Andy MacFaul
Consumer Policy Team
Office of Gas and Electricity Meters
9 Millbank
London SW1P 3GE

28 April 2015

Dear Andy,

Re: Opus Energy Response to 'Supplier Objections: a call for Evidence' dated 27 Feb 2015

We write to provide our response to the above call for evidence.

About Opus Energy

Opus Energy is a supplier of gas and electricity to business sites in the UK. We supply energy to approximately 250,000 supply points covering both the SME market and the I&C / Corporate business market. We have over 600 employees in the UK, based in Northampton and Oxford. Group turnover for FYE 2015 was £524 million.

Our View on the Proposed Options

We are strongly against the proposed options outlined within Section 4 of the call for evidence - numbered '2' (removing a supplier's ability to object for **debt** for non-domestic customers) and '3', (removing a supplier's ability to object due to **contractual rights** for non-domestic customers).

We consider that the implementation of any such arrangement along these lines would be cause serious harm to the markets for the supply of energy to the business sector and to business customers. It would damage Opus Energy's ability to compete in this marketplace and would impact our ability to offer competitive products to the market.

Specifically we consider the proposals would cause:

- Increased prices for business customers
- Material increase in levels of customer dissatisfaction amongst business customers
- Decreased competition in the energy sector
- Reduction in the products available to business customers

Further details of these views are provided below.

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1. Increased prices for business customers

<u>Objecting for contractual term commitments</u>

Electricity and gas are commodities traded in a volatile market. When a customer agrees to enter into a fixed term contract with a supplier there is a contractual agreement made between the two parties. On the one hand, the supplier agrees to fix the price (by entering into a forward contract on the wholesale markets) and on the other hand, the customer agrees to take delivery of the commodity over the duration of the fixed term. If the business customer does not want to enter into this type of agreement, they have the option to enter into a variable rate agreement or an evergreen product instead.

Without the right to object for contractual term, the supplier must take on the associated risk of the wholesale market price moving after the customer's forward energy needs have been secured in the wholesale markets. This is a complex cost (since it is related the 'mark to market' risk of the contract term) and can be very material.

For example, take a scenario where a business customer has fixed in their energy price at £60/mwh for 3 years, but then choosen to leave half way through the first year. If the market in the meantime has fallen to £40/mwh (a material but not unprecedented fall), the supplier would be left with a stranded cost equivalent to around 6 months' worth of total energy cost for that customer. (ie (£60 - £40) x 2.5yrs worth of demand). An independent supplier would have to charge the customer for these liquidated damages. This complex cost may be difficult for a business to understand, particularly a small business, since it is derived from what appears to be a small change in the wholesale curve (ie of 33% in this given case). Recovery of this cost would be difficult and would be likely to create customer dissatisfaction. The cost cannot be borne by the supplier since (where the customer has left) there is no longer any income relating to the supply to the customer.

This is "wrong way" risk for the supplier since the probability of a customer wanting to leave when the market has fallen rises significantly (since the business customer now has a financial incentive to break their energy contract). Businesses are much more likely than domestic consumers to react to such pricing signals and attempt to leave the contract early in this situation. The cost of this "wrong way" risk is significant and when applied to business contract rates, is likely to be material.

<u>Objecting for where debt has accumulated</u>

If the ability of suppliers to object for debt were removed, the only recourse open to suppliers will be to pursue such debt through the courts. This is a time consuming and expensive process. Removing the debt management tool of objection will drastically increase the overall cost of debt recovery for the industry.

This increased cost will be borne both by those customers who fall into debt and (where such debt is not recovered) by the wider business community through increased prices.

We do not agree that this would create a net benefit for business consumers. It must further be noted that there is currently budgetary pressures on the courts and the likely flood of new cases that would have to be raised by energy suppliers would be problematic. It would seem strange that where there is this budgetary pressure, the energy industry should consider abandoning a cost effective tool which encourages prompt payment and final support of debt.

2. Significant increase in customer dissatisfaction

We consider that the material cost of court action, which would be borne by business customers struggling with debt, along with the time that would be taken up by customers dealing with the court action is likely to lead to higher levels of dissatisfaction among business consumers.

It is also likely to the be the case that suppliers will refuse to supply those customers with debt issues who are attempting to move supplier and that suppliers would be less willing to take on customers whose credit profile is slightly negative. That means that struggling businesses are more like to end up supplied under Deemed or Out of Contract rates.

Where low credit score customers are unable to secure a new fixed product with their current supplier at the end of a fixed term, or secure a new product with a new supplier, they may end up stranded on expensive out of contract rates.

3. Decreased competition

Where the cost of providing a fixed rate contract (without the right to object for contract) is too great for an independent supplier to bear or to pass onto the business customers, the supplier will need to withdraw from offering fixed rate contracts. This will force the market towards supply based upon evergreen tariffs with a short term (ie domestic type) hedging strategy.

This would pass a significant competitive advantage to the Big 6 who can hedge these microbusiness customers along with their domestic portfolio, ie within their vertically integrated hedging strategy where back to back hedging with the market place is not needed. Conversely it would reduce the number of independent business-only suppliers offering fixed rate products to the market place.

We consider this would be a severely retrograde step for the industry to take, would benefit the 'Big 6', harm competition and would, when taken on a net basis, harm business consumers.

4. Withdrawal of Products

For the reasons outlined above, the removal of rights to object for contract and debt is likely to reduce the diversity of products available to business consumers.

- Suppliers will tighten the credit criteria surrounding which customers they were happy to take on. The unintended consequence of this could be that a higher number of customers are left on out of contract rates, unable to secure cheaper fixed rate deals.
- Due to the uncertainty of customers transferring, suppliers are potentially likely to only offer very short term contracts or evergreen contracts.

Summary

We consider the proposals to remove rights to object for contract and debt in the business sector would have a net effect of harming business consumers. We are not even of the view that it will increase switching. Instead it will lead to a reduction in switching as customers face a reduction in products available to them and a reduction in the number of suppliers offering products.

Please do not hesitate to contact me with any queries.

Yours sincerely,

Gemma Newsham
Regulations Manager

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