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Making a positive difference
for energy consumers

Consumer and Competition Policy
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Dear Sir/Madam

Response to government's consultation paper 'Reforming Competition and Consumer Policy: Driving growth and delivering competitive markets that work for consumers'

This letter forms Ofgem's response to the consultation on 'Reforming Competition and Consumer Policy' dated 20 July 2021 (the "consultation paper"). Our response focuses on the chapter 3 proposals about enhanced consumer law enforcement, and chapter 1 proposals about competition policy. We will also engage with your team separately about some of the more detailed questions about consumer law enforcement and other reforms.

Ofgem's position has consistently been that we would welcome improvements to our existing consumer law powers. These would enable us to regulate the energy market more effectively than we can at present. This is particularly important as energy consumers will increasingly engage with a broader range of companies, many of which are not regulated under our current sectoral regime. Maintaining consumer confidence in these markets will be crucial to support our journey towards net zero.

As the market changes, we need a regulatory framework that both supports innovation and allows us to respond promptly to any emerging consumer protection issues. In our view, being able to apply an administrative model for consumer law enforcement will help us achieve these aims.

Consumer law enforcement

The consultation paper seeks views on applying an administrative model for the delivery of consumer law enforcement to sectoral regulators.[1] This section of the letter sets out our response to this question. Broadly, we consider that energy consumers would benefit from Ofgem being able to apply an administrative model for enforcing consumer law. We also welcome the confirmation of fining powers for consumer law breaches, which will complement the benefits of an administrative model.

There are two areas where we think an administrative model will deliver better outcomes for energy market consumers:

1. Addressing harms arising in new and emerging areas of the energy market
2. Improved ability to enforce consumer law more efficiently and effectively

<u>Addressing harms arising in new and emerging areas of the energy market</u>

The energy market is undergoing significant change. New technologies and players are emerging which are changing how consumers interact with, purchase, and use energy services. The provision of energy is evolving from a hierarchical system where energy flows predominately through networks to consumers, to a much more decentralised system, optimised by technology, where energy consumers can also be also energy generators.

In this market, consumers will interact with a wider range of businesses such as intermediaries, energy service providers, equipment installers, peer-to-peer traders, and demand-side response agents. This new energy system will bring many benefits to consumers, including a decarbonised system that achieves our net zero objectives.

This new system will also create new risks. Many of these new market participants fall outside our existing sectoral powers.[2] This makes it difficult for Ofgem to regulate their activities and make sure they treat consumers fairly. If left unchecked, consumer harm from firms outside our sectoral remit could significantly impact consumer confidence in the market, harming the adoption of new technologies and our drive towards net zero. Current events highlight the importance of energy costs to consumers and therefore of Ofgem being able to make sure consumers can access trustworthy services to help them make informed decisions and for us to address potential harms.

[1] Q60. Should sector regulators' civil consumer enforcement powers under Part 8 of the EA 02 be reformed to allow for enforcement through an administrative model? What specific deficiencies do you expect this to address?
[2] By this we refer to our enforcement powers in the Electricity Act 1989 and Gas Act 1986.

Access to an administrative model for consumer law enforcement will help us deliver credible and effective consumer protections, as market participants not subject to our sectoral powers become increasingly prevalent. In combination with new fining powers confirmed in the consultation, an administrative model would enhance our regulatory toolkit, enabling us to protect consumers from a wider range of potential harms and encouraging companies to comply, especially those outside our sectoral remit. In turn, our ability to enforce consumer law directly will create stronger incentives for businesses to treat customers fairly and so influence market behaviour for the better.

As the sectoral regulator, we consider we are best placed to identify issues as they emerge and to tackle them using our sectoral expertise. Our existing market monitoring activities make us well placed to identify consumer harms; through an administrative enforcement model we can address those harms more efficiently than at present using available enforcement resources. In conjunction with new fining powers, this would enable us to better prioritise our regulatory activities, and to take more effective action to target the issues that are causing immediate consumer detriment.

An administrative model only being available to the CMA could lead to situations where harmful behaviour occurs in the energy market that remains unchecked – potentially affecting large numbers of customers – as it may not be significant enough for the CMA to act. The CMA will have competing priorities that may limit the resources, or expertise, they can make available to address the range of consumer harms that emerge as the energy market rapidly changes. Enforcing consumer law through an administrative model would enable Ofgem to make more timely and effective interventions that not only limit the impact of those harms on the consumer but also send a strong signal to the rest of the market on what is acceptable conduct. This is particularly important as the energy market evolves and there is an increase in firms that are not subject to our existing sectoral regulation.

Improved ability to enforce consumer law more efficiently and effectively

Ofgem's main powers to enforce consumer law protections reside under Part 8 of the Enterprise Act 2002 and the Consumer Rights Act 2015. The Enterprise Act allows us to act where we have identified an infringement which harms the collective interests of consumers. The Consumer Rights Act enables us to act relating to unfair contract terms and notices. Broadly these powers provide us with the ability to seek undertakings from parties we consider have infringed consumer law or seek an appropriate order through the courts.

While these powers are welcome, we face several issues in proceeding with cases under the existing model. Firstly, we must apply to the court in circumstances where we consider a firm has breached consumer protection legislation or we otherwise wish to take action. This process can often be slow and require a significant amount of resource to determine if a case should be submitted to the courts.

Secondly, even if our case against a firm is upheld in court, sanctions can be weak. For example, a court can order firms to stop unlawful practices and pay compensation but, because currently there are no civil fines for breaches, breaches of consumer law can go unpunished, thereby undermining trust in the system.

Together, these reasons act to limit the number of cases we take forward under our existing consumer law powers. This is not the best outcome for energy consumers and a more efficient process will allow us to better prioritise consumer law issues against other enforcement actions considering the impact on consumers, resource commitments and the comparative opportunity cost.

The proposals for an administrative model need not change the scope of our existing powers. However, such a model will provide a faster, flexible, more efficient and less resource-intensive process for enforcing consumer law cases. It will allow us to provide the same benefits for consumers that the consultation paper sets out for the CMA. This includes being able to collect evidence more easily and intervene in situations where we think there is real consumer harm.

Taking on an administrative model would not increase the regulatory burden on businesses in the energy market. Ofgem already has the power to enforce consumer law. Rather, this would provide a means of running cases efficiently and effectively to the benefit of both consumers and businesses.

Enforcing consumer law through an administrative model would not necessarily lead to us significantly increasing the amount of consumer law actions we undertake. However, for the reasons given above, we do consider that we would look to use our powers more broadly in future and that clearly targeted action could have a deterrent effect as well as a direct impact on the case concerned. In addition, this model will avoid taking consumer law cases through a court-based model that can be costly in terms of resources, time, and cost for both Ofgem and businesses. In this regard, an administrative enforcement model should provide a more efficient process that is less burdensome for businesses.

Applying an administrative model would also allow us to better align consumer law cases with the enforcement of existing, sector-specific rules. We would use our experience and existing decision-making processes and panels to create synergies between sector-specific and consumer law cases. We would have wider options for determining what may be the most effective or efficient way to address consumer harms or detriment considering cost, resource, and timing benefits for Ofgem and businesses subject to enforcement action.

This in turn is also likely to provide more clarity and certainty for businesses across energy markets enabling a more level playing field between energy businesses regulated under our sectoral regime and those that are not. We know that many market participants in parts of the energy market we do not licence would welcome more clear and firm regulatory involvement from Ofgem. This would, for instance, help limit the actions of firms that cause detriment to consumers that can tarnish other firms active in the same space.

Being able to act more effectively through an administrative model would help us limit the actions of poorly behaving firms and improve overall market standards. This could also give government more time to consider broader, longer-term changes to the regulatory framework (eg noting the recent call for evidence from BEIS on third party intermediaries[3]) and may in turn limit the need for more onerous regulatory action to be taken in the future.

Competition policy - reforming the markets regime

This section of the paper provides our views on the two alternative proposals for reforming and improving the markets regime under the Enterprise Act 2002. Further details regarding these proposals were shared with us during subsequent discussions with BEIS, the CMA and the other sectoral regulators (hereafter "the regulators").

The consultation paper sets out two proposals for reforming the markets regime:

- Proposal 1: to retain the two-phased regime of market studies and market investigations and enable the CMA and the regulators to impose structural remedies at the end of a market study.
- Proposal 2: to replace the existing market study and market investigation system with a single-stage market inquiry tool to be reserved for the CMA alone.

We welcome and support the introduction of Proposal 1 due to the importance of market studies in sectoral regulation and to the likelihood of detriment that would result from removing these powers. We discuss these reasons in more detail below.

[3] *Third-party intermediaries in the retail energy market: call for evidence*, Department for Business, Energy & Industrial Strategy, August 2021

The importance of market studies in sector regulation

Ofgem places significant importance on the outcomes achieved through market studies and we have a record of using our powers in this area. For example, in November 2013 Ofgem launched a market study on how well competition in the energy retail market is serving the interests of households and small business in Great Britain (GB).[4] Following the adverse findings of that market study, in 2014, Ofgem made a reference to the CMA[5] for a full market investigation (the "2014 reference"). That investigation was wide-ranging, covering all aspects of the retail energy market, both the domestic and non-domestic segments,[6] and giving rise to a series of recommendations, implemented by Ofgem.[7]

We understand the rationale behind Proposal 1 is that the position under the current framework, according to which there is no separate power to impose remedies following a market study, does not allow for the efficient correction of competition issues. A power to impose remedies after the completion of a market study[8] (eg sale of assets or ownership separation) would allow a concurrent competition authority (such as Ofgem) to remedy any competition issues without having to either open a competition investigation or make a market investigation reference to the CMA.[9] Resolution would be achieved quickly and with fewer resources by the expert regulator for the sector.

For this reason, Ofgem supports Proposal 1.

Anticipated detriment from removing these powers

We understand that Proposal 2 would remove sectoral regulators' existing market study powers and replace them with a single-stage market inquiry tool, reserved to the CMA. This would represent the loss of an important tool for Ofgem in protecting consumers' interests in the energy sector.

In most sectors, the powers to conduct a market study under the Enterprise Act 2002 extend beyond regulated activities and regulated entities. This is true for the energy sector. That scope of powers aligns also with regulators' concurrent competition law powers under

[4] State of the Market Assessment | Ofgem
[5] Ofgem refers energy market for full competition investigation | Ofgem
[6] The CMA published its final report in June 2016 and decided on wide range of remedies, for implementation by Ofgem and other industry players.
[7] Ofgem has not prioritised a market study since its 2014 market investigation reference to the CMA due to the broad terms of this reference and the implementation of remedies arising from the CMA's report.
[8] The statutory timetable for a market study is currently 6 to 12 months.
[9] The statutory deadline for which is 18 to 24 months, with additional time to implement remedies, and it would be conducted by the CMA.

the Competition Act 1998 ("CA98"). For example, under the Electricity Act 1989[10] and the Gas Act 1986,[11] Ofgem's jurisdiction to exercise its competition powers under CA98 covers all licensable activities but it extends also to businesses offering services that are connected with or ancillary to licensable activities. Ofgem's recent CA98 investigations have concerned some such businesses.[12]

By removing market study powers from the sectoral regulators, a significant market monitoring and enforcement tool would be lost. While the removal of those powers may not affect Ofgem's ability to regulate businesses that are required to hold licences under the Gas Act 1986 and the Electricity Act 1989, a range of other businesses provide services in the energy sector that are essential to the operation of markets and affect consumer outcomes (for example, metering service providers, auto-switching services, price comparison websites and businesses providing back-office systems for energy licensees).

Withdrawing Ofgem's market study powers would limit our ability to address competitive issues arising in a rapidly evolving energy market. The information that can be obtained during a market study, concerning a broader range of parties, is likely to be particularly valuable in the coming years and should offer a robust evidence base to either introduce effective remedies (under Proposal 1) or to open a subsequent CA98 investigation, in respect of regulated and non-regulated businesses. As noted earlier, the latter are likely to become increasingly prevalent in the energy market.

While we recognise the rationale of Proposal 2 is to introduce a more streamlined and potentially resource- and time-effective process, we are concerned that this proposal may place over-reliance on the CMA to investigate aspects in each regulated market. This may lead to underenforcement in the future.

Considering the above, we would urge government to carefully consider the merits and downsides of the removal of sectoral regulators' market study powers, and the potential detriments to the markets regime overall and for the regulated industries. We understand that our concerns, as set out above, are shared by other sectoral regulators.

Yours faithfully,

[redacted]

[redacted]

[10] Section 43
[11] Section 36A
[12] Those businesses include back-office systems-providers, sales agents, price comparison websites and operators of power exchanges.