ENERGY MARKET INVESTIGATION

Summary of hearing with the National Association of Citizens Advice Bureaux operating as Citizens Advice, and the Scottish Association of Citizens Advice Bureaux operating as Citizens Advice Scotland, on 14 October 2014

Background

1. Citizens Advice and Citizens Advice Scotland were providers of free, confidential and independent advice to the general public on legal and financial matters. Both organisations provided a dedicated phone service for complaints about the energy market and in aggregate had approximately 74,000 and two million annual contacts with the public by means of phone and website respectively. They also offered advice from 3,500 locations in England, Scotland and Wales.

2. Citizens Advice Scotland hosted a dedicated complaints team known as the Extra Help Unit where it provided complaint handling services to vulnerable consumers across Great Britain. This unit dealt with between 7,000 and 8,000 consumers a year.

3. Citizens Advice and Citizens Advice Scotland also delivered programmes on behalf of Ofgem and the Department of Energy and Climate Change (DECC) such as the Energy Best Deal and the Big Energy Saving Week.

4. Within Citizens Advice was an energy policy team which had been part of Consumer Futures (a non-departmental public body which represented consumers across regulated markets) until April 2014 when it was abolished under the Public Bodies Act and its functions transferred to Citizens Advice.

5. Citizens Advice’s policy function included being a statutory consultee and providing a consumer advocacy voice in government policy development, representing domestic consumers and small businesses. It had direct contact with energy suppliers to help address consumer detriment through the distribution of best practice and it also publicised performance information to inform consumers and drive competition in the energy market.
Trust and transparency in the energy market

6. Recent research of consumers showed that trust in the energy sector was very low. Polling by Edelman’s Trust Barometer indicated that the energy sector in the UK was less trusted than in any other country polled from the developed or developing world. The same source also noted that the energy sector was the joint least trusted sector in the UK alongside the banking industry.

7. Customer insight research by Which? for September 2014 also showed that the energy sector was the second least trusted of 13 service provision sectors in the UK, while YouGov polling in September 2013 showed that 56% of people polled agreed with the statement that energy companies treated people with contempt while only 7% disagreed. Another YouGov poll in December 2013 found that only 3% of consumers fully believed suppliers justifications for price rises, with 57% saying they did not believe them at all.

8. The drivers for this lack of trust included the sense of dissatisfaction that consumers felt having experienced poor customer service from a large energy supplier and at the same time receiving significant increases in the cost of their average bill. Consumers were also dissatisfied with the way price rises were conducted which gave a perception that the larger suppliers all acted in the same way. Another factor was the lack of agreed narrative that existed on why price rises took place with different parties within the sector (suppliers, government agencies) blaming each other for each rise.

9. To restore trust within the sector Citizens Advice hoped that the Competition and Market Authority’s investigation would help remove the lack of consensus that existed on the profits obtained by suppliers and would place pressure on suppliers to provide attractive tariff options to all types of consumers and not just those in more attractive demographics.

Complaints and standards of service

10. Citizens Advice collected data on customer complaints and standards of service from a variety of sources. Since 2010 it had published a league table based on third party complaints data from three sources: phone calls requesting advice from Citizens Advice including those cases where the consumer was referred to an escalated level of a supplier’s customer service team; the complaints recorded by the Extra Help Unit; and complaints data received from the Energy Ombudsman. It was noted that the rate of complaints to the Ombudsman had recently increased significantly.
11. There were three distinct features from the published data. The first was that billing complaints were the most common and made up approximately 80% of all complaints. The second feature was that there had been a fall in complaints about how products were marketed to consumers. The third feature was that there had been a fall in the number of complaints around transfers, e.g. consumers that switched between suppliers.

12. The increase in complaints to the Ombudsman was due, in part, to two of the largest energy suppliers: RWE Npower and Scottish Power. Citizens Advice said that this was due to the implementation of new customer billing systems within each organisation and the impact this had on customer service. However, it noted that the recent politically sensitive environment surrounding the energy market along with the increasingly high proportion of consumers’ income being used to pay for energy could also have contributed to an increase in complaints.

13. Citizens Advice only published company performance data on the largest domestic energy suppliers but had recently gone out to consultation with plans to include information about independent suppliers within its performance matrix. Its future plans also included publishing a league table of non-domestic supplier performance. It was also at the initial stages of exploring with Ofgem how to better collate comparative information around customer service and price comparison to better inform consumers.

14. There was inconsistency in the way direct complaints were recorded, and Citizens Advice worked with suppliers to ensure that the data it received was accurate and consistent. It was conscious that unreliable information would not be helpful to consumers and could provide some suppliers with an unfair competitive advantage if they were not recording their complaints data correctly.

15. It was not aware to what extent consumers used Citizens Advice’s complaints data when deciding which energy supplier to switch to. A previous Citizens Advice survey showed that approximately 6% of consumers thought that service was a bigger consideration than price when deciding on their supplier. Price was, overwhelmingly, the biggest consideration for consumers when choosing supplier.

Views on competition in the energy market

16. The energy market was segmented, and the level of competition differed quite markedly between different segments. The market for customers who paid for energy by monthly direct debit through online channels had a fairly significant level of competition as smaller suppliers had taken some share of that market
from the larger incumbent suppliers. Citizens Advice was concerned however that the larger suppliers had not responded to this level of competition, and might be prepared to sacrifice their market shares to maintain the higher tariff prices they charged to customers who did not have a propensity to switch supplier.

17. There were some smaller suppliers who sought to attract new customers by offering cheaper energy prices, while some focused on attracting consumers who were interested in buying environmentally friendly energy. Some smaller suppliers were exempt from certain environmental policy costs which might have artificially made some suppliers more competitive on price than those who were exposed to these costs.

18. The level of competition in Scotland was also highlighted as three companies retained approximately 80% of the market share: Scottish Hydro (SSE), Scottish Gas (Centrica) and Scottish Power. One reason was that dual fuel tariffs were not available in some parts of Scotland as a significant number of consumers did not have access to gas, and switching to a dual fuel deal was the most common switching behaviour. A proportion of customers in Scotland were also reliant on electric or oil heating which were often more expensive alternatives to gas heating. As a result there was a feeling among these consumers that this was unjust that they had to pay more for their energy as they lived in remote locations.

19. Citizens Advice did not observe much competition in the market for consumers who used pre-payment meters. 16% of consumers used pre-payment meters and for these consumers there was a lack of attractive tariffs to switch to. There also existed significant barriers to switching payment method for these consumers as their pre-payment meter would need to be replaced by their supplier, which would incur a financial cost. Consumers without access to basic banking facilities or those who did not wish to use a direct debit facility due to fluctuations in their levels of income would also be prevented from accessing the more attractive monthly direct debit tariffs. While access to a pre-payment meter was not synonymous with poverty, it was less likely that a consumer who used a pre-pay facility, or did not have access to a basic bank account, would be in a prosperous demographic.

20. The impact of Ofgem’s retail market review (RMR) was unknown as the complete package of reforms had not yet been in place for a long enough period of time with which to judge effectively. Citizens Advice felt that the reforms focusing on ensuring that tariff information was more easily available should help increase the level of consumer knowledge and engagement in the market. It had previously expressed concern about the large number of tariffs available to consumers prior to the review and was keen to understand what
impact the four-tariff limit would have on the market. The limit had resulted in suppliers ceasing to offer tariffs with no standing charge, and this had impacted on consumers with very low consumption who had seen the costs of maintaining their supply rise.

21. Citizens Advice had analysed data from the company Energylinx and noted that there were 117 tariffs available from all suppliers in the market. Of those tariffs 10% were available to users of all payment methods, 89% were available to consumers who paid by direct debit, 35% were available to those who paid by standard credit and 10% were available to those who had pre-payment meters.

22. Citizens Advice argued that the market was more interested in engaging with consumers who paid by direct debit than those who paid by other methods. It suggested that those customers who did not feel engaged would not look to switch supplier. The personal circumstances of consumers could also drive disengagement, which might sometimes be rational behaviour. For example, some consumers who lived in private rented accommodation may not switch supplier as they may not have lived in that property for long enough to benefit from a fixed-term tariff, or might lack the familiarity of how much energy was needed to light and heat that property to make an accurate price comparison.

23. The Consolidated Segmental Statements produced by the largest suppliers had shown a significant shift in their sources of profit over the period from 2009 to 2013, with an approximate billion pound per year shift from generation to domestic supply. If competition in the retail market was significant, Citizens Advice would not have expected vertically integrated companies to have been able to offset more challenging conditions in the generation market by taking more profit in the supply market, as competition in the latter should have eroded these margins away.

**Switching suppliers**

24. Consumers who had a monthly direct debit tariff primarily switched supplier through price comparison websites. The main channel for consumers who were not engaged with regularly or did not have a monthly direct debit tariff was by face-to-face or telesales methods.

25. The Confidence Code for price comparison websites was originally an instrument that Citizens Advice used as a Code of Practice to govern energy price comparison sites. The Code was passed to Ofgem in April 2013 and Citizens Advice believed it should be strengthened so that it could be extended beyond web-based channels to cover face-to-face and telesales services. Citizens Advice was also concerned about the willingness of price
comparison sites to show all tariffs available in the market given that the majority of sites required an income, through commission from suppliers, in order to maintain their business models that make their site free to use.

26. Citizens Advice was in favour of collective switching and had urged Ofgem to introduce a fifth collective-switching tariff as part of the RMR reforms. It had received data from collective switching companies such as iChoosr that showed there was an increasing number of people who would traditionally not have had the propensity to switch supplier going through with a collective switch. It considered that collective switching could also potentially drive improvements in tariff design given the auctioneer’s ability to stipulate the features of the product that suppliers were bidding to supply. This could provide a mechanism to stimulate simpler tariffs, and minimise features that potentially sterilised competition such as substantial exit penalties, without the need for formal regulation of product design.

27. Citizens Advice’s Switched On report from 2012 reported that consumers within the social demographic groups D and E had the lowest switching rate and were less likely to switch again in the future. This was because of the length of the switching process and the financial problems consumers had encountered by receiving the final bill from their old supplier and the first bill from their new supplier at similar times.

28. Citizens Advice would not wish to prescribe a percentage figure for what a healthy level of switching was in the energy market. It had concerns that focusing simply on the level of switching could provide a misleading picture of how well the market was performing, and that the quality of switching and who was switching needed to be taken into account. Ofgem’s 2008 Energy Supply Probe had revealed that a high proportion of consumers found themselves worse off as a result of switching – particularly when the switch was made through a face-to-face sales channel. Any measure of success would have to take into account whether a consumer who switched had found themselves with a better outcome based on the initial reasons why they had chosen to switch supplier – whether to save money, to choose a more environmentally friendly option, or receive better service. Given that energy was an essential service, it was imperative to see engagement across all demographics and not simply among those who might be considered most attractive to serve.

Codes of governance

29. Citizens Advice sat on two industry codes governance groups that oversaw the assessment of proposed changes to that code. The first group was the Balancing and Settlement Code where it could raise, and vote on, code modification proposals. It also sat on the Uniform Network code group where
it could vote on, but not raise, modification proposals. While it believed that engagement with these forums was beneficial, it questioned whether one consumer representative sitting among numerous industry representatives was a sufficient and effective way of scrutinising code modifications. It also doubted whether smaller supplies would have sufficient human resource to effectively influence the many codes of governance that made up the overall code governance structure.

Social and environmental policies

30. Citizens Advice had expressed concern about the design and the potential outcomes of government policies around energy efficiency. Firstly it believed that asking energy suppliers, companies who were generally not trusted by the general public, to deliver these policies was not the most effective way to deliver policy. It also queried whether it was a fundamental conflict of interest to ask companies whose core business was to sell more energy to sell less.

31. Using suppliers as the vehicle to deliver social and environmental policies also had an ongoing negative impact on public trust as suppliers were known to attribute consumer price rises to the rising cost of policy delivery despite the publically available data on the impact of policy costs on suppliers that suggested this might not always be the case.

32. Also by using consumer bill based levies to pay for energy efficiency schemes, all consumers were paying for a scheme which they might, or might not, receive the benefits of at a later date. This was leaving those consumers who would not receive such benefits more exposed to higher energy prices than if energy efficiency schemes were paid for through direct forms of taxation.

Smart meters

33. Citizens Advice was supportive of smart meter technology but was concerned that there was not a sufficient regulatory framework in place to ensure that the benefits of smart meters, such as accurate billing, were passed on to consumers. It noted that from the complaints it received, 10% of consumers that had early generation smart meters did not receive accurate bills, got estimated bills instead, or received no bill at all.

34. It also noted that the DECC impact assessment of smart meters reported that of the £5.73 billion savings the scheme would achieve, £5.69 billion would be delivered through behavioural change by consumers. However, with 50% of pre-payment meter users already rationing their energy use to the point that it affected their lifestyle, Citizens Advice found it difficult to understand how all
consumers in the market would benefit. It was also concerned that unless more was done to provide the benefits of smart meters, or additional extra help, to low-income consumers there could be a significant proportion of the population who would resist using a smart meter based on the perceived cost of having one. This would serve to undermine the smart meter business case overall.

**Fuel poverty**

35. Citizens Advice agreed that the Government’s strategy was correct in focusing on energy efficiency as the primary solution to fuel poverty and the targets to improve household efficiency by 2030. However, it questioned whether the strategy was ambitious enough in terms of what and when it would deliver. It also noted that there was a mismatch in the amount of money required to improve the energy efficiency ratings of all low-income households – where the Government’s strategy makes reference to an £800 million cost, Citizens Advice believed the cost of this policy would cost about £2 billion.

**Network regulation**

36. Citizens Advice highlighted that its joint response to the issues statement had called for network costs to be brought within the scope of the inquiry as the returns allowed to these companies was disproportionate, with even the least efficient usually outperforming their base allowed returns, which in turn had been set far higher than wider equity returns in the market. It argued that investment in the sector could still be attractive with lower returns.