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Default Tariff Cap: Policy Consultation

June 2018

Summary

Bulb is supportive of the default tariff cap, which we believe will benefit consumers and make the market more competitive. In particular, we support Ofgem's intention to close the green loophole and have no exemption for renewable tariffs. However, we have significant concerns that the proposed methodology for wholesale costs could have unintended consequences, leading to [XXXX] and a reduction in both competition and innovation in the market.

Bulb has grown significantly over the last three years - whilst delivering great customer service and value. We now supply 100% renewable electricity and 10% renewable gas to over 450,000 members.

At Bulb, we have a single 'Vari-Fair' variable tariff, which means all our members are always on our best rate. This tariff reflects the true wholesale cost of energy, and means we're quick to pass on savings to consumers when any part of our cost base, including wholesale costs, decrease. That's why we have lowered our prices seven times since launching in late 2015.

This is different to how the vast majority of suppliers use Standard Variable Tariffs (SVTs). SVTs are usually deemed tariffs that disengaged customers mature on to. It's important to remember that not all variable tariffs are expensive deemed tariffs, and that variable tariffs can deliver better value to consumers than fixed price tariffs.

In this context, we're concerned that the proposed methodology for both setting and updating the wholesale allowance within the cap will have a number of consequences which undermine the overall value of the price cap to consumers. In particular, we believe this methodology will:

1. Reduce the ability for suppliers to quickly pass on savings to consumers as wholesale costs go down (by making suppliers hedge up to 20 months in advance and codifying the common excuse of the "Big Six" suppliers for not doing so).
2. Increase prices for consumers (as smaller suppliers would be forced to adopt long-term hedging which requires large amounts of working capital / significant premiums to investment banks, or oil majors who provide liquidity for smaller suppliers).
3. Stifle innovation and competition in the energy supplier market, whilst benefiting the Big Six (by forcing suppliers like Bulb with innovative pricing models to hedge as the Big Six do).
4. Reduce transparency for the public (as the wholesale update mechanism isn't easily explainable to consumers and perpetuates the myth that energy bills are complex).

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QA6.1: Do you agree with our approach to setting the wholesale allowance? In particular using 2015 for the base period of the adjusted existing safeguard tariff approach.

We have no issues with using the 2015 base period.

QA6.2: Do you agree with our approach to updating the wholesale allowance?

No - the proposed methodology means [XXXX].

Bulb's current strategy is to buy energy [XXXX]. This means that our tariff better reflects the true cost of energy, rather than the complex proposed index which reflects traders' relatively long-term expectation of prices.

The proposed approach would [XXXX], and [XXXX]. A common criticism of large energy suppliers is that they are quick to increase prices and slow to reduce - and a common excuse made by the Big Six suppliers for not doing so is that they hedge in advance. By implementing the proposed approach, Ofgem would codify this excuse, resulting in greater distrust and disengagement.

We propose that the wholesale allowance be based upon ICIS Heren prices for the next 12 months at any one time, rather than the 12-month period following a 6-month observation period. This would be a far more dynamic cap that reflected the real cost of energy, rather than reflecting wholesale prices from many months before. We would be happy to run through our proposal in more detail with Ofgem.

Question A6.3: Do you agree with our proposed approach to use a semi-annual cap period, compared with a 6-2-12 annual model, or shorter observation period? Please explain how the alternatives would affect you, if we were to choose those options Instead.

We are in favour of shorter observation periods, and shorter cap periods. We prefer the semi-annual cap period to an annual cap period. However, we believe all of these approaches would stifle competition and increase costs for consumers

QA6.4: Do you agree with our approach to modelling forward contracts? In particular: that initial shaping should be based on a 70-30 split between baseload and peakload, and the cap will be semi-annual. If not, please provide evidence to support alternative approaches.

We believe 70-30 is the correct split between baseload and peakload.

Question A6.6: What are your views on the necessity and size of an additional allowance for transaction costs relating to brokers and collateral?

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There should be allowances for collateral under the proposed methodology as the cost of hedging 20 months in advance ([XXXX]) would add [XXXX] to the average consumer's bill through additional collateral costs. In our experience, broker costs are[XXXX].

There should also be an allowance in the cap for Unidentified Gas costs / working capital

QA13.1: Do you agree with our minded-to positions not to provide exemptions for renewable electricity or gas tariffs?

Bulb supports closing the green loophole by not providing exemptions for renewable electricity and gas tariffs.

As we have stated publicly, we are concerned that any exemption for green tariffs could be exploited by unscrupulous suppliers to continue charging households unfair prices above the level of the cap. The Chief Executive of Ofgem, Dermot Nolan, has himself pointed out that suppliers "*may try to game*" this exemption in his oral evidence to the Business, Energy and Industrial Strategy Select Committee during its pre-legislative scrutiny of the draft Domestic Gas and Electricity (Tariff Cap) Bill inquiry last year.

The Minister for Energy and Clean Growth, The Right Honourable Claire Perry MP, also correctly outlined the risks of allowing for such as exemption for green tariffs when she told the House of Commons in the second reading debate of the legislation on 6th March that, "*Ofgem has never been required to scrutinise existing green tariffs… the expectation will be that customers should not have to overpay to be on a green tariff*".

Moreover, Bulb believes that a green loophole in the price cap legislation would perpetuate the myth that renewable energy need be more expensive than non-renewable energy. A search on price comparison website uSwitch reveals that, again for a typical London property, there are 48 green tariffs available for households. For EDF and npower customers on a SVT, only two of these 48 tariffs cost more. For British Gas, Scottish Power, EDF or SSE customers on an SVT only four green tariffs cost more.