements, if it is to be accessible to a range of customers. In the example provided by Ofgem, all of the copy seems fairly small, meaning that again the statement format looks crowded and fairly text heavy. The example Statement looks to be set in Arial size 9 font – which is the size that we normally only use for caveats, which we consider to be too small. We would be keen to engage with Ofgem to develop a revised format that works in relation to customer needs.

88. We have the same concerns with the supplier cheapest deal information on the Annual Statement as with the bill, specifically the impact that this might have on our ability to deliver the Annual Statement to the customer.

89. In terms of the proposed content for the Annual Statement, this must obviously be considered in light of any further changes to the Tariff Information Label and Tariff Comparison Rate. We are concerned about the level of detail and prescription required to complete the bar chart for comparison purposes – this would appear to be increasingly detailed when compared to the consumption comparison graphs that already appear on the bill. These graphs in themselves are complex to produce, with a number of supporting rules to account for the a range of scenarios including where part or all of the period in question has been estimated or where the customer's

consumption has changed significantly over the period for comparison. We would appreciate the opportunity to discuss this in more detail with Ofgem at a practical level, to explain the dependencies and agree a suitable solution. For example, it is not clear how the information would be presented for a new customer where there is no consumption history.

90. Again in terms of content, we would appreciate guidance from Ofgem as to how data should be presented where the customer has an electricity meter with multiple rates – as this has the potential to significantly affect the prescribed format of the Statement. It is also notable that there is no reference to Green Deal charges at all on the current Statement draft. Adjustments will need to be made for these, in light of the new Green Deal Licence Conditions.

91. Beyond this, while we understand Ofgem's rationale for sending the Annual Statement as a standalone mailing, we estimate that this will create an additional annual cost on ScottishPower of around £600,000 for postage costs alone. This cost estimate excludes any system change costs and assumes that electronic versions of the Annual Statement for gas and electricity are sent to online customers, and that Dual Fuel customers receive the Annual Statement in the same envelope.

<u>Supplier Cheapest Tariff</u>

92. We are worried about our ability to deliver the supplier cheapest deal information easily on routine communications such as bills and Annual Statements, as we are not yet clear how this can be done at a technical level. In any case, we anticipate that this will be the most complex and costly of the information remedies to implement. Primarily, our fundamental challenge to implementing this requirement is a practical one. We consider that this scale of intervention to the format of the bill will need a wider review of our bills in our new SAP system, which will be restricted by the flexibility of the system during the migration process. We find the implementation timescales for this, specifically including the level of personalised information that needs to be provided to the customer, to be especially challenging. We consider that we would need at least 9 months from the date that the final Licence Conditions are confirmed to make changes to the bills and Annual Statements based on the level of prescription defined. And the more in-depth the rules that we need to implement, the more challenging this will be to implement in a reasonable time.

93. At face value, this information may appear to be relatively straightforward; however it is actually technically challenging to deliver within the billing system, due to the potential number of calculations that have to be completed in order to identify both the cheapest relevant and alternative tariffs for that customer and the savings amounts for each. We are currently investigating whether there are ways in which we can do this outside of the billing system, which may make this process less difficult from a technical perspective. To explain, if this is to be done within the billing system – which is the expected standard for bills and Annual Statements – it will involve having to generate more than 3 bill value calculations for each customer and then selecting the bill values from each of those bills to be used in the document going to the customer. At a practical level, this has the impact of increasing the time that it takes to generate bills, meaning that a number of bills may not be sent every day. We are currently carrying out extensive analysis in order to understand the impact that this is likely to have on the billing system.

94. The impact of these changes is likely to be lessened if the requirements are simplified. For example, if the personalised information was limited to one savings message, to only include details of the relevant cheapest tariff and to encourage the

customer to contact their supplier for details of other tariffs, this would be much quicker to implement and easier to manage.

95. We have identified two points relating to dual fuel tariffs that may require further consideration in the context of supplier cheapest tariff messaging. The first point is that suppliers sometimes choose not to offer certain tariffs on a solus basis (e.g. some of ScottishPower's tariffs are offered on a dual fuel or solus electricity basis, but not on a solus gas basis). We assume that there is no intention to restrict this commercial flexibility as part of the RMR proposals, in which case we would note that suppliers may need to caveat their cheapest tariff messages to explain that the quoted price for gas (say) is only available if purchased as part of a dual fuel bundle with electricity (i.e. with both gas and electricity on the same tariff). However, naturally, the more conditions that are attached to a message, the more caveats that need to be presented to customers. We are keen to ensure that messages to customers on this point are kept as simple as possible, in line with our concerns set out in paragraphs 80 and 81 above. We consider it is important to keep this as simplicity, so as to pique the customers' interest and encourage action. We do believe that any further explanation or savings opportunities can then be reviewed with the customer when they contact their supplier to explore realising those savings.

96. The second point is that a situation could in principle arise where, for a particular customer, the cheapest overall offer is gas on one tariff and electricity on another (assuming that each tariff was available on a solus basis). Under our current business model, this would not qualify for a dual fuel discount, and the customer would not enjoy the normal benefits of dual fuel account management (such as single bills, single direct debit, single account etc). We think this situation is very unlikely to occur, and if it did, the price difference is likely to be small, but the possibility needs to be considered. In such circumstances we can see two options: include the non-dual fuel combination in the supplier cheapest tariff message, with caveats to explain the implications for the customer (two separate bills etc); or respect the customer's existing account management preference and limit the cheapest tariff messaging to dual fuel tariffs. We think the latter approach is preferable and would accord with our own research into customer preferences. [40] (A further disadvantage of the former approach is that, if the customer opts for non-dual fuel tariff combination, they will then start receiving separate bills for gas and electricity and the supplier cheapest tariff messaging will no longer be able to alert them to dual fuel offers.) We would be wary of the potential for customer disruption or confusion from being forced to take separate bills and separate payment methods, when they have previously preferred to manage these as a single account.

97. We also think that the rules for presentation of the cheapest tariff information must be thoroughly assessed. We consider that it is inappropriate for example for a supplier to provide details of the cheapest tariff to customers on fixed price tariff, where this may mean moving to a variable price evergreen tariff. We know that customers who choose a fixed price tariff currently do so for the benefit of the tariff i.e. the protection from price increases for the duration of the offer. ScottishPower's own customer research[41] shows that only 17% of customers would never consider a fixed price product. Almost 70% of customers however considered that they would value fixing their prices for between 1 and 2 years. Where there is a cheaper version of that same tariff available, namely a tariff that offers the same benefits but at a cheaper

[40] Our ongoing Voice of the Customer research shows us that customers consider the option of a single bill for both fuels to be an important satisfaction factor in the service offering from their supplier.

[41] Source: YouGov Omnibus 1,765 (Respondents with joint or sole respondents for energy bills). Fieldwork 26-27th September 2012

price, it is sensible that the supplier should be required to make the customer aware of this. However, if a customer has actively selected to fix their prices for a period of time, we should be wary of encouraging the customer to make potentially poor decisions by switching from that tariff to a cheaper price that may rise again in the future. This point could possibly be resolved by an appropriate caveat, but this is another example of the issues associated with providing customers with this kind of information in isolation.

Tariff Comparison Rate

98. While we welcome the concept of the Tariff Comparison Rate, we think that establishing the correct methodology for calculating this will be vital. We are seriously concerned that the proposed methodology for calculating a national average may unfairly disadvantage suppliers who have a high proportion of customers in areas with high network costs, and may also provide a misleading ranking of tariffs for some customers.

99. We consider it would be more appropriate to use either a flat average or weighted average based on the total number of meter points in each region. This would achieve the same aims while eliminating the risk that suppliers will be placed at an unfair competitive disadvantage. Ofgem appears to be concerned that such approaches would be more open to gaming, but we consider that the risks of gaming are far less significant than the risk of challenge from suppliers who are placed at a competitive disadvantage. It must be recognised that it will be impossible to calculate a perfect national TCR; some level of approximation and risk of misleading some customes must be accepted. The alternative would be to look at a regional TCR, though there would then have to be simplifications about when and how it was used.

100. We also believe more thought needs to be given to how the TCR is to be presented and marketed to customers. Firstly, while we have no difficulty in preparing a TCR in a p/kWh format, we are not convinced that there would be sufficient differences in TCRs across similar tariffs to make any meaningful impact on consumers. We know that customers typically need to see savings of over £50 per annum to encourage them to switch. However, it is feasible, particularly if tariff prices do start to converge, that differences in gas TCRs become as little as 2 decimal places over average consumption, and customers may struggle to translate that figure into potential savings. It is more likely to be meaningful to customers if a TCR was presented as a £ per annum figure. This would also make comparisons with the personal projection more relevant.

101. We also believe that careful consideration must be given to the volume and scope of any supporting information that would need to be provided with the TCR. The current draft Licence Conditions suggest that a number of caveats and supporting explanation would be needed. A careful balance must be struck here.

Market Cheapest Deal

102. The Market Cheapest Deal pilot proposal does cause us some concern in terms of both the market implications of this approach and the practical challenges in managing such a scheme. We are conscious that this proposal is currently very much in the early stages and much further thought and discussion is needed as to how this could work. However, much of this depends on the way in which the scope and application of the trial will develop. We would welcome more insight from Ofgem on its intentions for the proposal.

103. As a general rule, regulatory interventions should seek to replicate practice in fully competitive markets, and we can think of no competitive market in which companies alert their customers to rival's cheaper prices. Ofgem is effectively asking suppliers to undertake the role of market intermediaries such as comparison sites, and such distortions of market behaviour carry a risk of unintended consequences. Furthermore, we can see significant practical implementation difficulties, and potential risks to vulnerable consumers. If Ofgem proceeds with a pilot, the target group should be narrowly defined to minimise distortions, and careful consideration should be given to the various practical difficulties.

104. We would note that a similar idea has been proposed as a potential remedy in BIS's current consultation on extending the civil enforcement remedies available to public enforcers of consumer law[42]. However the consultation notes the Courts are unlikely to be willing to impose such a remedy, due to the "difficulty in proving benefit to consumers".[43]. If the Courts are not prepared to impose such a remedy where a business has been found in breach of consumer legislation, it might appear disproportionate to impose the remedy where there has been no such breach.

105. However, more generally, we think that the biggest challenges with this proposal are the practical problems of implementing it. There are a number of practical questions that would need to be answered before any trial activity can be properly considered. This includes questions as to where the data to inform the advice for consumers would come from and who would be responsible for managing it. There is also a question as to who will be responsible to the consumer if the advice to the customer turns out to be inaccurate or misleading. The approach also seems to overlook the fact that customers have indicated through Ofgem's own research that they would be much more likely to rely on switching advice from an independent source.

106. Great care is required in defining the terms 'vulnerable' and 'sticky' customers. Customers who have not switched supplier, for example, may well have switched their tariff or payment method on more than one occasion, or indeed may simply be happy with their current supplier offering and level of service. And customers who fit the traditional definition of 'vulnerable' may not necessarily be in need of switching advice or may manage their account in a particular way for their own preference. Indeed, we should be particularly cautious of any approach which encourages customers to make a switching decision which could lead to a move that is not necessarily the best for the customer.

107. We are also concerned that there is an element of risk associated with this proposal, that vulnerable elderly consumers may be induced to switch to a small supplier for a modest saving and then lose out on any Warm Home Discount payments that they would have received with their previous supplier.

In view of the above points, any activity in this arena should be particularly focused on a tightly defined group of customers who are both vulnerable *and* 'sticky' and who are most likely to benefit from such advice. However, beyond this, we consider that a much more sensible, and manageable, approach would be to target broader switching reminders to these customers, with a signpost to reliable switching intermediaries, perhaps with example savings that could be available. This option will

[42] Civil enforcement remedies - consultation on extending the range of remedies available to public enforcers of consumer law, BIS, 5 November 2012
[43] Ibid, p22

have lower compliance costs and be much easier to manage on a practical scale, while still encouraging customers to think about switching options for themselves. We would also support the model proposed by DECC, where independent trained consumer advisors engage with those customers to provide a more rounded, valuable and holistic service for those customers including tariff advice.

Price Increase notifications

108. We are fairly comfortable with proposals in relation to the content and format of price increase notifications. We do feel that there is a good case to permit the sending of additional information with the price increase notification, provided that this is relevant to the content of the notification. For example, in order to better help customers understand the reasons behind our most recent price increase, we included an illustrative leaflet with more detail around the costs that resulted in the need to increase prices. This leaflet also included energy efficiency tips for customers who may need to consider ways to reduce their bills in light of the rising prices. Under the revised proposals, suppliers would not be able to provide additional helpful information for customers.

109. We do have a concern with the proposed changes to the right to cancel process which are not detailed in the consultation document but which are a feature of the draft Licence Conditions, namely the removal of the requirement on the customer to notify the supplier that they wish to cancel as a result of the price increase. We could understand Ofgem wishing to review this process where there is clear evidence that this process causes harm to customers. However, we have not yet seen such evidence. Indeed, our experience of the price change process suggests that most customers do not have difficulty with the current right to cancel process, including the requirement to notify their supplier that they wish to switch. We would welcome more detail on the evidence supporting this change. We are also not convinced that the increase in the switching window from 15 to 20 working days is necessary, nor that the current process is causing customers harm. All of these changes have an incremental effect on the potential lost revenue that suppliers have to account for, which will then have to be factored into the scale of the price increase.

End of Fixed Term period notifications

110. We are fairly comfortable with the proposed new information requirements within the End of Fixed Term period notifications and consider that most of this can be managed on this kind of communication fairly easily. We think, however, that in reality, the level of information that needs to be set out is highly detailed and this has the potential to make the Notification more complex if not managed correctly. We already consider that this will add an extra page of information in table format, which would have to be presented in size 8 Arial font in order to fit all of the information in to the Notification in the same number of pages. We are currently in the process of producing a ‘mock up’ of this new approach and would be happy to share this with Ofgem once available. We also dislike the proposed ‘Statement of Renewal Terms’ header and consider that this will not work for most customers, and indeed is likely to put some customers off from reading the information due to the legalistic tone.

111. We are again more concerned with the process issues that surround this change. We currently treat all ‘product maturities’ in the same way as we would if they were facing a unilateral variation to their contract terms. This means that we provide the customers with 30 days advance notice of the end of their fixed term period and tells them what happens next, what their options are and that they can switch supplier if they are unhappy.

112. Specifically, in relation to Ofgem's proposals we are not comfortable with proposals to extend the notification window to 42 days before the end of the fixed price period. For a decent sized product maturity of around 50,000 customers, this means that the Notification letters need to be drafted and sent for printing at least 4 weeks before the start of the 42 day window, in order to ensure that every customer receives the mailing on or about 42 days. This creates both a practical problem, in terms of knowing what relevant and alternative cheapest tariffs will be available at the end of the customer's current tariff, and runs the risk of the Notification becoming less relevant for customers, as they consider that the end date of the tariff is so far in advance that they don't need to do anything about it at this stage. There is also an operational challenge in honouring the previous tariff terms beyond the end of the term if the customer is switching supplier. We would strongly suggest that the endpoint of the window remains at 30 days in advance, or even that the Licence requires that the customer received the notification between 50 and 30 days before the end of the Fixed Term period.

113. The final potential impact of the revised process is that, based on the current draft Licence Conditions, this may preclude customers from signing up to an alternative fixed term tariff at the end of their current deal by telephone. This is because the draft Condition requires the customer to accept the terms of a new fixed term tariff in Writing. This would exclude the potential for customers to contact their current supplier for a tariff check at the end of their current deal and then take up a new fixed term tariff offered during that tariff check. We do not think that this is Ofgem's intention here, and this may be resolved by some drafting amendments, however we would appreciate clarity on this point.

Proposal 3 – Fairer Conduct

114. We fully agree that consumer trust will play a vital role in building better engagement within the energy market and we welcome the role that the proposed Standards of Conduct Licence Condition is likely to play in bridging the gap between the industry and its consumers. We welcome Ofgem's intention to drive an industry that engages with customers and provides a good service for a fair price. However, such a new approach will require innovation and imagination from both suppliers and Ofgem if it is to be truly successful.

115. The advantage of a principles based approach such as the Standards of Conduct is that it is flexible and adaptable and therefore more responsive to the customer need. We also welcome Ofgem's intention that it will take a 'step back' and that the focus of the Condition should be on the relationship between suppliers and customers, allowing suppliers to take the lead on applying and implementing the Standards of Conduct. However, we cannot overlook the fact that the underlying enforcement regime means that Ofgem retains the ultimate discretion over how the Standards will be enforced. This gives Ofgem a significant level of discretion around the application of the Standards 'after the fact.'

116. There remains a risk that longer term uncertainty over how individuals interpret the concept of 'fairness' will inhibit innovation, investment and new entrants to the market. This is particularly relevant in an environment where changing political focus means that the concept of what is considered 'fair' may vary widely. A Licence Condition with discretionary enforcement powers but without a clear set of rules for suppliers to follow is likely, in such an environment, to be perceived to create a burden of regulatory risk that deters new entrants from entering the market and

encourages larger suppliers to restrict innovation and development, in case this results in enforcement action. In order to realise the true benefits of the Standards of Conduct, confidence in the enforcement regime becomes vital.

117. We would prefer a 2-stage enforcement regime to support any principles-based Licence Condition, as we believe that this would help to balance the risk outlined above. Under this approach, which would be underpinned by Licence, Ofgem would have a dialogue with affected suppliers in the first instance. This would allow the supplier or suppliers the chance to make representations and justify their approach, or rectify the behaviour as appropriate. If evidence exists of consumer harm after this, Ofgem could move to a formal enforcement investigation. We think that an appropriate two-stage regime could be enshrined in Licence specifically for the Standards of Conduct, therefore not fettering Ofgem's discretion in any other areas. Ofgem could retain the right to take immediate enforcement action in exceptionally serious cases.

118. We appreciate that Ofgem has proposed a bespoke enforcement approach as an alternative to the two stage enforcement previously requested by suppliers. While the proposed bespoke enforcement procedure goes some way to allay concerns, which we appreciate, it does not eliminate the significant potential for subjective application of the Standards and therefore retains a level of regulatory risk which could inhibit innovation and discourage market entry.

119. A Standards of Conduct-type approach is not one that is unique to energy, although in other markets it is not an approach that is supported by such an absolute enforcement regime. We would therefore be keen to explore Ofgem's proposed bespoke enforcement process further with Ofgem, and in particular to consider the other tools that may be used in addressing potential breaches of the Standards of Conduct. In other industries, such as with the Health and Safety Authority or Financial Services Authority, such approaches have been put to great effect to protect customers where regulators and the regulated providers can work together to ensure that the aims of the requirements are met.

120. Primarily, we would expect Ofgem's bespoke enforcement process to be the subject of a separate consultation and clearly enshrined in a document that binds Ofgem in its application. It will be important in this process for the procedure to provide suppliers with confidence that Ofgem will take a consistent and proportionate approach to applying the Standards. In particular, the Standards are a much more high level approach to regulation than the traditional rules and therefore should be incompatible with an automatic 'tick box' approach to compliance. Therefore, Ofgem's approach to the bespoke enforcement regime needs to reflect this just as much as supplier approaches do.

121. We would also expect that Ofgem would clearly set out in its bespoke enforcement procedure how the Standards of Conduct relate to the other, more prescriptive Licence Conditions. For example, when a supplier has implemented a process or practice with the intention of complying with a particular Licence Condition, this should not therefore be subject to scrutiny under the Standards of Conduct.

122. This approach would also help to make the Standards more manageable for both industry and Ofgem as the regime develops, by mitigating some of the regulatory risk that might otherwise dissuade suppliers from truly taking ownership of the Standards of Conduct. For example, there would be value in developing an independent assessment or appeal panel which could review cases from an independent

perspective against the ‘reasonable intention’ test that Ofgem is proposing. We also think that there could be value in exploring the potential for translating the Standards into outcomes for customers enshrined in Licence, For example, a key outcome would be that customers are provided with clear, understandable information from their supplier. Another key outcome would be that customers are always provided with a service that is focussed on the needs of customers. This would replace the current draft Licence Conditions to provide a better focus on Ofgem’s aims and we think that this would also help to encourage the innovative and individual approaches from suppliers that Ofgem is seeking to achieve and would be a manageable way for the Standards to be enshrined in Licence.

123. This is not to say that we expect Ofgem to leave suppliers to have to decide for themselves, without assistance, what types of behaviour are acceptable or not. Indeed, drawing on the experience of the FSA as an example, while suppliers are responsible for achieving the outcomes of the Standards of Conduct, Ofgem should also be responsible for providing suppliers with ongoing guidance and support in implementing the Standards. And while the Standards are high-level by nature, this does not mean that they cannot be clearly drafted and easy to understand. Ongoing engagement with suppliers on the practical application of the standards would also help both Ofgem and suppliers to understand how they are working for the benefit of consumers, and indeed could assist in making this more transparent to customers as part of the drive to rebuild trust in the market.

124. We would also be keen to explore further the test that Ofgem intends to apply, specifically whether a reasonable person applying the Standards of Conduct would have taken the action that the supplier did. We consider that this may place an impractical standard of compliance on suppliers by using the benefit of hindsight to assess the suitability of a particular course of action. Instead it would be more appropriate to consider whether in acting the way it did, the supplier would be considered by a reasonable person (without the benefit of experience) to have attempted or intended to have complied with the Standards. We consider that, while it may be a subtle difference in interpretation, this is a more reasoned and practicable approach to enforcement, which would help to provide more clarity and certainty to suppliers in applying the Standards.

125. Overall, we consider the Standards of Conduct to be a worthwhile approach, but one which requires a completely different attitude to management and application from both suppliers and Ofgem. We think that much can be learned from the approach of both the FSA and industry participants in that regard. In terms of the cost impact of the Standards of Conduct, it is too early for suppliers to be able to assess this. We consider that the cost of implementation will be materially impacted by the approach to enforcement and the final drafting of the condition.

126. In this context it would be very helpful, whatever the enduring enforcement governance, for Ofgem to have a period of “soft” enforcement long enough for all parties to understand each other’s expectations.

127. Finally, the draft licence condition defines fair as follows:

> “25B.3 For the purposes of this condition, the licensee or any Representative would not be regarded as treating a Domestic Customer fairly if:
>
> (a) their actions or omissions significantly favour the interests of the licensee; and
>
> (b) give rise to a likelihood of detriment to the Domestic Customer.”

We would suggest that the word ‘undue’ should be inserted before ‘detriment’, to make it clear that not all actions which may cause detriment to the customer (such as disconnection for theft) are necessarily unfair. Blocking a transfer due to debt (in accordance with the rules) would benefit the supplier and be detrimental to that particular customer, but ought not to be considered unfair within this context.

Annex 2

RETAIL MARKET REVIEW DOMESTIC PROPOSALS
SCOTTISHPOWER ANSWERS TO CONSULTATION QUESTIONS

Chapter 2 Why the market needs reform

2.1: Do you agree with our characterisation of the problems in the retail energy market?

We disagree with many aspects of Ofgem's diagnosis, particularly with regard to the effectiveness of competition. For example, claims that suppliers are focused on retaining customer numbers at a steady level to keep generation and supply demand at equilibrium, and that suppliers seek to avoid competing on price to gain customers are contentious and unsubstantiated.

2.2: Do you agree with the findings of our evidence base?

No. As above, while we accept that there are issues of trust and disengagement within the market, we do not agree that the findings of Ofgem's evidence base are necessarily correct. See our response in Annex 1 for more details.

Chapter 3 Rationale for our package

3.1: Do you agree with our rationale for the proposed RMR package?

While we may not agree with Ofgem's characterisation of some of the issues in the market, we appreciate that there are problems that the RMR is designed to address.

3.2: What are your views on the proportionality of the proposed RMR package in the light of the evidence we have presented?

We think that the RMR package is generally proportionate to the concerns seen in the market, but with certain exceptions. For example, we think the tariff restrictions are likely to have an adverse overall impact on competition and are therefore not proportionate.

We are also concerned that some of the detail proposed, for example around the level of information to be provided on cheapest tariff messaging, could be disproportionate if not managed correctly.

We consider the Market Cheapest Deal pilot proposal to also be a disproportionate reaction to the issues seen, as it seems to go beyond the aims of encouraging increased customer engagement and could create unintended market distortions.

3.3: Do you agree with our reasons for not proceeding with the alternative options set out below?

Yes.

Chapter 4 Tariff simplification

4.1: Are our rules to reduce the number of tariffs appropriate? Have we set the cap on core tariffs at the right level? Should a different cap be set for time of use tariffs? What derogations from our tariff cap would be appropriate?

We think the tariff cap should be set at five core tariffs rather than four. This would allow for innovation and address some of the risks to competition that we think will come from suppliers withdrawing special offers under a reduced cap.

We think it essential that the tariff restrictions are subject to a sunset clause. There is a wide range of opinion as to the likely consequences of the restrictions, and if it turns out that they have an adverse impact on competition, a sunset clause will help avoid the situation where they are overlaid with yet more regulation when the correct course would be to remove them.

4.2: What surcharges should suppliers be able to offer without this counting as an additional core tariff, and why? How could these be defined in a licence?

We consider that Ofgem has broadly captured the range of surcharges that suppliers should be able to offer outwith a 'core tariff.' This should include charges that are largely dependent on customer behaviour or additional services that are not exclusive to that tariff. Particularly we think that this should include late payment charges and debt follow up charges, additional metering charges and charges for replacement payment devices such as prepayment keys.

We think it is important that the Licence does not dictate how these are applied to customer accounts (e.g. on a daily basis) or presented (i.e. as an annual amount), as the nature of these charges means that they will generally never be capable of being presented as an exact annual amount to that customer.

4.3: Are our rules to simplify tariff structures and discounts appropriate? Should they only apply to open tariffs or be extended to cover dead tariffs too?

Generally speaking we consider the rules to simplify tariff structures and discounts are appropriate. We think that it is most appropriate that these are defined to apply to open tariffs only. Otherwise, applying these rules to dead tariffs will mean applying a unilateral adverse contract variation, which is likely to cause a natural level of customer concern. In this case it will be important for suppliers to ensure that customers fully understand the reason for the variation.

4.4: What categories of dead tariffs should be derogated from our proposals, if any? Are any other measures required to avoid any consumer harm?

We cannot see a strong rationale for derogations for any dead tariffs at this point in time. The only exception may be for preserved meter tariffs in some areas, however we consider that the number of affected customers is likely to be small.

4.5: What would be the implementation issues and costs of our proposals?

We are in the process of providing a fuller estimate for the purposes of the costs and benefits information request.

4.6: Is our proposed timeframe for implementation appropriate?

It is difficult to comment conclusively on plans for implementation until the timetable is known. Such changes are unlikely to be implemented in isolation and the timescale for delivery will be entirely dependent on the scale of change, complexity of solutions needed and the date of confirmation of the final Licence Conditions. We appreciate that Ofgem has tried to take this into account in suggesting implementation timescales, but we consider that these to be challenging.

Chapter 5 Clearer and simpler information

5.1: What are your comments on the degree of prescription proposed, and on the design of the documents and messaging?

We think that it is right that there is a level of prescription in some documents, such as the Annual Statement, and we are comfortable with this. However, we strongly believe that suppliers should be allowed to continue to develop their own bill format in conjunction with what their customers need, and therefore significant prescription is not appropriate in this area. Instead, we consider that clear rules that allow suppliers to have some flexibility in the presentation of information are appropriate.

We think that the draft designs are currently fairly text heavy and 'clunky' in format. We don't consider that these are particularly inviting or accessible to customers. The designs therefore run the risk of dis-engaging some customers, particularly those with less developed literacy skills.

5.2: What are your views on the appropriateness of content requirements for each of the communication channels?

We broadly consider that the appropriate information is in the appropriate place for each communication channel.

However, we do have concerns about including both the relevant cheapest tariff and alternative cheapest tariff information on all communications, particularly bills and statements. In most places, this provides an extra level of information to customers and has the effect of making the information look more detailed and 'busy.' We would suggest that providing the relevant cheapest tariff with more details of how to find the alternative cheapest tariff would be most appropriate.

5.3: Should Ofgem explore further ways in which suppliers might increase the effectiveness of online/paperless communications?

We think that this is an issue for each individual supplier in conjunction with their own customer needs.

5.4: Should Ofgem consider making further recommendations, or issuing best practice for enhancing the impact of Annual Statements by looking at messaging and co-branding of envelopes?

We don't think that further recommendations are necessary specifically in the formatting or sending of Annual Statements. We do not support the co-branding of envelopes, primarily because we can only use one envelope design for all bills and Annual Statements – therefore an Ofgem brand would have to be used on all envelopes.

We do think that a broad information and education campaign should be considered in order to ensure that customers are aware of, and looking out for, their Annual Statement (and therefore may be more likely to remember receiving it).

5.5: Do you agree with the view additional contractual information can be included on an additional page on the Annual Statement?

We think it is appropriate to give suppliers freedom to provide this where appropriate. We think that more thought will need to be given to the formatting of the Annual Statement, in relation to customers with multi-rate meters, for example, as the formatting of the Statement does not currently seem to consider this scenario.

5.6: What are your views on the classification of dual fuel for the purposes of the template designs?

We strongly believe that customers who have selected a Dual Fuel service offering should be given information on a Dual Fuel basis going forward. We don't think it is appropriate, or helpful, to provide separate gas and electricity information on a Dual Fuel bill or Annual Statement.

5.7: What are your views regarding including energy efficiency advice in Annual Statements?

We consider that this should not be a mandatory requirement, given the full content of the draft statement. However, it would seem sensible that suppliers are given the option to provide such information in future, particularly as we move into a market with Green Deal and Smart options.

Chapter 6 Supplier cheapest deal

6.1: Do you agree with our view that the cheapest tariff message should include both supplier's cheapest tariff for their payment method, consumption and meter type, and the cheapest overall tariff from their supplier irrespective of their current circumstances, personalised by consumption?

No, we think that the cheapest tariff rules should be simplified as much as possible. We think that the personalised savings information should be limited to one savings message only. This should include details of the relevant cheapest tariff (narrow definition) and encourage the customer to contact their supplier for details of other tariffs. This would be much quicker to implement and easier to manage. We also believe that greater consideration needs to be given to the customer's existing account management preferences in creating these rules. For example, where a customer has selected to manage their account on a Dual Fuel basis, messaging about cheaper tariffs should reflect this, both to make this simpler for suppliers to implement and to reflect customer's existing service preferences.

6.2: Do you agree with the approach to tariff eligibility criteria proposed for supplier's cheapest tariff?

We don't agree that both relevant and alternative cheapest tariff information should be provided in the majority of cases, due to the complexity of change needed to implement this. Beyond this, the rules for presentation of the cheapest tariff information must be thoroughly assessed. We consider that it is inappropriate for a supplier to provide customers on a fixed price tariff with details of a cheaper variable price evergreen tariff.

6.3: We seek views from stakeholders on whether consumers with smart meters and any relevant time-of-use tariffs that the supplier is offering require separate consideration in relation to this policy proposal.

Yes, we are not convinced that the tariff rules will easily accommodate TOU tariffs, particularly as TOU tariffs may require a supplier to understand a customer’s daily or hourly consumption profile in order to be able to recommend the cheapest tariff.

6.4: Do you have any suggestions regarding additional rules which they consider relevant for the construction of the cheapest tariff messaging?

No

Chapter 7 The tariff comparison rate

7.1: Do you agree with our proposal to introduce a price comparison tool?

Yes, we agree with the concept. We do think that the proposed methodology would benefit from rigorous testing, both independently and with customers.

7.2: What is your view about the terminology we are proposing for the two price comparison metrics? Are they clear and easy for consumers to understand?

We think that customers will need some clear education on the concept but ultimately the terminology seems fairly straightforward.

7.3: In your view, does our proposal for the TCR strike an appropriate balance between different trade-offs in terms of simplicity, accuracy, confusion and saliency? Please explain the reasons for your view.

We strongly object to the current proposed methodology since it will place suppliers at an unfair competitive disadvantage who have a high proportion of customers in areas with high network costs, and may also provide a misleading ranking of tariffs for some customers.

7.4: Do you agree with our proposal for the different features of the Tariff Comparison Rate, and our related proposal on the personal projection? Do you have any thoughts on whether and how time of use tariffs should be accommodated in the TCR and personal projection? Please explain the reasons for your view.

We think that the TCR would be better presented as a £ per annum figure for better comparison between tariffs, and also to allow consumers to better relate this to the personal projection. We consider it would be more appropriate to use either a flat average or weighted average based on the total number of meter points in each region. An alternative (which would require changes in how the TCR is used) would be a regional approach.

7.5: In your view, should suppliers be required to make available up to date information on TCRs for their tariffs? What is your view on the barriers to the publication of best buy tables, and how could we better facilitate publication by third parties?

We think that the biggest barrier to the presentation of the TCR is the number of iterations for each tariff and the caveats needed to support each of these. We don’t currently see that a TCR in isolation will be effective – however, similarly, too many caveats will put customers off from engaging with the TCR.

Presentation of the TCR in p/kWh is also likely to show very small variances between tariffs at each consumption level, which may mean that consumers see very little differences in the TCR at a practical level. We think that presentation in £ per annum is much more likely to help show potential savings available and create a 'real' reference point for consumers, making it more likely to be used in best buy tables.

7.6: Do you have any concerns regarding the implementation of this proposal? How long after a decision has been made would you take to implement this proposal? What drives those timescales?

We do not consider that this proposal would be particularly difficult to implement for new tariffs going forward, assuming that a suitable methodology is agreed. We would be concerned about the ease of implementing a TCR for all existing tariffs and believe that this would be particularly time consuming and difficult to achieve. The biggest challenge overall will be the system changes needed to capture the TCR in the billing system and then represent that on the bill and Annual Statement.

Chapter 8 Standards of Conduct for domestic consumers

8.1: Do you agree that the revised Standards of Conduct (SOC) will help achieve our objectives?

Yes, we generally support the Standards of Conduct and think that, provided that they are given appropriate time to 'bed in' across the industry, these can help achieve Ofgem's objectives. The development of trust between Ofgem and suppliers will also be important in achieving this success.

8.2: Is there a different name for the SOC that will have more meaning to consumers and can be used by stakeholders across the industry?

We think the term 'Standards of Conduct' is fairly self explanatory. However, an alternative may be to focus the principles on achieving outcomes for customers, under the broader heading of 'Treating Customers Fairly.' This approach has already been adopted in Financial Services.

8.3: Does our approach to enforcement mitigate stakeholder concerns about clarity and regulatory risk?

We welcome the fact that Ofgem proposes to develop a bespoke enforcement process for the Standards of Conduct, and this may well mitigate some concerns about clarity and regulatory risk, provided that the processes is clearly documented and publicised. We do not think that this addresses the concerns to the same extent as a 2 stage enforcement regime would. In any event, an initial period of soft enforcement, to enable all parties to gain confidence with the new approach, would be very helpful.

8.4: Do you have any information regarding potential costs this may impose on suppliers?

It is difficult to assess the potential costs of compliance for such a new concept within the current enforcement regime. However, we do consider that the greater the level of subjectivity that is allowed to develop, the greater the regulatory risk and therefore the greater the compliance costs. We think that this will also hinder the potential for future market investment and innovation, which would be a significant cost.

Chapter 9 Protecting consumers on fixed term offers

9.1: Do you agree with our proposal for rules to be applied to fixed term offers in the domestic retail market?

We agree with the proposals to prevent customers from automatically rolling on to another fixed term tariff at the end of a current fixed price period. We do not consider that the 42 day switching window is necessary or appropriate for fixed term customers. Instead we consider that applying the same process as applies to unilateral variations (30 days advance notice) is appropriate and consistent and strikes the right balance between the practical process of communicating with customers and providing protection for customers.

We do not think it is in the best interests of consumers for Ofgem to prohibit tariffs with a time limited fixed discount relative to the supplier's standard tariff. Such tariffs can help reward switching and may have wider societal benefits (such as our Help Beat Cancer tariff). We see no reason why such introductory fixed discounts should be incompatible with consumer protection legislation, nor do we consider that a prohibition is a proportionate response to the risk that some customers may misunderstand them. In any event, customers on such products are unequivocally better off than customers on a standard product, receiving a cheaper price for a defined period of time, subject to the same protections if prices increase.

9.2: Do you agree with our proposed strategies to mitigate concerns regarding increases in network charges?

We appreciate the measures that have been designed to improve the predictability of allowed network revenues and proposals to consider potential improvements to charging methodologies. As consumers develop a better understanding of the market, there may in future be an appetite for 'pass through' tariffs in which changes in externally driven costs such as network charges can be automatically reflected in the tariff. It will also be important to consider the impacts of other costs, such as social and environmental costs, on the bill.

9.3: Is 30 days the appropriate notification period for mutual variations? Should there be any exceptions to our proposals for mutual variations (e.g. direct debit amount variations)?

30 days would appear to be an appropriate notification period for mutual variations initiated by a supplier.

We do not consider that direct debit amount variations would equate to a mutual variation in this context, since that by agreeing a direct debit payment plan, the customer agrees to the direct debit rules, as governed by Direct Debit scheme. The very nature of direct debit is that the amount can be varied in accordance with the guarantee, provided that the customer is given 10 days advance notice of this. Requiring Direct Debit amount variations to be treated as a mutual variation would make this payment method much more expensive to operate, necessitating price increases.

9.4: Are there any expected implementation issues or costs associated with this proposal?

Yes, we consider that there will be. We are in the process of providing a fuller estimate for the purposes of the costs and benefit information request.

9.5: Do you agree with our proposed timetable for implementation of our proposal?

It is difficult to comment conclusively on plans for implementation until the timetable is known. Such changes are unlikely to be implemented in isolation and the timescale for delivery will be entirely dependent on the scale of change, complexity of solutions needed and the date of confirmation of the final Licence Conditions. We appreciate that Ofgem has tried to take this into account in suggesting implementation timescales, but we consider that these to be challenging.

Chapter 10 Market Cheapest Deal

10.1: Do you agree that we should trial a Market Cheapest Deal initiative?

We have concerns about the proposed 'market cheapest deal' pilot. As a general rule, regulatory interventions should seek to replicate practice in fully competitive markets, and we can think of no competitive market in which companies alert their customers to rival's cheaper prices. Ofgem is effectively asking suppliers to undertake the role of market intermediaries such as comparison sites, and such distortions of market behaviour carry a risk of unintended consequences. Furthermore, we can see significant practical implementation difficulties, and potential risks for customers, such as the loss of Warm Home Discount benefits of up to £140 by moving to a small supplier. If Ofgem proceeds with a pilot, the target group should be narrowly defined to minimise distortions, and careful consideration should be given to the various practical difficulties.

10.2: Do you consider there are other approaches we should consider to address the particular issues with engaging sticky and/or vulnerable consumers? If so, what are they?

In the first instance, we believe that the focus should be on customers who are both sticky and vulnerable, as customers who have not switched supplier for a defined period of time are not necessarily facing harm or disengaged from their supply (as they may be happy on their current tariff or have switched tariff within their supplier. We consider that targeting these customers through relevant community groups or consumer champions is more appropriate (as is proposed in DECC's 'Ensuring a better deal for energy consumers' consultation), in that customers who are vulnerable or reluctant to engage in the market might be better supported by a more holistic package of help – and are more likely to trust independent advice in this area.

10.3: Would you be willing to work with us in conducting the trial?

We remain uncomfortable with proposals that would see us writing to our customers to tell them about other suppliers' products. However, it is obviously important for us to understand more about Ofgem's proposals as they develop. We would have serious reservations about participating in a pilot unless our major competitors were also involved.

ScottishPower
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