



Making a positive difference
for energy consumers

To all domestic electricity and
gas suppliers, consumer groups
and other stakeholders

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Implementation of Standard Licence Condition 32A: Power to direct suppliers to test consumer engagement measures – decision to make licence modifications

Dear Colleague

This letter notifies stakeholders of the Gas and Electricity Markets Authority's (the Authority¹) decision to proceed with modifications to the gas and electricity supply licences by inserting new standard condition 32A ('SLC 32A') which gives Ofgem the power to direct suppliers to test consumer engagement measures. The effective date for these modifications is on and from 00:00 on Monday 27 March 2017.

On 19 October 2016, we issued a statutory consultation (the 'October consultation') on these proposed licence modifications.² In this consultation, we set out our consideration that the introduction of SLC 32A is necessary and proportionate. We consider SLC 32A will be valuable in enabling Ofgem to gather evidence in order to identify the most appropriate way of promoting the interests of existing and future consumers, for example, through the development of new or more effective ways of prompting consumer engagement in the domestic energy market. This was based on the findings of Competition and Market Authority's (CMA) Energy Market Investigation³ and consideration of Ofgem's principal objective and general duties. A summary of the relevant CMA findings can be found in the October consultation.

In parallel with publication of the October consultation, we consulted on the selection criteria Ofgem would use to select the right supplier(s) to test consumer engagement measures under SLC 32A. A summary of the responses and the final selection criteria have been published today.⁴ The selection criteria will constitute the published criteria for the purposes of paragraph 32A.7 of SLC 32A and this means that all elements of SLC 32A will be capable of being enforced from the implementation date set out above.

¹ The terms "we", "Ofgem" and "Authority" are used interchangeably in this letter.

² https://www.ofgem.gov.uk/system/files/docs/2016/10/slc_32a_stat_con_-_open_letter_final.pdf

³ <https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf>

⁴ <https://www.ofgem.gov.uk/publications-and-updates/decision-selection-criteria-mandatory-supplier-testing-measures-promote-domestic-consumer-engagement>

Policy overview of SLC 32A

As the October consultation set out, the CMA found that a combination of features in the domestic retail supply of gas and electricity gave rise to an Adverse Effect on Competition (AEC) through an overarching feature of weak customer response. It found that features leading to weak domestic customer response were:

- customers' limited awareness of and interest in their ability to switch energy supplier, arising in particular from the role of traditional meters and bills and the homogeneous nature of gas and electricity;
- actual and perceived barriers to accessing and assessing information; and
- actual and perceived barriers to switching.

As part of the remedies to address this AEC, the CMA recommended that Ofgem establish a programme of work to provide customers with measures to prompt them to engage. It considered that suppliers have the ability to engage their existing customers through the regular communications they send to them, but they are likely to face limited incentives to do so.

As such, the CMA recommended that this Ofgem-led programme should identify, test (through randomised controlled trials (RCTs), where appropriate)⁵ and implement measures to provide domestic consumers with different or additional information with the aim of promoting engagement in the domestic retail energy market. The CMA further recommended that we introduce a licence condition (SLC 32A) to require suppliers to participate in this programme, to ensure the programme's effective implementation, for which it provided the draft licence condition wording.⁶

SLC 32A has two key features: (i) the power to direct licence holders to undertake testing and trialling; and (ii) information gathering powers. Both are with regards to us being able to use RCTs or other forms of testing to identify effective domestic consumer engagement measures.

Our response

As the October consultation set out, we support the findings on the AECs and remedies to address them, including establishing a programme of work to identify new and more effective ways of prompting consumer engagement. This programme of work also aligns with our proposals to require suppliers to enable their customers to make informed choices.⁷ To support this we have established a Behavioural Insight Unit and we have begun research to aid in the identification and development of new and/or more effective ways of engaging consumers.

As set out in October "In light of the CMA's compelling AEC findings, Ofgem considers that the introduction of proposed SLC 32A would be both a necessary and proportionate regulatory intervention. We also consider that this intervention is consistent with Ofgem's principal objective and general duties. In particular, we note that the power of direction afforded by proposed SLC 32A will ultimately facilitate Ofgem decisions on the most appropriate ways of protecting the interests of existing and future consumers, including in terms of the balance between the promotion of effective competition and more direct methods of consumer protection."

We still considers the introduction of SLC 32A both a necessary and proportionate regulatory intervention. This is based on market developments and consideration of responses to the October consultation.

⁵ And through quasi-experimental and other research methods where not.

⁶ See Appendix 13.1, <https://assets.publishing.service.gov.uk/media/576bcc89ed915d3cfd0000c1/appendix-13-1-standard-condition-32a-fr.pdf>

⁷ <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-enabling-consumers-make-informed-choices>

Since the October consultation, we have not seen any developments to suggest that the CMA's findings are no longer valid, including the "magnitude of the detriment resulting from the Domestic Weak Customer Response AEC" observed by the CMA. There is still a need for the development of more effective consumer engagement measures. RCTs will provide the most robust mechanism for assessing the effectiveness of different measures at driving changes in consumer behaviour. We are aligned with the CMA's position that this licence will "enhance the effective implementation of the Ofgem-led programme".

Following careful consideration of the responses to the October consultation, there was also no compelling evidence for why the introduction of SLC 32A was either unnecessary or disproportionate. Many respondents sought voluntary engagement by Ofgem in the first instance. Nevertheless, they recognised that we may need access to these powers to ensure that trials occur and to the standard required, particularly if an intervention we seek to trial is not aligned with a suppliers' incentives.

Summary of consultation responses and Ofgem's view

We received 20 responses to the statutory consultation. Respondents included a consumer group, suppliers and a trade association.

The majority of respondents were broadly supportive of the introduction of SLC 32A, recognising why we may need the ability to direct suppliers. Most respondents sought that this power to direct should be used as a back stop, suggesting that Ofgem primarily pursues trials through voluntary arrangements.

Some respondents asked for clarification and requested further information about how certain elements of SLC 32A may work in practice. The section below notes these points and, where relevant, provides Ofgem's views. We set out in Annex 1 an example of the process of and stages leading up to and following Ofgem issuing a supplier with a Direction to test a consumer engagement measure.

1. The interpretation of consumer engagement measures

The scope of SLC 32A as a whole is determined by paragraph 32A.1 of that condition. In both the version of SLC 32A published in the CMA's final report and the version set out in Ofgem's October consultation, the drafting of paragraph 32A.1 was identical and provides: *"For any purposes connected with the Authority's consideration of measures or behaviours which may impact on consumer engagement ('consumer engagement measures'), the licensee must comply with a direction issued by the Authority in respect of Relevant Matters for Standard Condition 32A."*

In the October consultation we set out its interpretation of paragraph 32A.1 for the purposes of giving clarity on the scope and effect of the proposed modifications. This essentially made clear that the reference in the drafting to "measures or behaviours which may impact on consumer engagement" means that the scope of the licence condition is broad and not limited to information or communications. We also explained that it intended to focus initially on information measures but the broad scope of the licence condition would ensure it was future-proof in the light of ongoing market developments or industry changes.

Eight respondents felt that this interpretation was too broad and that we had moved significantly from the intent of the CMA. Some respondents wanted Ofgem to focus solely on the list of measures for testing put forward by the CMA.

We have decided not to amend the drafting in paragraph 32A.1. Instead, in the light of consultation responses, we provide here further clarification on our interpretation of the scope and our envisaged focus of trialling/testing.

As we set out in the October consultation, we can confirm that the initial focus of our programme of work will be with the provision of information, which could be provided in different mediums such as email, text or post, or combinations of these.

We can also confirm that we do not interpret the scope of SLC 32A as covering commercial decisions of suppliers as to whether to offer or withdraw particular types of product such as tariffs, bundled goods and services or incentives such as discounts. However, we do consider that trials/testing of information in connection with products offered by suppliers (including products offered by rival suppliers) would be within the scope of SLC 32A. Such as, the CMA's proposal for a market cheaper deal prompt whereby suppliers would inform their customers of cheaper tariffs available from other suppliers. The CMA's proposed prompts fall within scope but the list put forward by the CMA was not intended to be exhaustive.

We are also firmly of the view that the scope SLC 32A would include supporting and ancillary measures or behaviours of suppliers which may impact on consumer engagement due to the important relationship with the products and information suppliers offer to customers. For example, training provided to call centre staff to deal with contacts from customers who receive a new prompt that is being trialled.

2. Drafting changes

The October consultation provided a list of drafting changes⁸ we have made to the original version of SLC 32A that was set out in the CMA's final report. Two respondents felt that a change to sub-paragraph 32A.8(d) had changed and broadened the scope of SLC 32A. The specific change is the replacements of "potential regulatory measures concerning the information provided to Domestic Customers" after "testing of any" with "consumer engagement measures in the manner and time frame specified by the Authority".

As we set out in the October consultation, we consider this to be a minor change for the purposes of consistency with the drafting and scope of the power of direction in the remainder of SLC 32A. As explained above, the scope of SLC 32A as a whole is determined by paragraph 32A.1 which is framed in terms of "...measures or behaviours which may impact on consumer engagement..." and this drafting is identical to the version of SLC 32A which was published by the CMA. Therefore we consider that the changes it has made to sub-paragraph 32A.8(d) do not alter the overall effect and scope of SLC 32A.

3. Consultation prior to issuing a Direction

Some respondents suggested that we should consult prior to issuing a Direction; this included a suggestion from one supplier for an explicit requirement to be included in the licence drafting. The purpose of such a consultation was generally to ensure that Ofgem sought and considered representations from suppliers who might be the subject of a Direction.

Engaging effectively with suppliers will be critical to the success of the trialling programme. As such and as illustrated in Annex 1, we can confirm that we would always have some form of prior engagement with suppliers throughout the process of developing and issuing a Direction, and the subsequent trialling activity and analysis. As part of this, we will seek to co-design trials with suppliers where possible, although we are prepared to dictate terms where necessary to ensure progress.

Whilst the form of engagement may vary throughout this process, we would expect to seek representations from suppliers regarding, for example, their capability and the costs of running a particular trial. This and other information would be given due consideration in order to determine whether running a particular trial with a particular supplier is reasonable

⁸ Table 1, Appendix 1

and proportionate – in line with both the Selection Criteria and Ofgem’s better regulation duties. As a result, we do not propose to make a change to the drafting of SLC 32A.

4. Notice period following a Direction

The drafting of SLC 32A contains a provision for Ofgem to provide suppliers with at least one month’s notice for a trial to start once a Direction has been issued. Respondents felt that one month would not be adequate time to develop and implement a trial. A number of respondents proposed different notice periods for different types of trials, while others set out that there was no single time frame, so flexibility would be required.

The one-month notice period set out in SLC 32A is a minimum period intended to provide suppliers with a degree of regulatory certainty. As we set out in the October consultation, the actual notice period in any case will be chosen to allow for a reasonable period of time for a suppliers to make all the preparations and other necessary steps to enable successful testing/trialling to be undertaken. A ‘reasonable period’ will depend on the circumstances and will be considered on a case-by-case basis.

Furthermore, as explained above and illustrated in Annex 1, we will always have some form of prior engagement with suppliers and so suppliers which we have selected will have awareness of trial proposals including the time scales prior to receiving a Direction to test/trial.

5. Commercial Impact

There were concerns from a number of respondents that participation in a trial may have a negative impact on their own commercial standing. The examples given include a trial that results in high levels of complaints and low levels of satisfaction.

The development of each trial protocol, will include an ethical review where potential areas of consumer detriment as a result from the trial will be considered. This will also include monitoring strategies, to ensure that, should any detriment arise, this is quickly identified and appropriate action taken, which may include stopping the trial. Furthermore, it is highly likely that we will be interested in all consumer actions taken as a result of receiving a prompts and as such specific codes (or equivalent) for complaints will be developed to allow trial related complaints to be ring-fenced. Where appropriate, we may then ring-fence these complaints in the regular complaints reporting.

A second area of concern was that an intervention being trialled might prove to be highly effective at prompting engagement and, as a result, a supplier loses a significant number of consumers either to another supplier or from a particular tariff type.

The impact of this can be managed by ensuring that the burden of trials is fairly spread across suppliers, that the size of a trial is appropriate and proportionate – ie a trial with 200,000 customers should not be pursued when a trial with 40,000 customers is sufficient, and that by selecting suppliers of a sufficient size proportionate to the scale of the trial. However we do recognise the potential for some commercial impact and would not consider this a valid reason for a supplier to avoid or be excluded from a trial. Of course, if a proposal was proven to be successful in promoting engagement, it is highly likely that we would seek to put this in place for all suppliers to facilitate competition.

6. Impact on Innovation and Competition

A small number of respondents raised concerns that SLC 32A may hamper innovation and competition. This was in part due to concerns that participation in an Ofgem-led trial would require resource that cannot otherwise be used to develop innovative products and services.

A primary objective of this programme is to develop more innovative and effective ways of prompting consumer engagement to improve consumer outcomes and help address the AEC identified by the CMA.

We recognise that trials will require resource from suppliers (at least for the duration of the trial). To support this, we will ensure that trials are appropriately designed – ie that they are only as large or as costly as is needed. We also seek to share the burden across suppliers, for example by not choosing the same supplier twice in short successions. This should also ensure that suppliers still have some scope and resource opportunity to develop their own innovative offers to improve outcomes for consumers to respond to the AEC identified by the CMA.

7. Scope of the information gathering power

Two respondents set out that either the scope of the information gathering element of SLC 32A was too broad or that it was unnecessary as Ofgem has other information gathering powers it could use for the same purpose.

Ofgem has a number of information gathering powers which relate to different statutory functions, including enforcement and certain market monitoring activities. However we do not consider the scope of those existing powers enable us to collect all the information which would be relevant for SLC 32A purposes. In particular, existing powers would not appear to enable the collection of information to aid the identification of both the most appropriate proposals to be tested and the appropriate supplier to undertake the testing/trialling. For this reason and to avoid inefficiencies with the potential need to issue multiple requests using different powers to obtain all relevant information, we consider that it would be appropriate to put in place a new bespoke power which is fit for purpose in connection with SLC 32A.

8. Commercially-sensitive data

Reassurances were sought by a number of respondents who were concerned that commercially-sensitive data gathered through the information gathering powers may be shared with other market participants.

As with other information we receive or obtain in connection with its regulatory functions, in respect of information obtained pursuant to SLC 32A powers we would need to ensure that any disclosure or publication is consistent with the relevant legal framework, i.e. section 105 of the Utilities Act 2000 and sections 35 of the Gas Act 1986 and 48 of the Electricity Act 1989. For example, this would mean that we would need to seek representations from suppliers about any information which relates to their affairs and take these into account before deciding to publish such information.

9. The introduction of a sunset clause

A number of respondents proposed the addition of a sunset clause or a formal review of SLC 32A. This was based on concerns regarding cost and level of disruption that undertaking a trial may incur, and the ongoing nature of the SLC.

In the October consultation we set out our intent to act in a proportionate manner. Following consideration of the responses, we have decided to include a sunset clause in SLC 32A as we consider this to be inline with this intent.

The effect of the sunset clause is that SLC 32A will cease to have effect at 24:00 on 31 December 2022 unless the Authority issues a Direction to extend the lifetime of the SLC. The Authority may extend the life of SLC 32A on one or more occasions by issuing a Direction following consultation. This commits us to reviewing the effectiveness, necessity and proportionality of SLC 32A should we be minded to maintain it. This is also in line with our Better Regulation duties.

Six years – to 2023 – should provide a sufficient timeframe to assess the effectiveness of SLC 32A and determine whether there is value in maintaining the licence condition.

The Authority's Decision

Having carefully considered the responses to the October consultation, the Authority has decided to proceed with the modifications to the gas and electricity supply licences by inserting SLC 32A. The effective date for these modifications is on and from 00:01 on 27 March 2017.

Statutory directions modifying the standard conditions of the electricity and gas supply licences have today been issued to all relevant licensees along with this Decision. The statutory directions have also been published on the Ofgem website.

Next Steps

Licence holders, trade bodies representing licence holders and Citizens Advice/Citizens Advice Scotland will have 20 working days to decide (from the first working day after this letter is published) if they want to appeal to the Competition and Markets Authority against the licence modifications. Barring any appeal the licence modifications will have effect from the relevant dates set out above.

In the coming months we will also be publishing guidance for trialling, this will include outline of a trial protocol (or specification for testing). Along with this guidance, we intend to publish a framework for trials, setting out areas of interest.

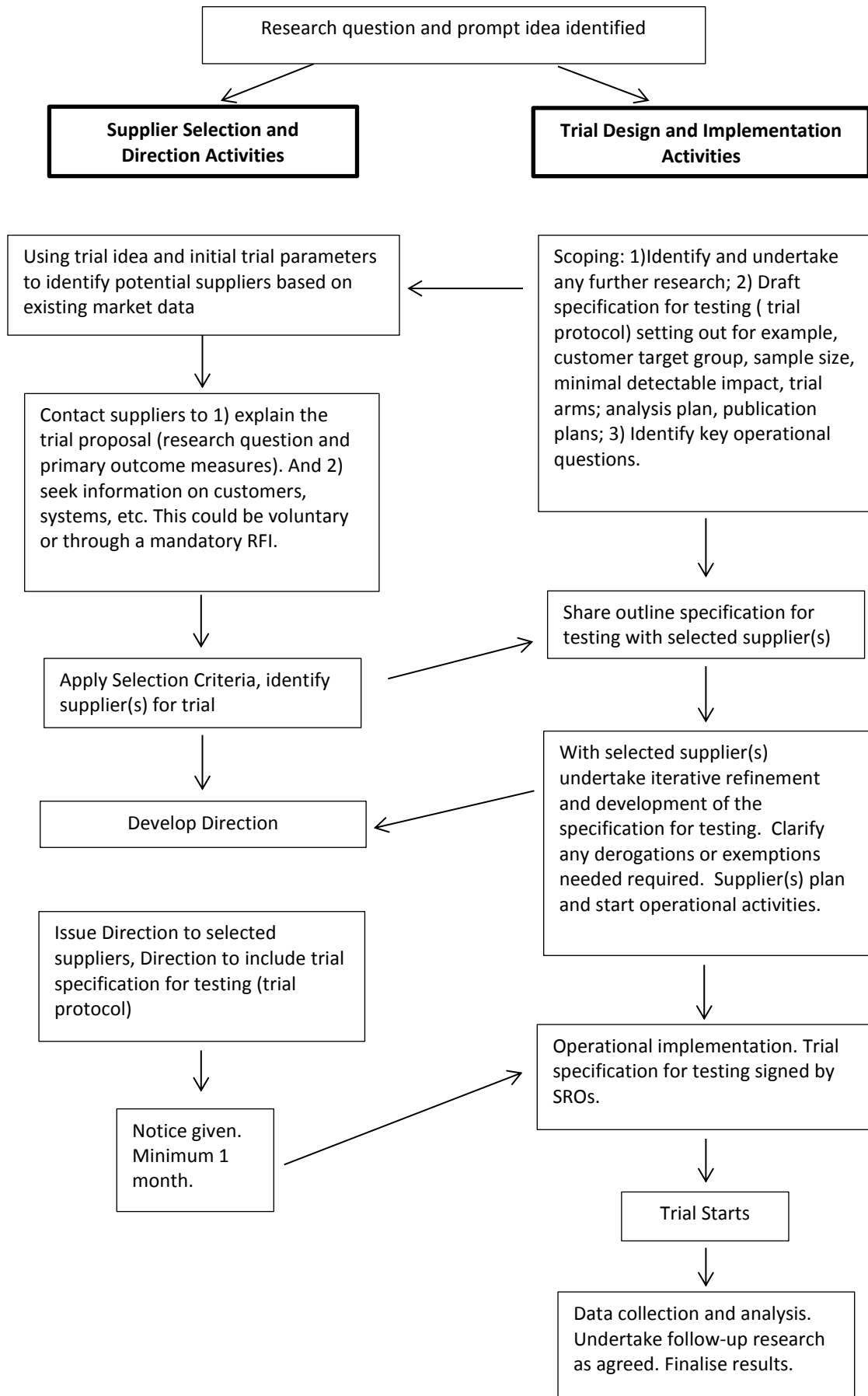
If you have any queries regarding the content of this letter, please direct any questions about this letter to Fiona Cochrane-Williams at DomesticRetailPolicy@ofgem.gov.uk or 0207 901 1802.

Yours faithfully,

Neil Barnes

Associate Partner
Consumers & Competition

Annex 1- Illustrative example of issuing a Direction



Annex 2 – Condition 32A. Power to direct suppliers to test consumer engagement measures

Power of direction

- 32A.1 For any purposes connected with the Authority’s consideration of measures or behaviours which may impact on consumer engagement (‘consumer engagement measures’), the licensee must comply with a direction issued by the Authority in respect of Relevant Matters for Standard Condition 32A.
- 32A.2 The licensee is not required to comply with a direction issued pursuant to 32A.1 unless the Authority has given the licensee at least 1 month’s prior Notice.
- 32A.3 A direction issued under paragraph 32A.1 may include a requirement to comply with any instructions from the Authority or a third party agent appointed by the Authority for the purposes of conducting any test of consumer engagement measures.

Provision of information

- 32A.4 The licensee must provide the Authority (or such other person as specified by the Authority) with information specified by the Authority in relation to matters that it reasonably considers are relevant to:
- (a) the Authority’s consideration of whether to issue a direction pursuant to paragraph 32A.1; and/or
 - (b) the licensee’s compliance with any direction issued pursuant to paragraph 32A.1.
- 32A.5 The Authority may direct the licensee to comply with paragraph 32A.4 by providing to the Authority (or such other person as specified by the Authority) information:
- (a) in a particular form or medium by a particular date;
 - (b) in a particular form or medium at such reoccurring intervals of time as the Authority considers appropriate; and
 - (c) of any description specified by the Authority, including any documents, accounts, estimates, returns, records or reports and data of any kind, whether or not prepared specifically at the request of the Authority.
- 32A.6 The licensee is not required to comply with paragraph 32A.4 if it could not be compelled to produce or give the information in evidence in civil proceedings before a court.

Compliance with this condition

- 32A.7 The licensee is not required to comply with paragraph 32A.1 until the Authority has published criteria for the selection of one or more licensees to conduct testing (including through Randomised Controlled Trials) of any consumer engagement measures.

Definitions for condition

32A.8

For the purposes of this condition:

'Relevant Matters for Standard Condition 32A' means any or all of the following:

- (a) a requirement to test or evaluate (including through a Randomised Controlled Trial, where the Authority considers it appropriate) any consumer engagement measures in a manner and time frame prescribed by the Authority (including on the basis of the Authority's Specification for Testing), and to provide information to Domestic Customers in a manner and time frame specified by the Authority;
- (b) where appropriate, a requirement to submit an implementation plan to the Authority for approval;
- (c) a requirement not to comply with any licence conditions which are relevant to the subject matter of this condition to such extent and subject to such conditions as the Authority may direct; and
- (d) a requirement to provide the Authority (or such other person as specified by the Authority) with information relating to the results (and the underlying data) of the testing of any consumer engagement measures in the manner and time frame specified by the Authority.

'Randomised Controlled Trial' means a form of consumer research (which is statistically robust for measuring behavioural impact) for Domestic Customers which is for the purposes of testing one or more consumer engagement measures relevant to the subject matter of this licence condition and includes two or more randomly assigned customer groups from the pool of eligible participants (which may be determined and specified by the Authority) in circumstances where:

- (a) at least one of those groups are not subject to the consumer engagement measure; and
- (b) all of the customer groups are comparable (including on the basis of the randomised selection) but for the consumer engagement measure(s).

'Authority's Specification for Testing' includes detail on some or all of the following:

Design

- the objective(s) of the testing;
- the details of the consumer engagement measure(s) (and any variants) to be tested;
- the testing methodology (including, but not limited to, the approach to randomisation and maximising the equivalence of groups and the proposed sample size);
- the testing of outcomes and how they will be measured;
- the proposed timetable;
- any planned piloting activity; and/or
- any supplementary research or follow up analysis to gain a better

understanding of the behavioural impact.

Implementation

- the identification of third parties who will be involved in delivering the proposed specification for testing and clarity around roles and responsibilities;
- the details of any proposed supplier-initiated activity that might have an impact on the testing;
- proposed approach for monitoring (including possible arrangements for independent moderation) and quality assurance; and/or
- the approach to dealing with ethics and consumer protection issues, including how any possible consumer detriment will be identified, monitored and addressed should any issue be identified.

Analysis and evaluation of the results

- criteria and approach to evaluate and analyse the results of the testing; and/or
- data to be shared, consideration of format, precise content, file types and data security.

Duration of condition

- 32A.9 Paragraphs 32A.1 to 32A.8 will cease to have effect at 24:00 on 31 December 2022 unless, following consultation, the Authority specifies a later date by publishing a statement in Writing.
- 32A.10 The power to specify a later date in paragraph 32A.9 may be exercised by the Authority on more than one occasion (before, on, or after the expiry of any later date specified by the Authority).