Making a positive difference
for energy consumers

To all retail energy market participants, price comparison websites, consumer groups and other interested parties

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Dear Colleague

Decision: New typical domestic consumption values

This letter presents our final decision to update the Typical Domestic Consumption Values (TDCVs) in line with recent evidence of a sustained fall in domestic energy consumption.

Ofgem, suppliers and price comparison sites often use TDCVs to quote the annual electricity and gas bills of a typical domestic customer. These bill values are frequently quoted in the media. As such, they influence consumers' perception of the cost of energy, even if the amount individual customers pay is different. These values can influence customers' switching decisions. Elements of the TDCVs will also form the basis of the Retail Market Review's (RMR) Tariff Comparison Rate (TCR) [1] and Tariff Information Label (TIL). We intend to confirm these arrangements before the relevant new RMR licence conditions are in force.

We therefore aim to ensure that estimates of the TDCVs are both representative of typical domestic consumption and broadly stable over time to provide a degree of certainty. To that end, in May 2013 we launched a review[2] to determine whether the evidence of falling domestic consumption warranted an update of the TDCVs. The data confirmed a downward trend, especially for domestic gas consumption. In July we consulted[3] on our proposal to reduce the TDCVs. The consultation also included a proposal to establish a transparent framework for future updates.

Our proposal

As set out in our consultation, we view the need to make these figures representative of domestic consumption and broadly stable over time as the two key principles underpinning the TDCVs.

We consulted on a proposal to estimate future TDCVs using the average of the latest two years of available consumption data (ie 2010-2011).We believe this strikes the right balance between not relying too much on a single year's observation in order to reduce the impact of erratic consumption years. At the same time, it did not depend excessively on past years' data, which may not be representative of current consumption given the falling trend.

[1] Single metric to allow consumers to compare tariffs more easily.
[2] https://www.ofgem.gov.uk/ofgem-publications/39337/review-typical-domestic-consumption-values.pdf
[3] https://www.ofgem.gov.uk/ofgem-publications/74735/tdcv-review-consultation.pdf

We further proposed to establish a transparent framework for updating the TDCVs every two years, with the objective of keeping them representative of typical domestic consumption and minimising the burden of revision on relevant stakeholders. Specifically, we proposed to assess domestic consumption every two years and revise TDCVs if the latest consumption data results in different TDCVs given the current approach of rounding to the nearest 100 kWh for electricity and 500 kWh for gas.

We considered this approach to be appropriate for the current environment which is characterised by falling consumption and uncertain future demand.

Decision

A summary of responses to our consultation is set out in an appendix to this letter. After full consideration of the responses received, we have decided to proceed with our original proposal. Therefore, we will:

- Derive typical low, medium and high domestic consumption levels for gas and electricity by averaging the two most recent median[4] consumption values; and,

- Assess domestic consumption every two years and revise the TDCVs if the latest consumption data results in materially different values. Material in this context means changes to the TDCVs of at least 100 kWh for electricity and 500 kWh for gas when rounded.

In our view, the above options result in TDCVs that are representative of typical domestic consumption and likely to be broadly stable over time. Furthermore, this decision reflects the preferences of most of the stakeholders who responded to our consultation.

Our final TDCVs result in an annual bill of £1,129 for a typical dual fuel "medium" customer paying by direct debit.

The table below presents the updated TDCVs.

Updated TDCVs and the impact on the typical bill

kWh	Level	Current TDCVs	Revised TDCVs	Difference in reporting the typical bill*
Gas	Low	11,000	9,000	-£84
	Medium	16,500	13,500	-£127
	High	23,000	19,000	-£169
Electricity: Profile Class 1 (single rate meters)	Low	2,100	2,000	-£14
	Medium	3,300	3,200	-£14
	High	5,100	4,900	-£27
Electricity: Profile Class 2 (multi rate meters)†	Low	2,900	2,700	-£22
	Medium	5,000	4,600	-£45
	High	8,300	7,800	-£56

* Annual bill for a typical customer on a standard tariff as of September 2013 paying by direct debit. The standard tariff we use is the average of the six largest energy suppliers' standard tariffs.

† We used a 45/55% assumed day/night split. We expect to review this split in 2014. The new Profile Class 2 TDCVs are based on temperature adjusted consumption data.

[4] The first, second and third quartiles (the median being the second quartile) will be used to represent the consumption of a low, medium and high typical domestic customer, respectively.

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Supply Market Indicators

As part of this consumption review we also looked at the consumption assumptions used in our Supply Market Indicators (SMI). These estimate a forward-looking snapshot of bills, costs and margins in the retail energy market. We are updating these assumptions as of today to reflect the same consumption trends that underpin our revised TDCVs.

The consumption assumptions we use in the SMI are different to the TDCVs. For the TDCVs we use median consumption. Our aim is to focus on what a typical consumer uses, so we do not take account of people who use very large or very little amounts of energy. For the SMI we are looking at the overall trend in the relationship between wholesale prices and retail prices. We therefore need to take account of very high or very low users in order to get a representative figure. This is why we use the mean.

We have included more detailed information about this update on our SMI webpage.

Next steps

We expect the industry to use the new TDCVs from 1 January 2014. The current TDCVs will remain in place until then. This should allow stakeholders enough lead time to embed the new values and provide for consistency in the information to consumers.

We will complete the next assessment of the TDCVs in the first half of 2015. This will use 2013 consumption data, which we expect DECC to make available in December 2014.

If you have any questions on the contents of this letter, please contact Diego Villalobos, in the Energy Market Monitoring and Analysis team, at diego.villalobos@ofgem.gov.uk or on 020 7901 1846.

Yours sincerely,

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Appendix: Summary of stakeholder responses

We received eight responses to our consultation. These are available on the Ofgem website. There was broad support for reviewing the TDCVs and for our proposed updated values.

The consultation asked whether respondents agreed:

- with the options presented for calculating updated TDCVs
- with our recommended framework for future updates of the TDCVs
- that our proposals strike an appropriate balance between having TDCVs that are representative of current consumption and providing broad stability over time.

Regarding the options for calculating TDCVs, there were mixed views but most respondents broadly supported our approach. Specifically, three unambiguously agreed with our proposed approach (Option 2). One preferred a hybrid approach between Option 1 and Option 2; two expressed mixed support for Option 2 and Option 3; one preferred Option 3 and the last one did not comment specifically on ways to calculate TDCVs.

One respondent suggested using one year's data unless weather has been sufficiently unusually (warm or cold) such that a two year average would be necessary to smooth its effects. While we see the appeal of this approach – providing the most up-to-date measure of consumption – it would require Ofgem to determine whether a particular years' consumption was erratic. To do this properly, we would need to consider other drivers of consumption beyond weather, such as the economy or other social trends, which would introduce a degree of subjectivity to the process and the estimates. We therefore favour our proposed approach of taking the average of the latest two years of available consumption data as it is a more objective and transparent way to calculate TDCVs.

The respondents that recommended basing consumption over more than a two year period argued that it would make the estimates more robust. It would reduce the risk of anomalies, which may arise for example from a series of unusually cold winters, which could skew the data and result in higher TDCVs. We recognise that in general, more years makes estimates more robust. However, we remain of the view that given the declining trend in consumption, including many years makes the estimates less representative of current consumption. Furthermore, the gas data we use is weather corrected and the Profile Class 2 electricity data we use is temperature corrected, which should address to an extent any weather driven consumption anomalies.

In relation to our recommended framework for future updates, five respondents agreed with our recommended two year frequency under Option B, while two preferred consumption to be assessed every year instead. One respondent did not express a preference on the frequency of updates.

Those respondents recommending an annual assessment cited TDCV accuracy as the key benefit. One explicitly though it outweighed the administrative costs. One respondent said that revising TDCVs was not likely to be as burdensome as Ofgem suggested. Another thought it was desirable to provide reasonable stability, particularly as the RMR will broaden the range of systems and processes which incorporate the data.

Respondents also raised additional important issues, which we fully considered. These are the issues and our response:

1. *Weather adjustment for Profile Class 2 electricity consumption*: three respondents argued that Profile Class 2 electricity consumption data should be weather corrected. This is because consumers with these meters tend to use electricity for heating. We agree. Therefore we have adjusted Profile Class 2 electricity consumption data using a ten year temperature correction factor sourced from Elexon. The adjustment resulted in slightly lower TDCVs for "medium" and "high" consumers from those proposed in the consultation (4,600 kWh down from 4,700

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kWh and 7,800 kWh instead of 7,900 kWh). We propose to do a similar adjustment in the next domestic consumption assessment.

2. *Link with SMI consumption assumptions*: two respondents noted that the SMI should use the same values as the TDCVs as this consistent reference would minimise confusion. We decided to continue with the current approach, for the reasons outlined above, namely that the SMI needs to capture the very high/low domestic energy users, as their consumption may impact on suppliers' bills, costs, and therefore margins. On the other hand, the TDCVs aim to be representative of the typical consumers' usage. We therefore calculate them based on *medians*, as this measure is more representative of the typical consumer than the *mean.*

3. *Rounding thresholds*: three respondents argued for lower rounding thresholds of 250 kWh for gas and 50 kWh for electricity. We propose to keep the current roundings of 500kWh for gas and 100kWh for electricity on the grounds that these thresholds are more consistent with our stability objective, as only material changes to consumption would result in updated TDCVs. The maximum deviation with our preferred thresholds is around £17[5] on a typical dual fuel annual bill of £1,129 or about 1.5% of the bill. We do not view this as significantly affecting our other objective of representative TDCVs. Furthermore, our preferred thresholds are unlikely to mislead switching decisions based on at-a-glace comparisons, since most consumers on average report that they require a much higher expected saving to switch[6].

4. *Day/night split for customers on Economy 7 tariffs*: three respondents noted that Ofgem has not provided a percentage split between day/night consumption for Profile Class 2 electricity consumers, and would like us to do so. We will not stipulate a split as part of this review. However, such a split will be needed to calculate the Tariff Comparison Rate for time of use tariffs. We expect to work with industry in the coming year to develop the methodology.

5. *"Fuel Poor Discount" consumption*: one respondent noted that the consumption level used to calculate the "fuel poor discount"[7] was different from the proposed gas TDCV (19,000 kWh vs 13,500 kWh). We will consider this as part of our review of the fuel poor extension scheme next year.

[5] For customers on standard tariffs as of September 2013 paying by direct debit.
[6] https://www.ofgem.gov.uk/ofgem-publications/74756/customer-engagement-energy-market-tracking-survey-2013.pdf. Those who report never having switched (62 percent for both gas and electricity) and who are able to give a numerical estimate consider they would need to save a minimum of £153 a year on average by switching supplier to be encouraged to do so. Those who report having switched supplier in the past (38 percent for both electricity and gas) and say that saving money was a motivating factor report they expected to save £195 a year on average the last time they switched supplier.
[7] The "fuel poor discount" is applied to the gas connection charge of fuel poor households, so they can more cheaply connect to the gas network. Gas is usually a cheaper source of space heating energy than its conventional alternatives, so it can help alleviate fuel poverty.

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