Response to DECC Consultation on
Ensuring a better deal for energy consumers

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Summary

The DECC consultation sets out “a package of proposed measures that are designed first and foremost to ensure consumers get the cheapest tariff offered by their supplier that meets their preferences. The package will also enhance overall consumer protection and enable consumers to compare different suppliers’ tariffs and to switch more easily.”

Those measures set out in Section 1 of the consultation, mainly based on Ofgem’s simpler tariff proposals, propose to limit the tariffs that suppliers can offer and/or force suppliers to put consumers onto the cheapest or best tariffs. Other measures set out in the rest of the consultation seek to enable customers to engage more effectively in the competitive market without restricting or distorting that market.

The general aim of the policy – to protect the interests of customers by enabling them to get better tariffs - is laudable. However, the first group of measures will have the opposite effect. They will make customers worse off by reducing choice and making competition less effective, leading to higher prices and supplier profits. At a time when customers generally, and fuel poverty customers in particular, are very sensitive to energy price increases, it seems indefensible to implement measures that will increases energy prices further. In contrast, many of the other measures proposed by DECC could be helpful to customers, and merit further investigation.

The following comments take in order the six sections of the DECC consultation paper.

1. Simpler tariffs and the cheapest tariff for you

I have argued in response to Ofgem’s recent consultation that its proposals to simplify tariffs will make all consumers worse off, including those that it is intended to help. This is because these measures will i) lead suppliers to remove their best tariffs from the market ii) prevent the suppliers from offering a full range of tariffs to meet the different needs of different customers iii) effectively prevent innovation because of the limited number of tariffs allowed iv) reduce the extent of competitive pressure on the remaining allowed tariffs and v) facilitate the coordination of prices and tariffs by the existing suppliers. The consequence will be less choice, less competition, higher tariffs and higher profits for the suppliers.

A copy of my response to Ofgem’s consultation is attached to this present response to DECC. I note that Professors Waddams and Loomes of the UEA Centre for Competition Policy, in their response to Ofgem, make a number of similar points based on their own empirical evidence.

The proposed tariff simplifications will not increase customer engagement or customer switching between suppliers as Ofgem hopes. Evidence produced by Ofgem itself shows that customers are primarily motivated to engage and to switch, not by tariff simplicity or more information, but by attractive tariff offers supplemented by supplier advertising to bring these offers to customers' attention. The proposed measures will severely restrict the ability and incentive of suppliers to make attractive offers. In consequence, competitive pressure on suppliers will be less than now, not greater. This will further increase prices and profits.

Since 2009 Ofgem has increasingly intervened in the retail energy market, purportedly to protect less active customers and to make the market more competitive. There is now empirical evidence that the outcome has been precisely the opposite. These measures have restricted and distorted competition, customer switching has declined, and prices and retail profit margins have increased. The calculations in my evidence to Ofgem, based on Ofgem's own data, suggest that, over the last three years, energy customers have been paying nearly £2 billions per year in higher net margins (profits) to suppliers as a result of Ofgem's measures. Furthermore, during 2012 most of the major suppliers responded to Ofgem's call for simpler tariffs, and Ofgem's own projections suggest that suppliers' net margins will increase by a further £1 billion per year in 2013.

If there are other reasons for these increases in tariffs and profit margins, Ofgem has not explained what they are. The measures that Ofgem now proposes, and that DECC endorses, can be expected to further increase prices to customers and profits to suppliers.

DECC proposes certain restrictive measures in addition to those proposed by Ofgem. Specifically, it proposes to require that the four "core tariffs" contain one standard variable rate tariff, and one fixed term fixed price tariff, that are comparable like with like across the market. This will make things worse. It will prevent suppliers from specialising or offering tariff variants that some customers prefer, thereby further restricting choice and innovation. It will also further encourage suppliers to coordinate their tariff offers, leading to higher tariffs with less scope for customer savings from shopping around.

2. Clearer information

Ofgem proposes to require suppliers to give personalised estimates of savings from moving to the supplier's cheapest tariff, and to provide a tariff comparison tool. As explained in my response to Ofgem, there are pros and cons: these measures could be helpful to some customers but they will be costly to provide and the costs will fall on customers generally; more information is not necessarily better information; more information will not necessarily provide the stimulus to engage in the market – or even to read the information; Ofgem has already taken previous steps in this direction and it is not clear why the proposed measures would have any greater effect; the measures could encourage more coordination between suppliers rather than more competition; there is no shortage of tariff comparison websites for those consumers that want that; these websites are better placed than Ofgem or DECC to discover what sort of information customers want and how to present it; and the measures could make customers frustrated rather than satisfied if lower tariffs necessitate conditions that customers are unable or unwilling to meet (eg direct debit or online billing). But it is worth discussing these issues with suppliers and customer groups, and Ofgem, to see if these potential disadvantages can be overcome.

3. More help for vulnerable customers
4. Helping you to switch
5. Facilitating collective purchasing and switching

Proposals to work proactively with vulnerable customers seem a sensible route to understanding the situations faced by vulnerable customers and to assisting them to engage effectively in the market. Quick response codes sound an imaginative, useful and potentially pro-competitive idea. Collective switching is perhaps more effective in markets where individual switching is less well developed than in GB, but it could play a useful role in the market. I suspect that its main contribution will not be by securing a better deal than an individual could negotiate, but by encouraging or assisting consumers to switch that would otherwise not do so. In that way, it could enable them to take greater advantage of what the market can offer. All these proposals deserve further discussion with those more closely involved in the retail energy market. There would also be merit in widening the discussion to include those in other sectors, such as banking and supermarkets, that might be able to play a part in increasing the effectiveness of retail competition.

6. Third party intermediaries

Third party intermediaries do play a significant role in the small business sector, but to date their role in the domestic market has been limited. There may or may not be a significant increase in third party intermediaries operating in the domestic market in future, and this may or may not prove problematic. These outcomes remain to be seen. A danger of premature regulation is that innovatory intermediary activities that could be useful to customers could be prevented, discouraged or unduly constrained. Moreover, Ofgem's record on retail competition is now questionable, and there could be a danger of it imposing regulatory restrictions that are harmful to customers rather than helpful. It would therefore seem premature to assume that intermediaries will emerge on a significant scale in the domestic market, that they will be a problem, that more regulation will be the answer, and that Ofgem will be best placed to regulate them. Regulation of third party intermediaries is an issue that can be addressed in due course, on a more informed basis, if indeed it actually turns out to be a problem.