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Switching Programme

EDAG 14

19 July 2017

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Agenda

10.00	1. **Welcome & introductions**		Rachel Clark
	2. **Impact Assessment – Assumptions (optional)** • Summary of assumptions made in developing the IA	60 mins	Tom Fish
11.00	3. **Impact Assessment** • Update on Impact Assessment	90 mins	Tom Fish
12:30	Lunch	30 mins	
13:00	4. **Agent Appointments, Customer Raised Objections & Change of Occupancy flag** • Overview of latest position	45 mins	Jenny Boothe
13:45	5. **Regulatory Design** • Overview of latest position	60 mins	Caroline Ainslie
14:45	6. **Transition Approach** • Overview of latest position	60 mins	James Crump
15:45	7. **Next steps and AOB**	15 mins	Rachel Clark

SWITCHING PROGRAMME IMPACT ASSESSMENT

Analysis still to be developed

The information presented in these slides is a summary of our latest analysis on a number of areas in the impact assessment, with a focus on our quantified analysis. It does not provide the full picture of the IA, in particular with most of the qualitative analysis excluded. There are a number of areas where either the analysis shared is still in development, or there are sections of the IA for which the analysis has not yet been undertaken. The main areas we recognise that further work is required are:

- Refining estimates of the cost data gathered through RFI. In particular, further work required to fully incorporate the costs of delivery of data improvement remedies and industry regulatory programme engagement costs during the DBT phase and beyond. There is also some further analysis to be undertaken on the expected impacts on metering agents.

- Analysis for benefits to non-domestic consumers. The analysis for consumer benefits has focused solely on domestic consumers to date, so the value of the benefits to consumers overall is currently understated. We have prioritised analysis of domestic consumers due to volume, availability of data, and because the benefits to domestic consumers are expected to be greater. The IA will cover all types of consumers, though some benefits for non-domestic consumers may not be quantified.

- Capturing uncertainty through appropriate ranges. Currently some of the analysis incorporates ranges for particular assumptions to reflect the uncertainty, but this is a work in progress. Many of the assumptions in the log that do not currently have a range simply require some further work to refine.

- Capturing risk and uncertainty through sensitivity analysis. The IA will contain a section that includes analysis where we test how sensitive our conclusions are to particular assumptions. We will use this analysis to test the strength of our findings. This analysis has not been completed yet.

- Analysis of expected cost pass-through from industry to consumers. Our preliminary analysis suggests that a range of 75% - 100% may be appropriate, though we will need to carry out further analysis to determine an appropriate central assumption and ensure consistency across Ofgem where appropriate.

- Qualitative analysis of enabling a more innovative, competitive market. This analysis is in development, and will be included in our IA. Introducing switching arrangements and systems that are capable of adapting efficiently to future requirements is a key programme objective, so the IA will focus on the extent that the reform packages achieve this aim.

- Potential development of an industry-led new MIS. A new MIS could potentially have a wide range of functions and associated benefits that could have an impact on our counterfactual e.g. relating to reliability. The proposals are not currently developed to the point at which we could count on them being taken forward, or understand how to factor them into our baseline. We will give this issue further thought as the proposals are developed.

IMPACT ASSESSMENT - KEY ASSUMPTIONS

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NPV modelling assumptions

Variable	Assumption	Rationale
Appraisal period	18 years, including 1 year for DBT, 2 years for implementation, and 15 years of operation.	For proposals that relate to investment in new assets, the appraisal period should cover the costs and benefits over the expected life of the asset. 15 years appears a reasonable expectation for the useful life of the new CSS, based on existing market systems. While uncertainty increases as the time horizon is extended, large-scale investment would be held back by only a short-term view of the benefits.
Discounting	3.5% discount rate	Applied in accordance with HMT Green Book.
Price base year	2017	Cost/benefit figures need to be adjusted for inflation as appropriate so that they are in a single year's prices.
Counterfactual	Switching volumes, operational costs, switching speed, customer numbers assumed equal to 2016 and flat.	Deliberately simplistic approach to the analysis. While we recognise there will be significant variation, accepting 2016 figures as an average for future years does not appear unreasonable. Although switching rates are currently rising, this is not for the first time. If other reforms do lead to a sustained increase in switching above current levels, we would not expect this to invalidate our analysis. Claiming additional benefits of the switching reforms would not untenable until the switching market was saturated, which is a very ling way off. As we are only presenting illustrative analysis of increased switching, we only require an illustrative baseline.

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Reliability

Variable	Assumption	Rationale
Volume of ETs, delayed switches, rejected and abandoned switches [caused by data issues] in the counterfactual	85% of estimated current volumes	We have used market data to estimate current volumes of negative switching outcomes, then applied a reduction factor of 15% to account for ongoing efforts alongside the switching programme to improve data and prevent ETs. This assumption is entirely judgement-based, does not include estimates for specific interventions, and is not a target. We have invited challenge from the ETWG on this. The assumption has only a small impact on the outputs of the analysis, which are assessed relative to the counterfactual.
Volume of ETs prevented during existing switching window	2 x the volume of ETs. ie next day switching with no other changes would treble ETs.	Based on market data for CROs and registration withdrawals. Assumed 100% of CROs are ETs, and 10% of withdrawals. We have invited challenge from ETWG on these assumptions. We are awaiting data from Electralink on the time profile of when CROs and withdrawals are actioned.
Proportion of ETs caused by data quality issues	80%	Market data suggests 85% are down to incorrect MPxN selected. We have applied a small reduction to account for human error. Some initial feedback from ETWG members suggests human error rate may be higher.
Impact of RP2a / 2 / 3 on the volume of negative outcomes caused by poor data quality	85% reduction for RP2a / 2 / 3	An assumption is needed to consider the impact of data improvement remedies on reducing numbers of ETs. Remedies to introduce a premises address database and improve plot addresses should help to reduce ETs. Initial assumptions are based on PWC research conducted during the blueprint phase, which suggested that automatic fuzzy matching of data would have approx 80% success rate, and manual data cleansing could cleanse a further 15%. Cleansing the remaining few per cent might require more costly interventions such a site visits. Given that the data problems causing the reliability issues may be the most difficult to cleanse, we have taken a cautious central assumption that only 85% of the data issues causing reliability problems will be corrected. In practice, we will expect the impact to increase over time closer to 100%.
Impact of RP1 on the volume of negative outcomes caused by poor data quality	60% reduction for RP1.	Cleansing existing address data within UK Link and MPAS against an address database and matching addresses to an MPxN would be expected to deliver some improvements to data quality and therefore to reliability. However, RP1 would still retain two separate databases with existing issues around governance and stewardship retained. Without the single premises address database within the CSS it will not be possible to gain as much certainty that the MPRN and MPAN are linked to the same premises address and that the link will be correctly maintained over time. We have scaled down from the above assumption based on judgement only at this stage.

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Direct benefits of faster switching

Variable	Assumption	Rationale
Proportion of consumers that would be committed annual switchers in the counterfactual	4% - 8%	Ofgem 2016 consumer engagement survey found that 12% of consumers have switched electricity supplier four or more times, and the equivalent for gas is 11%. While this proportion of consumers are regular switchers, not all of them will do so very regularly over time. An assumption has been made that half this group are highly engaged consumers that will switch internally or externally on an annual basis. This is to some extent supported by the data from the same source that 6% and 7% of consumers have switched internally for their gas and electricity tariffs respectively at least four times before.
Proportion of switches requested early enough to avoid lapsing onto the SVT	20% - 60%	This assumption is entirely judgement-based. This is on the expectation that, even for the most engaged consumers, switching their supplier or tariff may often be left to the last minute or forgotten until there is an increased energy bill.
Time saving to consumers from faster switching	5 – 10 minutes	Faster switching will improve consumers' experience in a number of ways. During the existing switching window many consumers may spend time wondering what is happening with their switch, being frustrated or concerned, checking their app/emails/online account for updates, or even contacting suppliers for an update online or by phone. By having to submit a meter read weeks after the initial decision to switch they may also have to re-engage mentally with the process. They may have read their meter when they first switched. Though the fundamental improvement of faster switching will be the increase in certainty and a reduction in frustration, there is also expected to be a small time saving to consumers associated with this uncertainty and frustration. On average the time spent by consumers engaging mentally or actively with the lack of progress is likely to be low, hence a cautious range of 5 - 10 minutes has been assumed.
Value of consumers non-working time	£6.93	Figure used by Ofcom for leisure time in their 2016 IA for reliable and easier switching. Value based on consumer valuation of non-working time in relation to transport / commuting - the extent people will pay more for a faster journey. Placing a monetary value on non-working time in this way is accepted practice within central government. We will be engaging with Ofcom to reconcile this assumption against their DfT source, which appears to have been updated (upwards) since publication of the Ofcom IA.

Impact of increased consumer engagement

Variable	Assumption	Rationale
Consumer saving from external switching	Dual fuel = £280 Gas = £160 Electricity = £120 Average single meter = £137	Currently based on data from May 2017 for the differential between the average SVT and the cheapest fixed deal. On average, across all switchers, this is the maximum value a switcher could save at the point this data was gathered. While not all consumers will choose to switch to the cheapest fixed, so many consumers will not achieve this level of saving, they all have the option to. Given the freely available information through PCWs for comparing tariffs, we assume that where a consumer has opted for a more expensive tariff, it is because they value another element of the chosen supplier's offering (e.g. confidence and familiarity, customer service, recommend a friend incentive etc) at a value equal to or greater than the difference in the price. All consumers are therefore assumed to achieve the (average) maximum saving available. This assumption is a placeholder. We will be doing more data analysis to base the assumption on an average over a whole year, as well as identifying highs and lows to inform a suitable range and sensitivity analysis.
Consumer saving from internal switching (single fuel)	£35	Analysis of market data for 2017 produced an estimated average differential between suppliers' SVT and their fixed tariffs of around £70 for a dual fuel account. We have halved this as the data we have for switching rates is based on individual accounts (ie single fuel).
Marginal cost to suppliers of an external switch	£25	Average of RFI responses.
Marginal cost to suppliers of an internal switch	£10	Only involves one supplier so taken to be no more than half of the external switching cost. Assumed to be slightly under half the cost as process is assumed to be more straightforward.

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Illustrative analysis of increased engagement

Variable	Assumption	Rationale
Scenario 1 (Based on cautious assumptions)	1% increase in external switching volumes 2% increase in internal switching volumes	Intended as cautious assumptions to illustrate the scale of benefits available with only a very small change in consumer and supplier behaviour. This scenario is viewed as a reasonable lower bound for the potential impact of the reforms.
Scenario 2 (Based on survey evidence of barriers to switching)	10% of consumers will undertake one additional external switch over the appraisal period.	When consumers were asked in Jan 2017 (source: GfK Energy360, a syndicated energy market tracker) to select the most important factor that would make them more likely to switch or consider switching their energy supplier in the future, around one fifth identified issues being tackled by the switching programme. This scenario is based on an assumption that half of this group (hence 10% of consumers) will make a small behavioural change as a result of the reforms (just one additional dual fuel switch each over 15 years). The scenario does not include any benefits from additional internal switching.
Scenario 3 (Based on experience in current account market)	Spike in external switching, gradual decline, then sustained 3% increase. Gradual increase in internal switching followed by a sustained 5% increase.	Scenario, and the assumptions underpinning it, are based on an understanding of what has happened in the current account market following the switching reforms in 2013. Following a sharp increase in year 1 of around 20%, the increase fell to around 13% in years 2 and 3, from which point the level of switching is expected to continue at around the baseline level. The rise in switching was attributed to an increase in innovative product offerings and competition. At the same time customer retention efforts have now increased, with customers taking up incentives to remain with their current account provider. This is thought to be the sustained impact of the current account reforms. We have assumed the switching reforms in the energy market will have a larger sustained impact on external switching as research demonstrates the reforms are tackling genuine barriers to engagement, and there is a clearer financial incentive for repeat switching in the retail energy market.

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Consumer NPV

Variable	Assumption	Rationale
Cost (and benefit) pass-through	75% - 100%	We propose to assume a high level of pass-through of the direct costs of the switching programme on the basis that they are being imposed across the industry on all suppliers. A value of below 100% is proposed as some suppliers will face much higher costs than others, and those may be reluctant to pass the full costs on. Also, as some of the up-front investment costs will not be linked to marginal cost of supply (ie they will be sunk), suppliers may find it increasingly difficult to continue to pass these on in an increasingly competitive market. Academic research of the Spanish electricity market in 2013 found that 80% of emissions costs were being passed through to consumers (reflective of the level of market power and price-elasticity). We are yet to reach a conclusion on the most appropriate central estimate for this assumption.
Supplier response to increased switching	Not modelled.	Increasing switching away from the SVT will initially lower the average price paid by consumers. Suppliers may react to this in a number of ways, including accepting tighter margins, becoming more efficient, increasing their SVT price, increasing their fixed price etc. These different responses would each have a range of different potential knock-on effects relating to the differential between rates, further consumer engagement, and market shares. We are not seeking to model for these complex market dynamics within our simple illustrative models. We do expect that increasing competition for disengaged consumers will create strong incentives for suppliers to either accept lower profits, or become more efficient. We therefore expect increased switching to lead to a reduction in consumer detriment. This conclusion is consistent with CMA analysis of its remedies.

UPDATED SUMMARY OF IA ANALYSIS

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Performance against programme objectives

Programme Objectives		RP1	RP2a	RP2	RP3
1. To improve consumer experiences and perceptions of changing supplier, leading to increased engagement in the market, by delivering a switching service that:	a) Is more reliable, thereby reducing the instances of consumers being let down by delayed, unsuccessful or unwanted switches.	✓	✓✓✓	✓✓✓	✓✓✓
	b) Offers consumers control over when they switch, including providing the capability of doing so as fast as possible, and by no later than the end of the following day after a consumer has entered into a contract.	✓	✓✓	✓✓✓	✓✓✓
	c) Minimises any differences in consumer experiences of the switching process, to the extent that is possible, taking into account any physical constraints imposed by metering and issues relating to consumers indebtedness.	✓✓	✓✓	✓✓	✓✓
d) To deliver a simple and robust system architecture design that harmonises business processes across the gas and electricity markets where possible, and is capable of efficiently adapting to future requirements.		✗	✓✓✓	✓✓✓	✓✓✓
e) To encourage more effective competition by minimising barriers to entry for new entrants to the market, including the extent to which a successful switch may rely on the actions of an incumbent, and by having appropriate safeguards in place where this is not possible.		✓	✓✓	✓✓	✓✓
Cost-effectiveness (as per the programme's overarching objective)		✓✓	✓✓✓	✓	✗
Overall assessment against programme objectives		✗	✓✓✓	✓✓	✗

ASSESSMENT OF CONSUMER IMPACTS

Monetised direct consumer NPV

Direct net cost to industry X **Assumed pass-through rate** + **Direct monetised benefit to consumers** + **Savings to consumers from increased engagement**

Illustrative NPV for monetised direct and indirect impacts

Our monetised analysis does not include several important benefits that are fundamental to the objectives of the programme. In particular, we have not sought to place monetary values on the improved experiences of consumers (ie reduced stress or anxiety) or the benefits of a more innovative competitive market in the longer term. Our analysis of these non-monetised benefits will be central in informing our decision.

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CONSUMER NPV

The table below summarises our monetised analysis of the net impacts of the reform packages for consumers. The NPV for direct impacts incorporates costs and cost savings that we would expect to be passed through from industry to consumers, and the direct benefits to consumers of the reforms.

The table combines these figures with our illustrative analysis for the potential benefits to consumers from increased engagement in the market. While these aggregated figures are not intended to be a forecast, and we have not identified a 'central' scenario, they are intended to solely to give us confidence that the reforms will have a significant positive outcome for consumers overall.

	Consumer NPV from direct impacts only			Illustrative analysis of indirect consumer benefits			Illustrative NPV for monetised direct and indirect impacts
	Low (ie pessimistic)	Central	High (optimistic)	Scenario 1	Scenario 2	Scenario 3	(Illustrative range combines 'low' direct NPV with scenario 1, and 'high' with scenario 3)
RP1	(-£67)	£33	£204	£252	£622	£739	£185 - £943
RP2a	(-£89)	£32	£233				£163 - £972
RP2	(-£408)	(-£255)	(-£7)				(-£156) - £733
RP3	(-£470)	(-£311)	(-£54)				(-£218) - £686

This analysis does not incorporate the potential benefits that have not been monetised e.g. increased utility from improved experiences, and a more efficient, competitive innovative market. These figures therefore do not represent the full extent of the benefits for consumers of the reforms.

Refined reform packages

Estimated industry costs

Reform package	PV industry direct cost
RP1	£195
RP2a	£313
RP2	£631
RP3	£693

The estimates of industry costs, in particular for RP2a, are under review following submissions from industry with additional information.

Updated figures will be presented at EDAG on 19 July.

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Expected impact on reliability

There are a number of components of our reforms that will contribute to a more reliable consumer experience, ranging from those focused on centralising, cleansing and maintaining better quality address data and improvements to meter technical details, to more narrowly focused amendments to processes such as proposals for related MPANs and linking of dual fuel switches.

We expect the address database remedy, and associated cleansing, maintenance and stewarding activity, to have by far the biggest impact on the reliability of the switching arrangements. Our quantified analysis is therefore, at this stage at least, focused on the impact that improvements to address data quality could have. We have considered how these proposals may affect the volume of the following harmful outcomes:

- Erroneous transfers
- Rejected and abandoned switches
- Delayed switches

In addition to modelling the positive impact of data improvements, we have also set this against the potential harm that could be caused by faster switching, which will limit the industry's ability to identify and prevent erroneous transfers during the existing switching window.

Reliability summary

	ETs	Rejected switches	Abandoned switches	Delayed switches	Annual volume of switching experiences improved by reforms
RP1	+19k	-34k	-73k	-51k	139k
RP2a / RP2 / RP3	-5k*	-48k	-103k	-73k	229k

*A slightly larger reduction is expected for RP2a due to the additional day in the switching time.

	Annual consumer benefit	Annual supplier benefit	NPV
RP1	£7.2mn	£2.89mn	£111mn
RP2a / RP2 / RP3	£12.2mn	£8.1mn	£221mn

Our analysis suggests that our reforms will lead to hundreds of thousands of positive switching journeys that would otherwise have been a negative experience for consumers. As a result, we can expect that these consumers will be more likely to engage in the market in future than they may otherwise have been. That said, even a small increase in ETs could significantly hinder this positive outcome.

We are in the process of commissioning qualitative research with consumers to understand in better detail the impact that the various potential negative switching outcomes can have. The results of this research, expected from late-July, should help us refine the above analysis of the direct costs of unreliable switching, but also to understand what the consumer response to more reliable switching might be.

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Direct benefits of faster switching

1. Increased consumer utility due to faster switching: speeding up switching will improve experiences of the process by reducing frustration, confusion, anxiety etc. caused by existing slow process. This increase in consumers' utility has not been monetised for our IA, but is a key benefit in itself, in addition to the expected knock-on effects of increased further engagement.

2. Consumer time saving: in addition to spending time emotionally engaging with a slow switch, consumers may also actively seek out further information and updates. Engaging twice on the issue and potentially carrying out a needless meter read are also areas where time could be saved. Assuming just a 7.5 minute saving of domestic consumers' non-working time produces a NPV benefit to consumers of £72 million.

3. Supplier time saving: similarly to consumers, we would expect a move to next day switching to save some staff time, largely due to a reduction in consumer contact and removal of unnecessary duplication of messaging. We have assumed this benefit has been factored into supplier RFI responses for the overall impact on people costs.

4. Faster access to improved terms: by introducing faster switching, we are enabling faster access for consumers to cheaper tariffs ie they will be able to switch from the SVT to a cheaper fixed deal 2 – 3 weeks earlier than currently. They will make a saving during this period. However, due to the automatic roll-back onto the SVT after a fixed term has ended, the consumer will revert back onto the SVT 2-3 weeks earlier also, meaning the cost of their energy bills over an extended period is unchanged. However, there is still a benefit to these consumers as faster switching brings forward savings. Due to discounting for social time preference, this generates a very small benefit to consumers. This benefit has not currently been monetised.

5. Bill saving to highly engaged consumers: if consumers take action to avoid reverting back onto the SVT for prolonged periods each and every time their fixed term contract ends, they can effectively 'bank' the savings brought forward by faster switching in perpetuity. In particular, though these very highly engaged consumers may agree new fixed deals on an annual basis, they may occasionally lapse on the SVT for very brief periods (ie if they only remember to switch at the very end of their deal). With faster switching, these lapses would be reduced or avoided as the lag between decision and switch would be removed. Collectively, we estimate this group of consumers could save around £30 million over 15 years.

Public sector impacts

Costs to Ofgem that result from a decision to take forward a set of reforms will be included in the impact assessment. Relative to the industry and consumer impacts, we expect these costs to be small.

Transition:

- Ofgem programme costs are budgeted at a total of around £4mn following DB3.

Ongoing:

- Expansion of team managing DCC price control estimated at 0.5FTE band C (approx. £25k pa).
- The potential for efficiency savings regarding data monitoring and/or compliance needs further consideration.

The total NPV cost to the public sector over 15 years is estimated at around £6million.

Note: this analysis excludes the cost of drafting code modifications, which is being funded by the industry (so has been recorded as a cost to industry). Also, though Ofgem's work to approve modifications may increase in early years to fix issues with the new system, this may be offset by a reduction in the number of individual modifications that we are asked to assess that will be brought about by a dual fuel system.

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SUMMARY OF MONETISED DIRECT IMPACTS

	RP1	RP2a	RP2	RP3
Industry costs	(£195)	(£313)*	(£631)	(£692)
Improved reliability	£111	£222	£222	£222
Faster switching	£101	£101	£101	£101
Public sector costs	(£6)	(£6)	(£6)	(£6)

*We are expecting a small increase to this estimate once we have fully analysed the latest RFI data.

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Expectations for increased engagement

- By reforming the switching arrangements we will improve consumers' experience of the process, which should in turn improve consumers' general perceptions of the level of hassle and risk involved. Speeding up the process should help to dispel the misconception that the process is complex and risky, or that it needs to be resource intensive, and making the process more reliable will give consumers greater faith that they can engage with the market without something going wrong. By linking gas and electricity meters to the same single address, and giving the consumer greater confidence that they can switch both fuels together at the same time, and potentially working towards an 'Amazon-like' experience of how their switch is progressing, we anticipate making the process much more consumer friendly.

- By improving experiences and perceptions of the switching process in this way, we expect consumers to be more willing to engage with the energy market and to shop around for the best deal. This should lead to a higher level of switching than we would otherwise have seen, generating savings for those consumers on their energy bills.

- Both the threat and the experience of additional switching in the market will provide greater incentive for suppliers to try and attract new customers, and to take steps to retain their existing customers. They may seek to differentiate themselves by lowering their prices, improving their customer service, and offering innovative new products and services.

- As well as encouraging further increases in switching between suppliers, the stepping up of customer retention efforts ought to result in more consumers switching tariffs with their existing supplier, generating further savings.

- We have considered in the following slides what the scale of these benefits could be.

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Savings from more switching

A very modest consumer response to the reforms could generate significant financial savings. We have produced some scenario analysis to illustrate this point.

We have modelled four scenarios below, which are explained in more detail on the slides that follow. Scenarios 1 – 3 are not specific to a particular reform package.

1) Scenario 1 – based on very cautious and simple assumptions for an increase in both internal and external switching.

2) Scenario 2 – based on consumer survey evidence on barriers to switching

3) Scenario 3 – based on experience following reforms to the current account switching arrangements

4) Scenario 4 – the indirect benefits ensure that consumers break-even overall with the most pessimistic direct cost estimates

The analysis makes the simplifying assumptions that baseline switching rates, and the savings available from switching, will remain constant across the appraisal period. In truth, both are likely to vary significantly (most likely up and down) across the period.

Increased engagement: Scenario 1

Scenario 1: NPV consumer benefit of £252 million over 15 years.

We start the scenario analysis by seeking to illustrate, through a set of deliberately cautious assumptions, what might reasonably be seen as a lower bound on the savings we should expect to generate from additional consumer engagement.

To start with, in the first year, we have assumed that additional media interest and advertising will only generate a surge in switching over a one month period. We have then assumed that there will be a 1% increase in external switching for all years that follow. We also assume that, due to increased competition and customer retention efforts, there will be a sustained increase in internal switching of just 2%.

Over 15 years this would only mean an additional 1.4 million external switches, and around 4.3 million internal switches.

Increased engagement: Scenario 2

Scenario 2: NPV consumer benefit of £622 million over 15 years.
For this scenario, we model the consumer response to the reforms and the additional competition that follows based on the responses to a consumer survey on the barriers to switching. When consumers were asked in Jan 2017 (source: GfK Energy360, a syndicated energy market tracker) to select the most important factor that would make them more likely to switch or consider switching their energy supplier in the future, they responded in the following proportions:

Unweighted Base	*6734*
Base	*20394*
Better information about the deals available and likely savings	*12.86%*
Greater financial savings on offer	*61.16%*
Choice of when the switch takes place	*2.07%*
Ability to switch within a couple of days	*3.87%*
Confidence that nothing would go wrong	*9.56%*
Ability to switch my gas and electricity supply at the same time	*4.31%*
None of the above	*3.85%*
Other	*2.33%*

Around a fifth of consumers identified barriers that will be at least partially removed by our reforms. It may therefore be reasonable to assume that the reforms will have an impact on some of this group's propensity to switch. For the basis of this scenario, we have assumed that half of this group will conduct just one additional dual fuel switch over the 15 year period, plus a spike in the first year due to media interest and increased advertising. 10% of domestic consumers equates to roughly 2.1 million dual fuel accounts and 570k electricity only accounts.

We have assumed that the spike in the first year would be akin to a year that contains a two month surge in media interest relating to a price rise. This approach leads to an assumption that there will be an additional 650k meter point switches in year 1 (a 12.5% increase). This is then followed by an uplift from the baseline of 350k for each year thereafter. From a base of 7.8 million switches per year, an additional 350k switches pa would equate to a 4.46% increase in external switching.

This would only increase the average number of individual meter point switches per household over the 15 year period from 4.31 to 4.54. This scenario does not include any potential benefits from additional internal switching that might result from increased customer retention efforts.

Increased engagement: Scenario 3

Scenario 3: NPV consumer benefit of £739 million over 15 years.

We have developed this scenario based on our understanding of the experiences within the current account market following the reforms of the switching arrangements in September 2013. Through extensive discussions with Bacs we have developed the following understanding of the impact of the current account switching reforms:

- The reforms had a strong positive impact on the innovative offerings available in the market, both in the lead up to the launch (following announcement of the programme) and after the launch. The large increase in current account switching in the first year after the launch (around 20%) was believed to have been driven mainly by three factors: (i) the increase in more rewarding product offerings; (ii) the sustained high-profile media campaigns; and (iii) a drop off in switching the year before launch as banks and consumers waited for launch.
- In the two years that followed there was (roughly) 13-14% increase on years before the launch. This was still being driven by a combination of (i) and (ii) above.
- Over the last year both of those factors have diminished, and as a result the switching volume is likely to be below pre-launch levels.
- Product offerings and incentives to switch have fallen away as banks are focusing much more on customer retention as a response to the increased switching. This has included customers taking up rewards and innovative product offerings to stay with their incumbent current account provider.
- This situation is currently forecast by Bacs to continue, and the increased innovative offerings to retain customers is seen as the sustained impact of the reforms.

We have adapted the above narrative to generate this scenario for the domestic retail energy market, with the following assumptions:

	Year 1	Year 2	Year 3	Years 4-15
External	15%	5%	5%	3%
Internal	1%	1%	3%	5%

We have assumed the switching reforms in the energy market will have a larger sustained impact on external switching as research demonstrates the reforms are tackling genuine barriers to engagement, and there is clearer financial incentives for repeat switching in the retail energy market.

Increased engagement: Scenario 4

Break-even analysis

In this scenario, we consider how much additional external switching would be required so that the savings generated would ensure that consumers were not made worse off by the reforms over all. To give us greater comfort we have applied the pessimistic 'low' consumer NPVs for the direct impacts of the reforms.

	RP 1	RP 2	RP 3	RP 2a
Pessimistic estimate for consumer NPV from direct impacts	(£67)	(£89)	(£408)	(£470)
Additional external switches required per year	55k	75k	340k	390k
% increase in external switching from 2016 levels	0.7%	1%	4.4%	5%

Scenario analysis summary

These scenarios are intended only to illustrate what the benefits of increased engagement could be as a result of improving the switching arrangements for consumers. Each of the scenarios is not linked to a particular reform package, nor are we suggesting that each package will have an equal impact on consumer engagement and competition. While we would expect the features of RP2a, 2, and 3 to generate a larger consumer response than RP1, we have not sought to include this within this analysis.

Scenario	Indirect impacts NPV (£mn)			
1 – cautious assumptions, incorporating additional internal and external switching.	£252			
2 – based on consumer research on barriers to switching	£622			
3 – based on the experience in the current account market	£739			
Required for consumers to break even in the most pessimistic 'low' scenario of costs and benefits	RP1: £67	RP2a: £89	RP2: £408	RP3: £470

This analysis give us a very high degree of confidence that the net direct costs to consumers (including pass through from industry) of RP1 and RP2a would be comfortably offset by very modest indirect consumer savings, even when compared to our most pessimistic analysis for the expected net direct impacts. The analysis is less conclusive for RP2 and RP3.

Unblocking future system innovation

By introducing flexible, central systems designed with future change in mind, we will be unblocking valuable future industry innovation of systems and services that the existing platforms would not easily support. In particular, we envisage a situation in future where consumers may seek to be supplied by suppliers for relatively short periods of time, enabling them to move between them for different days of the week or even different times of day. There are a number of characteristics of the proposed new CSS that might enable this sort of innovation to either be unlocked, or achieved more cheaply:

- **Speed of switching:** by introducing new systems capable of instantaneous message flows, we would potentially be enabling a situation where a consumer switches frequently from one supplier to the next, for example to take advantage of different terms offered for peak and off-peak supply. This high-volume switching could be performed by the supplier, or potentially by a third party that would agree contracts with suppliers on their behalf.

- **System capacity:** A new CSS can be designed so that it can be easily scaled out to be able to cope with the sort of increases in message flows that would be generated by very high volume frequent switching activity. The existing suite of systems were not designed to collectively cope with this level of change.

- **Data model flexibility:** by designing the CSS in a flexible way that allows additional data fields to be added and is not resistant to future change, we could enable innovation in relationships between consumers and suppliers. For example, the CSS could relatively easily amended to be capable of having more than one supplier registered to a single MPxN at the same time, or including new types of parties to be registered to meter points.

These various avenues for future innovation could transform the way in which consumers interact with their energy supply. The suite of existing systems were not designed to collectively be flexed or scaled out in ways that would be required to facilitate these types of change.

Benefits of increased competition

Increasing consumer engagement in the market is expected to generate more competition in the market, both for attracting new customers and retention of existing ones. This could have a number of positive impacts for consumers:

- Increased innovation of products and services, leading to greater choice in the market and more incentives to switch suppliers or agree new fixed term deals. This impact has been reflected to some extent in the illustrative analysis of increased engagement.

- Improved customer service, coming as part of a push towards improved customer satisfaction.

- Downward pressure on prices created by increased competition will benefit all consumers, including those that remain disengaged. It will place pressure on suppliers to resist putting their SVT rates up to compensate for lost revenues as more consumers switch to cheaper fixed deals.

- Increased competition will drive suppliers and the industry to become more efficient, as consumers switch towards the more efficient suppliers that are able to maintain their rates even though increased switching reduces the average price they receive.

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Design Policy Update

Agent Appointments, Change of Occupancy & Customer Raised Objections

Jenny Boothe / Colin Sawyer
19/07/2017

Agent Appointments

Context

Blueprint Phase design proposed:
- MAM/MOP (MEM), Shipper mastered in CSS
- DA/DC part validated in CSS and mastered in MPRS
- MAP/ Meter Communication Provider (MCP) ID mastered in UKLink and MPRS
- notifications at Switch Confirmation and Switch Execution would inform the gaining and losing parties of: their appointment / de-appointment to a specified Meter Point; the Switch Date; and the IDs of the other parties

Issue

At the May design Forum (large suppliers) indicated that that all types of Supplier Agent should be processed in the same way (i.e.. to avoid a situation where CSS masters some agent IDs and MPRS/UKLink masters others).
the situations is more complex in electricity as the role of specific agents are prescribed.
In light of these concerns the RP2 position was revisited to determine if alternative approaches are needed.

Analysis

- In general, responses from Supplier Agents to the RFI have not attributed significant benefits to the notifications they would receive from CSS.
- MAPs are the exception, as lack of switch info makes it difficult for them to track the accountable party for their assets.
- Options:
  - Option 1 - CSS masters the Shipper and MOP ID and performs pre-validation of DC and DA (which are mastered by MPRS). Notifications are made available to all gaining and losing parties at Switch Confirmation and Switch Execution.
  - Option 2 - all Supplier Agents are mastered in CSS. Notifications to the gaining and losing Supplier Agents would replace the legacy appointment/de-appointment data flows.
  - Option 3 -all Supplier Agents appointments are mastered in MPRS or UKLink and reflected the CSS and no agent IDs would be submitted on a Switch Request
- Significant variation in the way communication services are provided to the various meter types

Approach

- **Recommended:**
  - Option 3: all Supplier Agent appointments are mastered in MPRS or UKLink – CSS would master the Energy Supplier and Shipper IDs and no agent IDs would be submitted on a Switch Request
  - MCP ID is not captured

Change of Occupancy

Context

- Domestic customer switch can be objected to on the grounds of debt
- Non-domestic customer switch can be objected to on the grounds on contract term.
- Where the gaining supplier indicates there is a change in the occupant, then the losing supplier cannot object.
- DLS design predicated on 'instant reactive' objections enabled the CoO indicator to negate the invitation to object

Issue

- A longer objection determination window will enable the losing supplier to determine if the CoO indicator is valid.
- Need to assess:
  1 – Should the presence of the CoO automatically be accepted and negate the invitation to object
  2 – should the incumbent be given the opportunity to object despite the presence of the CoO.

Analysis

- Options – Domestic
  A1 – Assume CoO set correctly – no invitation to object
  A2 – Test for objection in all case
- Options – Non-Domestic
  B1 - Assume CoO set correctly – no invitation to object
  B2 – Test for objection in all case

Approach

- Recommended:
  - Domestic consumers: Assume CoO set correctly – no invitation to object
  - Non-domestic consumers: Test for objections in all cases i.e. enable the losing supplier to investigate the status of the customer prior to sending their objection determination within the objection window.

Customer Raised Objections

Context

- The supply licence allows for co-operative objection and for domestic consumers, customer requested objections (CROs). During the Blueprint phase it was identified that the proposed objection determination window would be insufficient to enable either objection approach to be enacted.

Issues

- Should the E2E arrangements be designed to accommodate domestic and non-domestic CROs and 'annulment' of switches to avoid erroneous switches

Analysis

- Option 1: Supplier A raises customer requested objection
- Option 2: Supplier A raises an switch annulment transaction on CSS
- Option 3: Supplier A informs the customer that only Supplier B can raise switch withdrawal commands
- Option 4: Supplier A advises Supplier B that the customer has informed them of an unauthorised switch. Supplier B is then required to seek re-authorisation of the switch

Approach

- Recommended:
  - Option 2 is implemented for domestic customers – this offers the best customer experience and maximum opportunity of avoiding an ES. Noting regulatory and reporting provisions will need to be developed to ensure that annulment is only used sparingly and in the circumstances for which it is designed.
  - Option 3 is implemented for non-domestic customers

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External Design Advisory Group: Regulatory design: scope of consultation

Caroline Ainslie and Jon Dixon

19 July 2017

September consultation

As part of the September 2017 consultation we will set out our proposals for the regulatory and governance framework for the new retail arrangements.

Today, we are seeking your views on the following areas:

1) Governance framework;
2) Transitional arrangements; and,
3) Change process and timing.

Governance framework: background

April 2015 TOM originally suggested that all switching arrangements would be contained in the SEC with some residual arrangements in current codes.

Recent developments such as CMA remedies have placed a different perspective on this original assumption.

Regulatory Design Team (RDT) view was that switching working assumption to a Retail Energy Code (REC) would be:

- closer to direction of travel on code governance review;
- cleaner to draft a new code;
- beneficial for parties by having all activities in a single destination – clarifying obligations, etc;
- administratively cost-efficient by reducing the number of codes; and crucially,
- quicker to implement changes entirely through existing codes governance

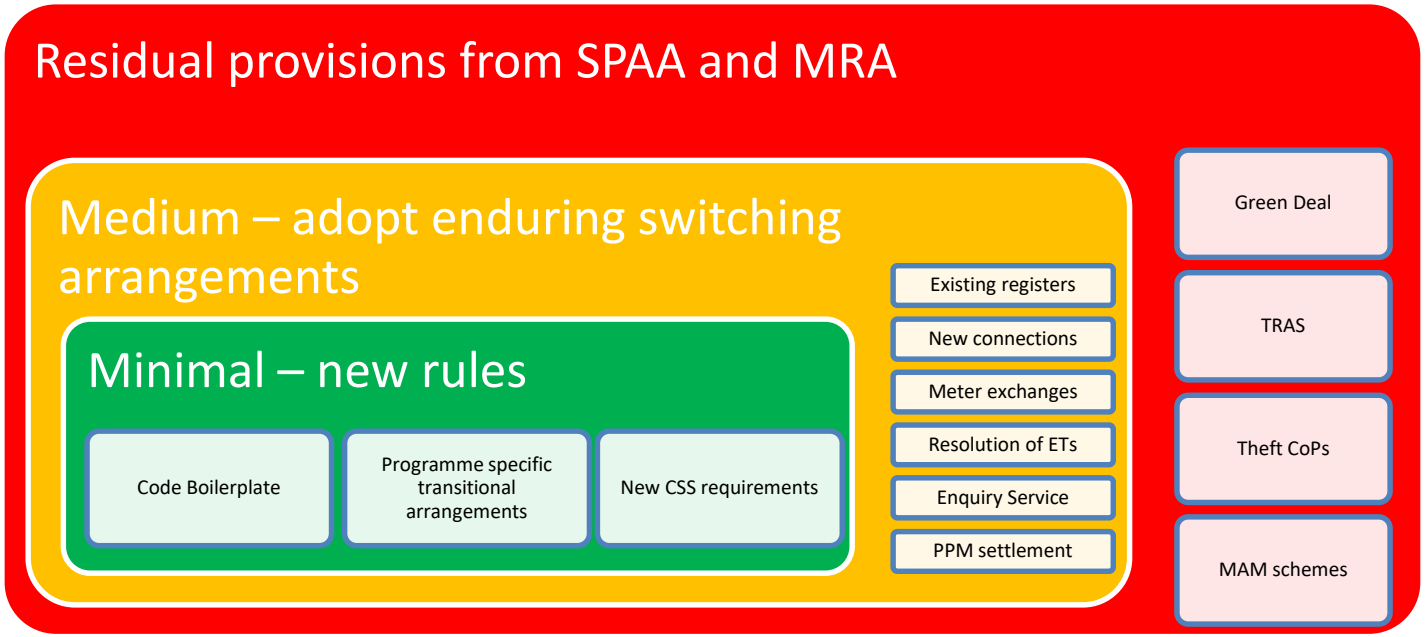
October 2016 Project Board supported RDT changing its working assumption, to instead develop REC, noting that decision would be subject to consultation and in particular the chosen reform package.

We have gained widespread support from industry parties for the concept of a REC and secured **£500k of external funding** from SPAA and MRA parties (primarily gas and electricity suppliers) for legal support on the drafting of the new code.

Governance framework: priorities

The REC may be developed in phases, prioritising those areas which are fundamental the chosen switching reform package being given effect, for instance rules relating to the proposed Central Switching Service (CSS) that do not currently exist elsewhere. There is also opportunity to introduce early formal governance to support the programme's transitional arrangements.

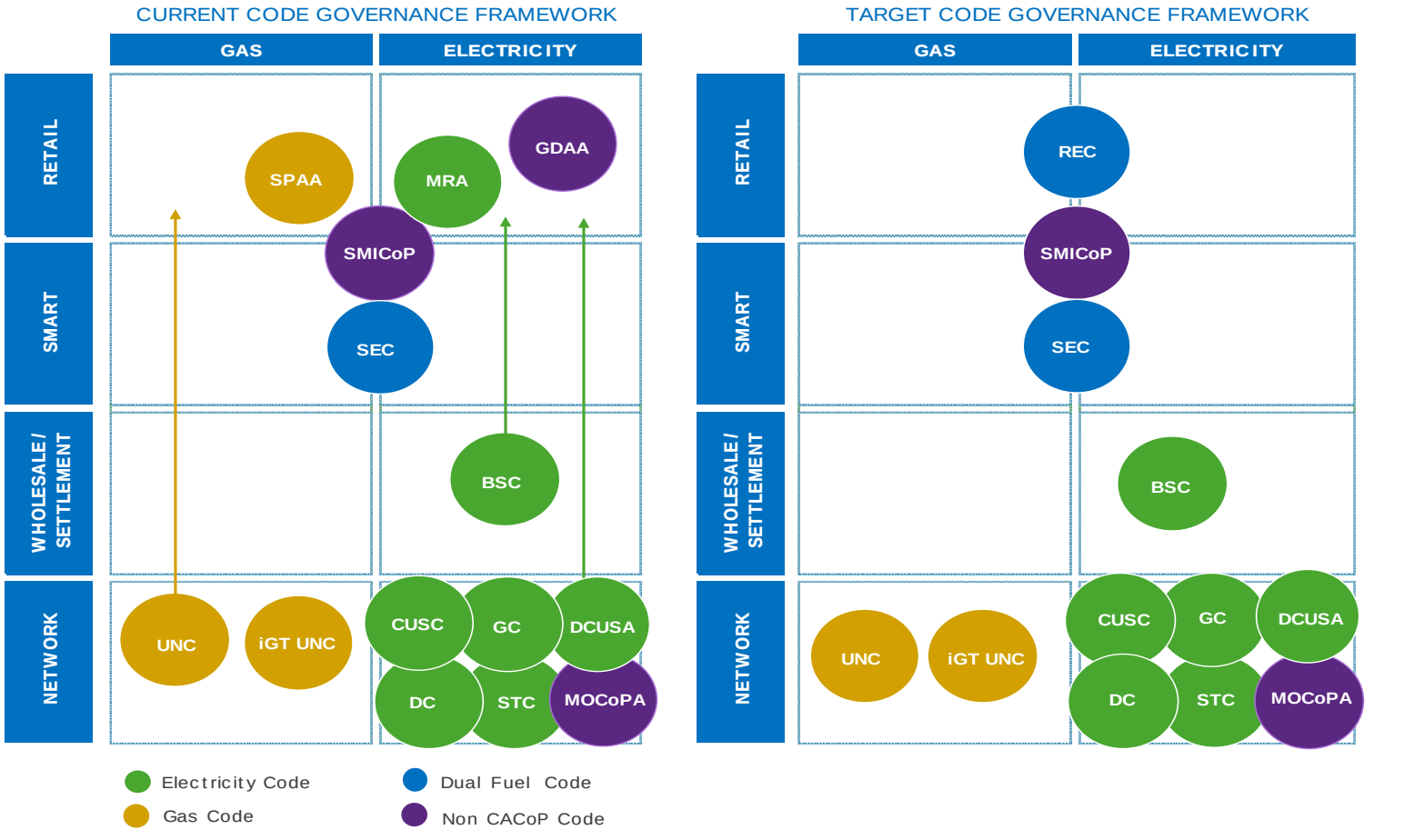
As switching is only one aspect of the retail activity governed by existing codes, as aim to ensure that other processes directly impacted by the new arrangements are also captured under new governance by the time they have effect. However, non-programme/non-essential consolidation could happen at a later stage rather than distract attention from critical line deliverables, as below:



Question: Do you agree that the initial scope of the proposed REC is appropriate?

Governance framework: Possible long-term REC scope

We envisage that a REC would in due course incorporate SPAA, MRA and the GDAA in their entirety, with elements of other codes to be determined on the basis of primary relevance



Transitional arrangements

The switching programme has been seeking to identify **lessons learnt** from other IT dependent programmes such as Project Nexus and SMIP, and consider that it would be appropriate to adopt formal governance of the transition as early as possible. We would expect these transitional arrangements to cover:

- **Data testing** – data owners may be expected to provide real data for testing as this is more robust than dummy data. Safeguards will be in place regarding data sharing and exceptions for new entrants who may not have historic data to draw upon;
- **Data cleansing and migration** – data owners (items relative to the CSS only) will be expected to cleanse standing data to a given standard and provide it in a required format for migration to the CSS as required;
- **Co-operation with the System Integrator** – expectation that they will respond to all reasonable requests rather than require Ofgem intervention, etc;
- **Testing** – shared test planned to satisfy certain common criteria established as part of a Go-No Go framework;
- Adherence to programme decisions (to the extent that they are within scope, reasonable, etc) including eventual go-live decision;
- **Transition** – transparency of and conformity with an established industry plan, with wider stakeholder communications of any impact on switching timescales, etc;
- **Post-implementation** – collaboration on identification and resolution of defects and other issues arising in the immediate post-implementation period, prior to hand over to business as usual governance.

We would be looking to codify many of the steps that Ofgem took in relation to Nexus and other programmes in order that parties can be suitable engaged with and accountable to the System Integrator and/or Project Management Office/Assurance functions, without requiring the same degree of regulatory intervention. The areas outlined above are not intended to be exhaustive, but will be further developed as the programme progresses.

Question: Do you agree that the switching programme should adopt a managed approach to transition and that it should cover, as a minimum, the areas above?

Transitional arrangements: sanctions (1)

Consistent with our desire that as much of the programme as possible be capable of self-governance without formal recourse to Ofgem, we have considered what levers could be applied to the DCC, its CSS delivery partner(s) and wider stakeholders. We would hold the DCC accountable through its licence and associated price control for meeting certain delivery criteria and milestones. Therefore, for the purposes of this presentation and the governance section of the September consultation we focus on the requirements of other market participants, primarily being the gas and electricity suppliers themselves. Possible sanctions include:

License enforcement – to the extent that individual suppliers (or other licensees) may need to achieve a particular state of readiness in order for the new arrangements to take effect, we will consider whether such key milestones should be established under and enforceable by licence. This could be in the form of a go live date to be directed at a later date, rather than prescribed in licence itself. This may not be necessary if the readiness of one of more licensees cannot hold up progress of the market as a whole – i.e. if the CSS arrangement can go-live before some parties are fully ready.

Restriction on registrations – as a potentially more proportionate and readily effected sanction than licence enforcement against a supplier party missing deadlines, could be to instead preclude them from registering new customers until such time as they are compliant. Such sanctions already exist in codes for default on credit rules.

Transitional arrangements: sanctions (2):

Requirement to put in place remedial plans and submit to greater oversight – should market participants fall behind their agreed implementation plans, it may be appropriate for them to work with the SI on a remedial plan, to be formally reported against.

- Consideration could also be given to whether parties should be directly accountable for any additional costs they impose on the SI, PMO or possibly other parties. We would need to consider whether exposure to these costs would create an appropriate incentive, or a perverse incentive not to ask for assistance when genuinely required.

Other options which we have considered but do not consider to be viable include:

- Removal of rights under the Code (to vote etc):
- Liquidated damages:

We will separately develop proposals to ensure compliance with the enduring provisions of the REC, and in particular interactions with the CSS or other parties with whom suppliers may not have a contractual relationship. i.e. we would not expect to cover areas that are appropriately a matter for agent contracts.

Question: Do you agree that possible sanctions other than licence enforcement should be developed in order to ensure compliance with transitional arrangements?

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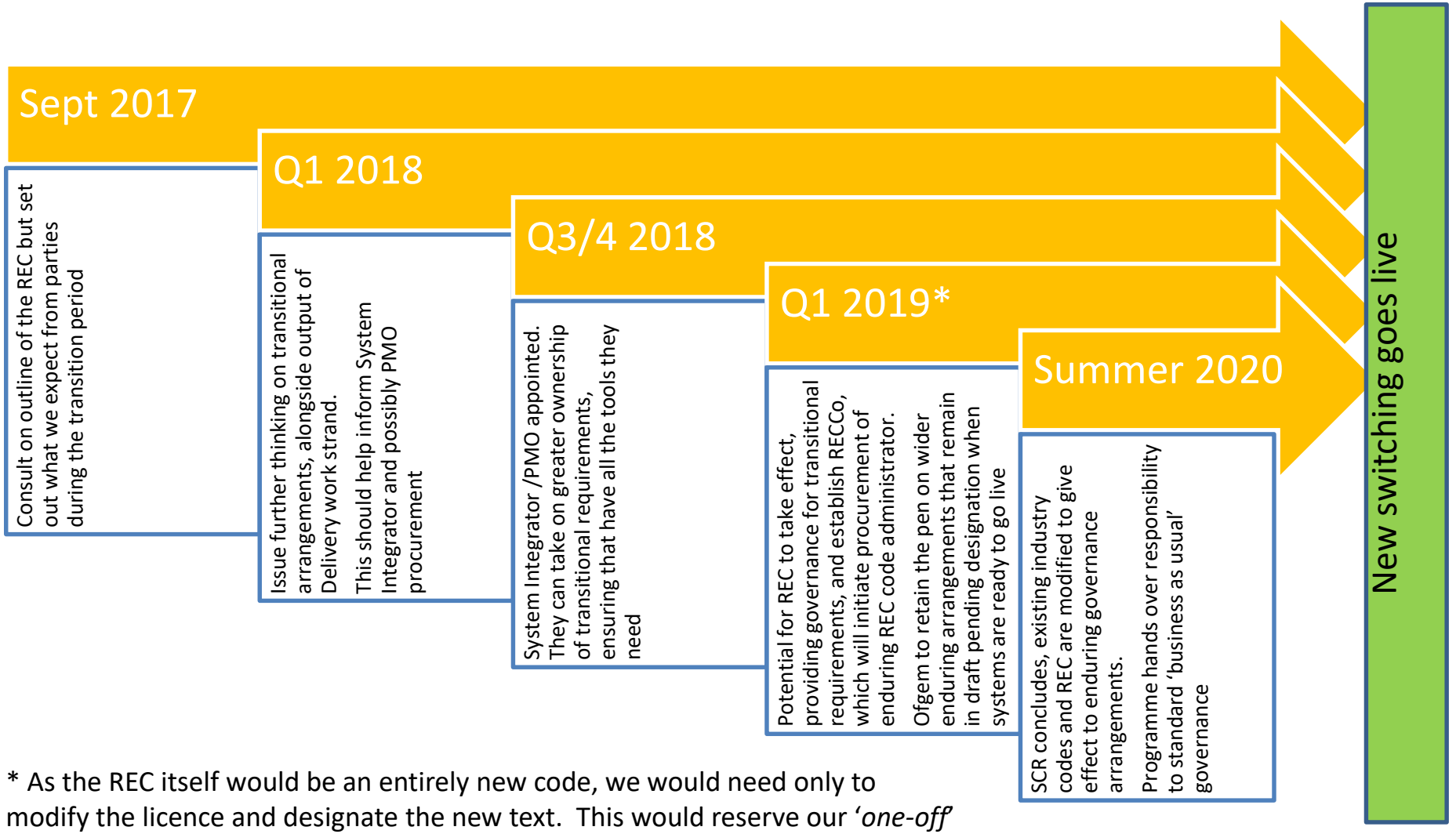
Change process and timing: high level timeline



* As the REC itself would be an entirely new code, we would need only to modify the licence and designate the new text. This would reserve our '*one-off*' SCR powers for subsequent modifications to other industry codes, as required.

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Change process and timing: Significant Code Review

The switching programme launched an SCR in Nov 2015. Since that time the SCR arrangements have been modified to give Ofgem wider process options on how to give effect to its conclusions from the SCR process. Those options are:

1) **Ofgem directs licensee(s) to raise the appropriate modification(s)** – we issue a direction setting out high level principles (with the detail to be developed by industry) or more specific, detailed conclusions to be given effect through code modification(s), which would follow the standard industry processes;
2) **Ofgem raises the modification proposal(s) itself** – dispensing with the need for a direction, but thereafter following the same standard industry processes as option 1);
3) **Ofgem leads and end to end process to develop the code modification(s) including provision of legal text** – standard modification process would not apply.

It is possible to move between options as the programme develops.

At this stage, we envisage that existing retail provisions would be substantively replaced by, or migrated to, a new REC. It is also important that the regulatory and governance framework is developed in a consistent and complementary fashion. The code modification(s) will therefore need to have appropriate regard to modifications to licences, and to the content of subsidiary documents.

We therefore propose to follow SCR option 3). If however, as the programme develops we end up with a much narrower REC than currently envisaged (with the existing retail codes necessarily enduring beyond the end of the programme) we may opt to follow options 1) or 2), as these may be more proportionate to the scale of change required.

Questions: Do you agree that a REC could be introduce ahead of wider code changes
Do you agree that option 3 provides the most suitable process for modifying other codes, consequential to the introduction of a REC:

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Delivery Workstream: DLS Phase Transition Approach

July 2017

Transition Strategy: DLS phase work

- Strategic approach to go-live
  - Discussed in this paper
- Business Continuity Plan in event of catastrophic failure
  - Industry view is to ‘fix forward’; we need to understand risk of catastrophic failure and plan accordingly
  - Consultancy scoping paper being drafted: however, will need greater certainty on final design before we can engage contractors
- Workstrand examining process for managing in-flight switches
  - Being drafted
  - This will derive policy approach (potentially a Nexus-style hiatus in switch management during implementation)

Transition approach: Recap

- Blueprint phase work identified that 'big bang' approach was preferable on cost and convenience grounds
  - Rejected phasing on basis of geography/supplier type etc on grounds of cost/fairness/risk of dual running
  - This prompted some concern amongst stakeholders regarding implementation risk

- In response, we have developed staged approach for DLS (based on RP2/2a), based on delivering parts of functionality in stages, but retaining a single go-live event for CSS
  - Aim is not to re-open other Blueprint phasing options, but to explore how the Big Bang can be de-risked
  - This is separate from the 'glide path' from five to next-day switching, and we believe that the two approaches are complementary

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Staged delivery approach

- Programme go-live involves complex processes:
  - Updating of existing industry resources (such as MPRS and UKLINK) with new data
  - Establishment of new interfaces between existing components and CSS
  - CSS switch-on
  - Removal of (some) existing interfaces between existing components
  - Changes to some existing supplier processes to reflect policy (objections and cooling off)

- Implementing more individual parts to a whole solution at the same time (a genuine ‘big bang’) increases the risk of catastrophic failure

Staged delivery approach (II)

- To de-risk transition to CSS go-live , we propose a staged approach by functionality
- New interfaces and architecture will be introduced on a piece-by-piece basis during DBT phase
- This is more than testing but less than a live production environment: ‘near-live’ environment
- When new interfaces are deemed to be robust, CSS becomes live interface and old interfaces are removed

A potential staged transition

Pre-Transition Activities undertaken during DBT → Initial Release at end of DBT → Release according to system readiness

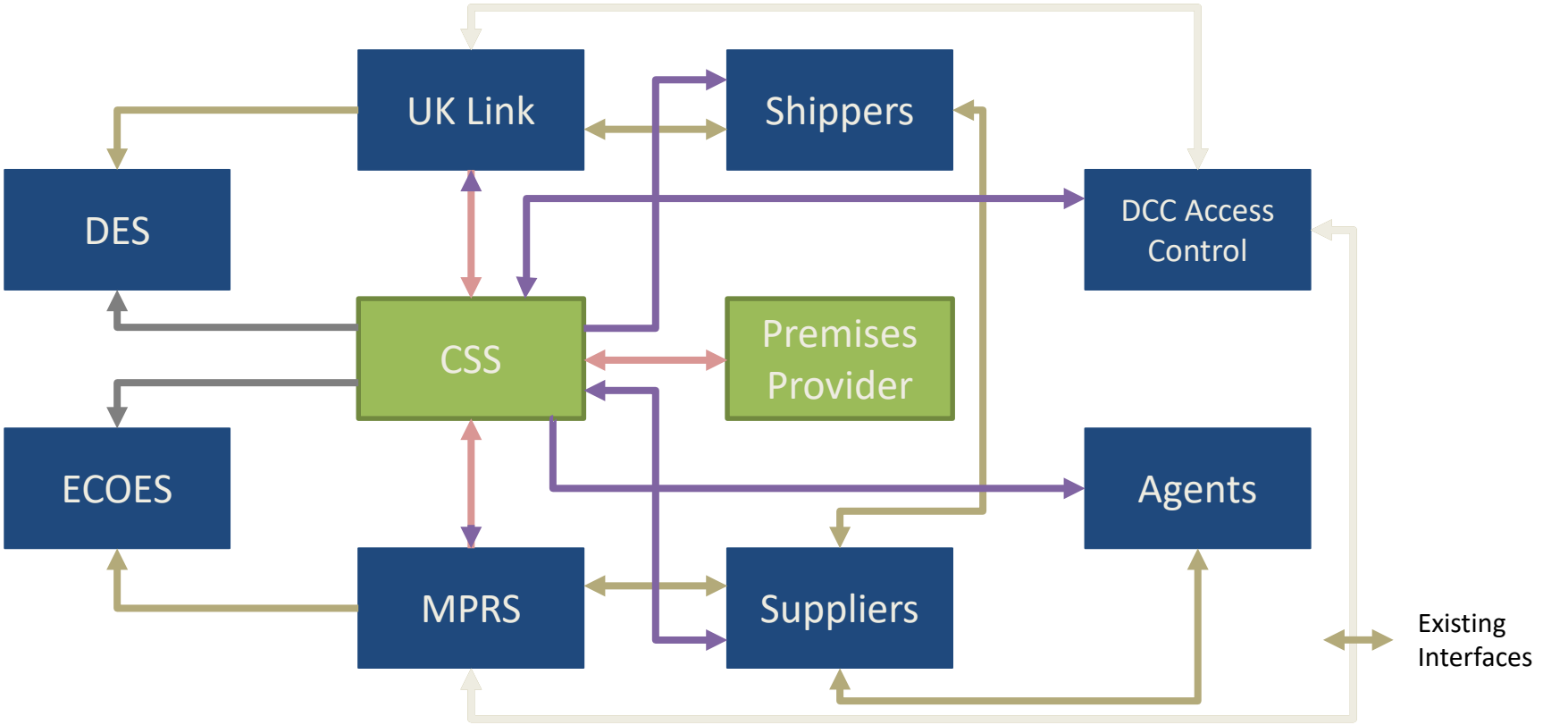
Stage 1	Stage 2	Stage 3	Stage 4
Data migration to MPRS and UKLINK	Migration of meter Point and Registration data migration to CSS	**CSS GO-LIVE:** CSS becomes live registration service, offering 5 day switching with 1-day (domestic) or 2-day (non-domestic) objections window	**CSS GLIDE PATH:** 5-day switching moves to end-of-next-day switching
	Premises address data improvement service implemented and used to populate CSS	CSS becomes live RDP interface to DCC Access Control; MPRS and UK Link to DCC Access Control interfaces retired	
	Production interfaces to UK Link, MPRS and Premises Provider tested in live environment (interfaces to MPRS and UK Link 1-way at this point)	CSS registration interfaces with suppliers and notification interfaces to Shippers and Agents go live	
		Adoption of new cooling off approach	

KEY
Pre-CSS development activity
CSS development
Implementation of policy change and related systems

STAGE 2
Meter Point and Registration data migration to CSS
Premises address data improvement service implemented and used to populate CSS
Production interfaces to UK Link, MPRS and Premises Provider tested in live environment (interfaces to MPRS and UK Link 1-way at this point)

STAGE 2 (PRE-CSS GO LIVE)
CSS Interfaces to Enquiry Services tested in live environment (but CSS data is not accessible at this time though DES and ECOES)

STAGE 3 (CSS GO-LIVE)
CSS becomes live registration service; registration interfaces with suppliers established
Retire MPRS and UK Link to DCC Access Control (RDP) interfaces
CSS becomes live RDP interface to DCC Access Control
CSS notification interfaces to Shippers and Agents go live



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Benefits of a staged approach

- **De-risks implementation of individual aspects of the programme's functionality.** Individual components and production interfaces are exposed to a near-live environment after testing.
- **Allows transition to occur at the right pace for the programme.** Transition can be advanced once each preceding stage is sufficiently robust and has cleared approval gateways.
- **Consistent with proposed 'glide path' under Reform Package 2a.** Initial 5-day switch creates an opportunity for staged implementation of instant/2-day objections window, further minimising risk of ETs after CSS go-live.
- **No dual running.** Retains all the key benefits of a 'big bang' approach (no dual running, benefits to all consumers at the same time).

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Questions for EDAG

- Do you agree that phased implementation of the CSS (and associated policy changes) offers a better chance of stable go-live when compared to a single 'big bang'?
- Are there changes to the proposed approach to staging contained in this presentation that EDAG members would like to see?
- Are there potential risks to go-live from policy changes (such as the new cooling off mechanism and objections) which are otherwise separate to CSS delivery?
  - If so, what are these risks and how significant are they?
- Should we be thinking about some sort of 'controlled market entry process for the initial period of CSS running? If so, what sort of risks should be targeted?

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