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TELECOM PLUS PLC RESPONSE TO THE ENERGY INDUSTRY REMEDIES PUBLISHED ON 7 JULY 2015

Background

Telecom Plus PLC, trading as the Utility Warehouse, is the UK's only fully integrated multi-utility provider. We currently supply almost 600,000 members with more than 2.1 million services covering electricity, gas, broadband, landline and mobile telephony.

We are a FTSE-250 publicly listed company with a current market capitalisation of around £900m.

We operate as a Discount Club, providing our members with substantial savings. Whilst we do not claim to be the cheapest in the market for every service we offer, our members save money on each of their services compared with the price(s) they were paying their previous supplier(s), whilst benefitting from the convenience of a single bill covering all their utilities and award-winning customer service.

Our fully integrated business model enables us to spread one set of overheads across all the services we supply, and thus offer better value to our customers than if each service was being provided and billed separately.

We have always worked on the principle that all our members should receive our best possible prices at all times. As a result, we do not have any customers stranded on old or uncompetitive legacy tariffs, nor do we offer introductory tariffs to new customers which are cross-subsidised by charging higher prices to existing loyal members.

Delivering exceptional customer service to our members is critically important to us, as we rely upon customer referrals for the vast majority of our growth. Our customer service is provided by a dedicated team (all of whom are based in London), which responds to queries on all of the services we supply.

Executive summary

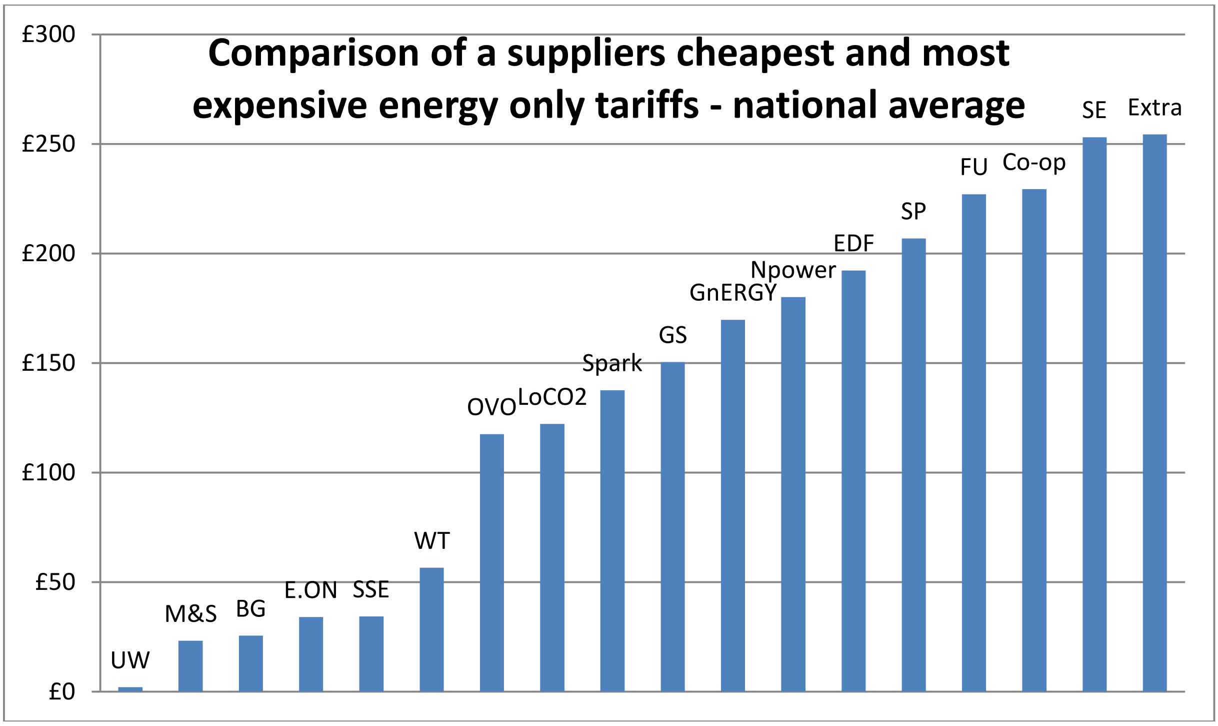
A severe lack of trust has been building up over the last few years within the UK domestic energy market, exacerbated by regular criticism from politicians, regulators and journalists who have focussed on the increasingly large gap between the Standard Variable Tariffs paid by most consumers and the much cheaper short-term fixed price introductory deals available to those who switch.

The industry as a whole has done little to dispel this criticism. For example, the 'Big 6' cited the proposed Labour price freeze as the reason why they could not reduce Standard Variable tariffs in line with falling wholesale commodity costs earlier this year. So post-election, once this threat had been lifted, one might logically have expected to see them announce rapid price reductions to these types of tariffs. Instead, we have seen them continue to invest the benefits of these lower prices in offering even more competitive introductory short-term deals to attract new customers, yet no changes (until British Gas' recent announcement of a 5% reduction in gas prices to take effect 27 August 15) to SVT tariffs on which the majority of consumers continue to be charged.

It seems to us inevitable that there will always be a substantial number of customers who have never engaged with the market by switching, or who, having switched, are unlikely to switch again - which can be for a wide variety of either positive or negative reasons. And there is clear evidence that these customers are in some cases paying significantly more for their energy than those who continue to switch on a regular basis to take advantage of the latest introductory deals.

The table below shows that virtually all energy suppliers (other than ourselves) are taking advantage of this inertia, using the extra profits they make from inactive customers to cross-subsidise the introductory fixed-price deals they offer new customers. This is being driven by a focus on price as the main (and in many cases sole) differentiating factor between suppliers, and the need to be at the top of the PCW tables in order to attract new customers.

This cross subsidisation of tariffs has become increasingly prevalent by the 'Big 6' over the past few years, and is now also starting to be seen in the pricing strategies of many of the independent suppliers.



Difference in annual cost (as at 23 July 2015) between the Cheapest Tariff and Standard Variable Tariff for each supplier, available to all direct debit customers, averaged nationally for typical consumption by a medium household.

We believe that it is fundamentally unfair that the vast majority of consumers, who for whatever reason have not switched recently, should pay significantly more for their energy (and in many cases to the same supplier) than those who have. On the other hand, we do not believe it is desirable for all consumers to switch suppliers on a regular basis, as this would simply increase administrative costs throughout the industry and lead to higher prices (in aggregate) for everyone than would otherwise be the case.

Your proposed transitional Safeguard Regulated Tariff ('SRT') potentially goes a long way towards protecting those customers who have not switched recently from being exploited by their current supplier, depending of course on the level(s) at which it is set, and we strongly endorse this approach. To minimise the scope for unintended outcomes and eliminate future debate and conflict over the most appropriate level in future, we suggest this new tariff is set automatically at 5% above the average of the cheapest tariffs available from all licensed suppliers during the previous quarter, and re-set on a quarterly basis. We are also concerned that this protection for consumers is likely to continue to be required in the medium term, and therefore do not agree that it should be introduced solely for a transitional period.

However, we still believe that a better solution to this unfair pricing issue, as we have previously suggested, would be the permanent introduction of a low single digit maximum delta (x %) between the Standard Variable Evergreen tariff and the cheapest fixed term tariff offered by any supplier at any given time. The advantage of this remedy would be that once set, it becomes entirely self-regulating with no further intervention or involvement needed from either the CMA or Ofgem. And fundamentally, if one supplier is more efficient than their competitors, then all that supplier's customers would benefit, not just those who have recently switched to them.

We are also concerned at the implicit assumption in your draft findings that it is better for consumers to be on Fixed Term tariffs rather than Standard Variable Tariffs, which would result in a significant transfer of future pricing risk onto consumers. The current environment where the vast majority of customers are on SVT's provides them with significant protection during periods of high commodity price volatility or rising commodity prices, due to the high proportion of future energy usage that is hedged by suppliers over an extended period. By contrast, if the majority of customers were on relatively short-term fixed price contracts, and suppliers only hedge their contracted revenues, then consumers will potentially face significant price rises when their fixed contract expires – further undermining consumer trust; and customers remaining on SVT's would experience greater volatility, as it will only be commercially viable for each supplier to hedge forward for these customers for much shorter periods.

Choosing a new gas or electricity supplier, whether on a fixed price deal or a Standard Variable Tariff, is not a one-off transaction akin to buying a tank of petrol. It is the start of a contractual ongoing relationship between the customer and the supplier, where the prices charged will vary over time, and the customer is likely to require significant service and support; how a supplier provides that service can have a material impact on their cost-base, their prices and the quality of service delivered. We believe that CPW's should be required to publish prominently alongside the cost of the energy being offered information on the quality of service provided by the supplier (ombudsman complaint statistics, average call waiting times, NPS/churn), the default tariff (and any increase or reduction it would deliver), and a 5/10 year APR equivalent.

Emergence of the Fixed Price Market

We are surprised that the CMA is not more concerned about the increasing penetration of short term fixed price tariffs in the market.

The CMA has received consistent feedback from all energy suppliers who have operated beyond the scope of the 2009-2014 window of investigation that the emergence of a market dominated by fixed term contracts represents a fundamental shift in pricing risk from suppliers to consumers in the event of a materially inflationary environment.

We see no evidence in the proposed remedies that the CMA views this as potentially detrimental to consumer interests, and indeed are alarmed by the wording within Remedy 11 that 'no other evergreen tariffs would be permitted'. This is entirely inconsistent with Remedy 3 which seeks to remove barriers to entry for Non-Traditional Business Models. We also do not understand why it might logically be necessary to prevent a supplier from having alternative evergreen tariffs (possibly as part of a bundle) which are cheaper than the Safeguard Regulated Tariff.

The CMAs implicit conclusion that competition is now only able to occur within the fixed price market is fundamentally wrong - as we have manifestly demonstrated through our ongoing and consistent success in growing our customer base via a variable pricing strategy, where the larger the bundle of services being taken by a customer the cheaper their energy tariff becomes. Furthermore it represents an endorsement of a marketplace that is increasingly becoming dominated by fixed price tariffs (with the inherent consumer risks associated with this), where the value each consumer receives becomes a lottery based on where the wholesale commodity price curve happens to be at the point each fixed contract is entered into and/or renewed.

As the only supplier in the UK operating more than one evergreen tariff, and the only supplier to acquire customers primarily via an evergreen pricing strategy, we fundamentally disagree with this direction of travel which in our opinion will have an adverse impact on both competition and choice. We therefore ask the CMA to reconsider its conclusion that the emergence of a marketplace dominated by fixed price tariffs is consistent with its duty of care to protect the interests of consumers.

We also seek formal confirmation from the CMA that it is not their intention to unintentionally outlaw evergreen pricing strategies through the current wording in proposed Remedy 11 that 'no other evergreen tariffs would be permitted'.

We welcome the opportunity to reiterate our views in more detail on the domestic retail energy market and offer our opinions on the package of proposed remedies that the CMA published on 7 July 2015.

Remedy 3 - Removal from domestic retail suppliers licences of the "simpler choices" component of the RMR rules.

a) We strongly endorse this proposed remedy, which we believe will be effective in increasing competition between energy suppliers by enabling market forces to work in an unrestricted manner to the benefit of consumers.

The removal of the 'simpler choices' component of the RMR rules also needs to include the removal of <u>all</u> the prescriptive aspects of the bundling and discount rules, rather than just the four tariff restriction. These broader prescriptive aspects of the RMR rules are fundamentally stifling innovation, and are a major barrier to the emergence of Non-Traditional Business Models that have the potential to play an important part in the development of a sustainable and competitive energy market.

Lack of consumer engagement has been identified by both Ofgem in the Retail Market Review and the CMA in their energy market investigation as the single largest challenge facing the emergence of genuine competition in domestic energy market, and these restrictions in the RMR rules are a major barrier towards widening consumer engagement in future as explained in more detail below.

Whilst the continuing high switching levels seen by the industry in recent months are seemingly indicative of greater consumer engagement, these have been primarily driven by the significant fall in wholesale commodity prices over the last 18 months which has enabled new entrants to advertise anomalously high savings.

These cheap introductory fixed price tariffs do not reflect a new paradigm in the energy markets, and the new entrants offering them do not enjoy a significant or sustainable cost advantage. So as wholesale prices start to rise again (which they inevitably will at some stage), or SVT's continue to fall (reflecting a lower weighted hedge book cost within the Big 6 – **but provided these lower costs are actually passed through to consumers rather than being used to cross subside introductory deals**), then the gap will progressively diminish and consumer engagement (as evidenced by switching volumes) can be expected to revert to normalised (lower) levels.

One of the major benefits of an open and competitive marketplace is the pressure it puts on all participants to find new ways to deliver their services more efficiently and at lower cost. And while price is clearly a driver of consumer engagement, it is only possible for a supplier to offer lower prices to consumers in a sustainable manner if they are operating more efficiently than their competitors or are prepared to accept a lower level of profitability (although industry wide profits are only in low single digits currently at best).

One important way that a supplier can achieve a genuine and material advantage in their operating costs (as opposed to simply cutting costs by reducing the quality of service they are providing), is by bundling other products together with energy, in the same way as the emergence in the communications sector of 'Triple Play' and 'Quad Play' bundles has enabled suppliers to reduce operating costs and offer better value to their customers. And whilst combining gas and electricity together to create a 'Dual Fuel' bundle has become normal, the development of broader and more innovative bundles (which we believe is vital to the emergence of sustainable competition in the domestic energy markets) has stalled under the new highly prescriptive RMR rules.

Furthermore, bespoke products that are tailored to the specific demands of certain demographic groups also drive consumer engagement, and these frequently involve practices such as bundling or discounting that are impossible under the prescriptive 'simpler choices' RMR rules.

Through the 4-tariff rule and the highly prescriptive rules relating to bundled products, Condition 22B of the Energy Supply Licences effectively prevents practical segmentation of the UK population, and acts as a material barrier to tailoring products to specific consumer demographics and their needs and desires. It therefore fundamentally undermines the ability of domestic retail energy suppliers to offer products that will engage new segments of consumers who have not previously become engaged with the energy market.

Our entire business model as an integrated multi-utility provider is predicated upon enabling our customers to bundle together an increasingly wide choice of essential household services: gas, electricity, landline, broadband, mobile, and (in future) insurance. This enables them to benefit from the simplicity of a single monthly bill (which makes it easier for them to manage their household budget), significant savings compared with their previous suppliers (as we can spread our overheads across multiple revenue streams), and award-winning customer service.

In the context of Clause 22B, (both in terms of a maximum of four tariffs and the highly complex rules around optional and tied bundles) we are now severely restricted in how we are allowed to bundle our services together. This means we are unable to pass through available but 'unallowed' cost savings to the end consumer (which is clearly illogical from a consumer benefit or competition perspective), or to construct innovative new bundles that would encourage even more households to engage with the energy market.

During the RMR process, we were concerned that Ofgem had initially completely overlooked the value of innovation and bundling in driving competition in the energy markets, through a narrow focus on 'energy only' suppliers. However, having steadily built a customer base of almost 600,000 households over the last 17 years, supplying over 2.1 million services, we have clearly demonstrated that the bundled strategy we have developed is one that is (a) meeting real consumer demand, and (b) has a vital role to play in reducing consumer costs, and stimulating sustainable competition in the market place.

We strongly support Ofgem's recent focus on Non-Traditional Business models, and believe that the removal of the entire Condition 22B is an absolute pre-requisite for the successful encouragement of such businesses into the marketplace.

b) & c) We question the CMA's conclusion that it is impractical for PCWs to retain an impartial and comprehensive coverage of the entire market, particularly when one looks (by way of analogy) at how successfully they have established themselves in the highly complex insurance market.

The CMA rightly suggest that there is material risk of PCWs building potentially biased partnerships with individual energy suppliers to the detriment of consumers, and if additional remedies to prevent such 'biased pseudo-independent' PCWs are not implemented, there is further risk of energy suppliers even acquiring PCWs themselves and potentially manipulating the search results. There is precedent for upstream suppliers acquiring PCWs in the insurance industry (Admiral Insurance own Confused.com), although we are unaware of any suggestion that the results are manipulated in Admiral's favour.

We believe the Ofgem Code of Confidence requirement for PCWs to provide coverage of the whole market becomes more important than ever in a world of increased tariff numbers. Indeed, in the context of a marketplace that is failing to engage consumers and earn their trust, and which is increasingly dominated by one year fixed price teaser tariffs, there are clear arguments for strengthening and broadening the current Code requirements.

We highlight the concerns raised by the Citizens Advice Bureau in July 2015 in relation to broadband pricing, and suggest that the CMA give consideration to mirroring their proposed remedies across to energy PCWs. This would involve, in addition to displaying all tariffs in the marketplace, PCW's also being obliged to clearly display the SVT that the consumer will default onto at the end of their fixed term period (as is prevalent in PCW tables for mortgages), and the % uplift that this represents.

We suggest consideration should also be given to making the energy industry follow the APR model that has been adopted within the financial services industry for comparing loans from different suppliers, which would mean customers being given an indication of the combined cost of the introductory deal and the SVT, blended over an extended period of 5/10 years, reflecting the long periods that most consumers choose to remain with their supplier after switching.

The CMA have clearly identified that consumers who do not engage with their supplier at the end of a fixed term contract are exploited through being rolled over onto an inflated SVT, and we believe that this remedy would drive transparency and trust and protect vulnerable consumers.

d) A key rationale for the introduction of Condition 22B as part of the RMR was to reduce consumer confusion by reducing tariff numbers. In fact the number of current tariffs available in the market has returned to higher numbers as a result of many new suppliers entering the domestic markets, and the watering down of the proposed white label rules.

We do not agree with the conclusion reached by Ofgem that the large number of tariffs previously available caused confusion and led to lower engagement. On the contrary, we believe that the recent restrictions on the number of tariffs post RMR has reduced competition by preventing suppliers from creating innovative tariffs to address specific segments.

If 1,000 or 10,000 tariffs in a market are confusing then so are 50 or 100. Artificial restrictions on the number of tariffs do not exist in any other market, and do not appear to have caused undue customer confusion; to the contrary, they have led to flourishing and highly competitive markets. In the UK mobile phone industry, there are dozens of suppliers and thousands of tariffs; and in the airline market, there can hundreds of different prices for a seat to the same destination on the same day.

In reality, customers do not make their final choice of tariff and supplier from a theoretical universe of thousands of possible tariffs. They apply filters which significantly narrow the range. On a PCW, the primary filter will be price, so the user would in practice look solely at the handful of suppliers at the top of each comparison table; whether there are 50 more expensive tariffs they don't give a second glance to, 500 more expensive tariffs, or 5,000 such tariffs, is simply irrelevant.

So it seems to us important that the Ofgem Code of Confidence should be further extended, to include a requirement that PCW's include a range of additional filters (other than just whether they can process a switch themselves) such as (for example) a threshold for customer service performance.

We are strongly opposed to a 'petrol forecourt' pricing model with a single unit rate for a number of reasons:

i. It discriminates against any household that has a larger than average energy consumption. Importantly, this is not just big houses - in many cases it is poorer households in smaller properties that are are older and therefore less thermally efficient.
ii. It means that during a cold winter, everyone would pay substantially more for their energy than under the current structure, increasing the number of customers who would get into fuel poverty.
iii. By increasing the unit cost, it puts additional pressure on the poorest members of society who have to choose between each additional unit and meeting an alternative basic need - particularly during very cold periods.
iv. From a suppliers perspective, the reality is that we all face significant fixed costs, many of them as a result of regulation. By charging them on a variable basis, suppliers have less certainty of recovering them, and this will be reflected in higher average prices as they seek to offset this risk, particularly affecting those who can least afford to pay.
v. It will increase the volatility of supplier's profits, which would fall sharply during periods of warm weather as their fixed costs would remain unchanged. This could lead to an increase in the cost of capital they face, potentially higher prices for consumers, and even difficulties for smaller suppliers in obtaining the capital they need to enter (or remain in) the market.
vi. There are significant costs associated with switching, that are currently borne directly by the losing and gaining supplier, and indirectly by all customers in higher prices. The more regularly customers switch, the higher these costs (and therefore prices for everyone) become. This is very different to petrol, where overall costs are unaffected by the loyalty (or otherwise) of customers to any particular brand or outlet.
vii. Energy suppliers cannot easily and quickly flex their fixed costs (staff, buildings etc) to react to rapid changes in the size of their customer base – in either direction – if petrol pump pricing were to create a tidal wave of customer switching. Again, this would inflate supplier costs, and be detrimental to customer service standards.
viii. What is important to customers is the total cost of their energy over an extended consumption period - 'petrol pump pricing' takes no account of the impact from suppliers moving their prices at different times. For example, supplier A could be 0.1 ppkwh more expensive than supplier B for 11 months of the year, but if during a period when prices are rising they hold their old price for a month longer than supplier B, then customers of supplier A could be substantially better off financially over the year as a whole.
ix. Price is an important part of choosing an energy supplier - but by no means the only consideration. Good customer service is expensive to provide, and becomes increasingly difficult to justify with an even greater focus in the market on headline prices. The analogy with petrol retailers is again instructive - almost all filling stations are now 'self-service' - and the reality is that in the energy market customers need good service.

Remedy 4 - Possible measures to address barriers to switching by domestic customers.

a) Whilst undoubtedly the quality of data available within the industry to facilitate customer transfers is an issue, individual companies can mitigate this risk through their processes and controls to ensure minimal issues or errors for their customers.

We have always erred on the side of caution when transferring new customers to us. If the address and supply details are flagged by our automated systems as showing a possible problem, we will pause the transfer and investigate the reason. We feel that this gives the best service and outcome for the customer – whilst it may slightly delay the transfer, it will also minimise the chance of errors which only erodes customer trust.

Uncertified meters are clearly a challenge – most of these are linked to new build properties and we would note that many of the installing (some supplier controlled) companies appear to drag their heels in updating the national systems with the correct details – whether this is a deliberate ploy so they can continue supplying them as long as possible, or merely a product of inefficient processes, is open to debate.

We are engaged with the Energy UK led program of looking at quicker switching and are involved within their various working groups to design new industry processes. We would like to comment that whilst this program will bring (albeit small) consumer gains, it will come at material cost to the industry – cost that will ultimately be borne by consumers. We feel there are bigger reasons for mistrust and non-engagement that should be tackled before the move to next day switching.
As an industry, we have already instigated three day switching (after the cooling-off period) and have had limited positive customer response to this. We feel it is important that Government and Regulators understand that major changes come at material cost to the industry, which will ultimately be borne by all consumers (not just those who are benefitting from next day switching). We do not believe the incremental benefit of moving from three day switching to one day switching justifies the significant investment this requires.

Achieving a material improvement in switching times can only be achieved by dispensing with the cooling-off period (which we understand is required under EU Law), or by allowing the Cooling-off period to operate retrospectively after the transfer has taken effect. Whilst theoretically possible, this would lead to even greater industry costs (and thus higher aggregate prices), enormous confusion over billing, and higher bad debts, which will ultimately undermine consumer trust still further. It seems to us fundamentally wrong as an industry to be pursuing a path that will deliver minimal further benefit (typically a few pounds of additional savings) to those who are switching, whilst generating higher industry costs and therefore higher prices for the vast majority who are either not engaged or who switch on a less frequent basis.

We are concerned at the suggestion that ECOES data should be made available to PWC's, given the wide-ranging nature of this data which includes a complete history of previous switches. There is a material risk that this data could be misused by PWC's or those connected with them for marketing purpises, particularly as there are no licensing, regulatory or other restrictions on who can become a PWC. We are also concerned about Data Protection issues arising from widespread distribution of this data.

We urge significant caution is exercised before granting access to this valuable industry data to anyone other than regulated energy suppliers. Strict governance processes and procedures would need to be implemented, and it is clearly appropriate that the costs of these should be borne by the PWC's rather than the industry as a whole; not least because PWCs are commercial organisations that take a significant amount of revenue from energy suppliers but return nothing in the form of support for consumers via social or environmental levies unlike licensed retail energy suppliers. Instead, they have a clear financial incentive to use all available data to target consumers more effectively, in order to further enhance value for their shareholders. Also, PCW's and other similar TPIs work on a numbers game, based on the principal that the more data they process, the closer they will be to a successful generation of revenue. Examples where this has spiralled out of control include 'no win, no fee' sales calls following reported car accidents, PPI miss-selling claims, and in the energy space the way that Royal Mail Home Mover Data is significantly overworked particularly in the SME arena.

We note your provisional findings talk about price being the main driver for change in a homogenised product market. If this was the really the case, one would logically expect virtually all customers switching each month to be moving to the cheapest supplier, rather than the actual figure of c.20% of total switches. It therefore seems clear that not only is the product not fully homogenised in practise, but that price is simply one amongst a number of factors which are important to consumers in deciding whether to switch and who to switch to. These other factors include the level and quality of customer service, the choice of tariffs available, the accuracy of the billing, whether they feel they are being treated fairly, other benefits they are receiving, and the reputation of their supplier.

But more fundamentally, even if price is a main driver, then the price that matters is not the price quoted immediately prior to the switch, but how much the new and old supplier respectively would have charged that customer over an extended period. We re-iterate that this is not an isolated one-off transaction like filling a car with a tank of petrol, but the start of an ongoing relationship more akin to choosing a financial institution for a new mortgage.

4b) We remain deeply concerned that British Gas has retained its derogation from the requirement to inspect meters every two years. This has undoubtedly created significant additional costs for our company directly (and our customers indirectly), as we attract former British Gas customers whose meters immediately need to be rolled into our 'Must Inspect' program to ensure compliance. Given that all suppliers will be commencing the mass roll out of smart meters within the next 18 months, we would encourage as a minimum the extension of this derogation to all suppliers in the market, and ideally permanently amending the licence conditions to reflect this derogation.

We note the consultation published by Ofgem on 23rd July of this year where they are exploring the possibility of reforming suppliers' meter inspection obligations. We believe both options being proposed by Ofgem represent a significant improvement on the current situation, and hope you will take these into account in considering your final recommendations.

Remedy 5 - Requirement that energy firms prioritise the roll-out of smart meters to domestic customers who currently have a prepayment meter.

We see smart meters providing material benefits for customers using the prepayment functionality, and have designed our own foundation stage roll out to prioritise this segment of our existing portfolio of customers.

However, we believe that the industry also needs to take into consideration the material costs of removing existing "dumb" prepayment meters that may have only been installed in the past two or three years. The removal of these assets before the end of their useful life will result in substantial "stranded asset cost" payments being made by the energy suppliers to their Meter Asset Providers ('MAP') from whom they rent the meters, reflecting the curtailment of the MAP's rental income stream before the useful life of the asset has expired.

To carry out this programme effectively, suppliers therefore need to retain a high level of flexibility in determining the most cost effective way to roll out their smart meters, taking into account both the age of their existing meters, their location, and the profile of their customer base. Additional costs created by putting constraints on suppliers will ultimately be borne by all consumers through higher energy prices.

In conclusion, we strongly recommend that option (b) of this remedy is not applied, given the substantial additional costs which the industry would incur if it were.

Remedy 6 - Ofgem to provide an independent price comparison service for domestic (and microbusiness) customers.

It is our belief that a newly centralised price comparison website should only be introduced if it is genuinely going to bring something new, fresh and different to the market that existing (or new) commercial providers are unlikely to deliver. At the present time there are 12 PCW's that are accredited under the Ofgem Confidence Code, and the establishment of a centralised 'me too' PCW therefore risks sending a signal to the market that the Confidence Code wasn't working – otherwise, why would the new centralised PCW have been required? It could also undermine trust and confidence amongst customers who had previous relied upon the Code.

PCWs are commercial organisations and are incentivised to repeatedly encourage consumers to switch suppliers in order to generate commission. It is therefore not in the interests of PCWs to show consumers the long term perspective (as discussed in 3 above), or to direct them to a supplier which will deliver consistent long-term value and where they will be less likely to switch in future.

In the event that the CMA does not strengthen the Code of Confidence as suggested, this would create a possible role for a newly created regulator PCW which would provide additional useful information such as the predicted costs over 5/10 years where consumers either choose not to, or forget to, engage at the end of any fixed term period, and perhaps measures of customer service and complaints for each supplier.

Whilst PCWs have recently become the primary means of consumer engagement in the energy markets, we are concerned that the CMA does not appear to recognise the significant contribution that can be made through other means. That the second largest independent energy supplier has built a near 600,000 strong customer base (almost 1,000,000 supply points) without any reliance on PCW's appears not to be recognised in the CMA conclusions. And the third largest energy supplier (Ovo) is actively seeking alternative routes to market (for example through its community energy projects) and similarly seeking to attract customers from amongst those who have not previously engaged in the market.

We strongly believe the CMA needs to ensure the energy market (including the regulator) does not prevent those seeking to use alternative and/or innovative routes to market in order to target different segments to those who have historically engaged with PCW's.

Remedy 7 - Measures to reduce actual and perceived barriers to accessing and assessing information in the SME retail energy markets.

Whilst we are principally a domestic supplier, we have a small portfolio of micro-business customers to whom we have attempted to bring a level of transparency that has historically been missing in this segment of the market. We have avoided an approach based on offering below-cost, introductory offerings which then default onto much higher rates once the fixed period has finished – unlike other suppliers who rely on subsequent customer inertia to obtain an acceptable lifetime margin. All our micro-business customers are billed on variable tariffs where they are free to leave at any time without penalty, and the price they pay for their energy throughout their relationship with us is entirely cost-reflective. We do not (nor have we ever) adopted a policy of rolling customers automatically onto new fixed contracts without their permission, and we have thus been bringing the same core values of consistent fair pricing and building trust to this market, that we have done in the domestic market for 17 years.

Notwithstanding our open and transparent approach to this market segment, we believe it is impractical to expect suppliers to list all available tariffs on their websites due to the number of different metering arrangements, consumption profiles, length of contracts and start dates within this market, all of which need to be taken into account by a responsible supplier, in addition to the creditworthiness of each customer. In order to take account of these, any general published tariffs would need to include a significant margin of safety, and therefore lead to higher prices for the most attractive customers, with little (if any) benefit for those who are less established; alternatively, there is a risk that some suppliers will simply decide not to compete in this segment at all, thus reducing customer choice.

Remedy 9 - Measures to provide either domestic and/or microbusiness customers with different or additional information to reduce actual or perceived barriers to accessing and assessing information.

As a supplier who already sends virtually all our customers an invoice every month, which includes the provision of cheapest similar and alternative tariff messaging together with projections of annualised costs, we feel we are in a strong position to provide feedback on this remedy.

In order for customers to access and assess information about their energy, make an informed decision and engage with the market, there are two key requirements. Firstly, the information must be provided clearly. And secondly, it must be provided frequently. The problem with RMR is that it has failed to deliver on both counts.

The regulatory requirement for the provision of information on invoice's is wide ranging and confusing for consumers. Under RMR, there is now a huge amount of information that must be included on each invoice, and the way the information is displayed is highly prescriptive. The end result is that when consumers receive their invoice, they are literally unable to see the wood for the trees. It is no wonder that consumers often advise that their energy invoice is the most complicated service invoice they receive.

In relation to frequency, we believe the number of 'touch points' a supplier has with any customer is vitally important. At the present time, we invoice the vast majority of our members monthly and they also receive the obligatory annual statement for energy. That means we have 13 touch-points with our customers each year, where we tell them whether they could be on a cheaper tariff.

However, some other suppliers send only semi-annual summary invoices to their customers in addition to the annual statement, resulting in just 3 touch-points per year.

We believe the current prescriptive regulatory requirements relating to the information that needs to be shown, and on how and where it is displayed, need to be rolled back. They are stifling innovation, and preventing suppliers from using their bills to differentiate themselves from each other, communicate effectively with their customers, and provide useful and relevant information (as opposed to a confusing 'QR' code which few will utilise) in order to make their bills less confusing and easier to understand.

We choose to send a monthly invoice because we believe this is good service, we have nothing to hide, and we want all our customers to benefit from the cheapest tariff they are eligible to receive. This is in stark contrast to our competitors, who in general rely upon the higher prices paid by customers on their SVT's to fund the introductory rates they offer to new customers. It is perhaps not surprising that 35% of UK consumers are entirely disengaged with their energy supplier if they never hear from them!

We believe that the energy industry should follow the recent example set by the FSA, who have recently sought to address the challenge of consumers who had been attracted to an attractive introductory rate for their ISA, only to find themselves stranded on low and uncompetitive rate when the introductory period expires. We therefore suggest that where suppliers are not billing customers on a monthly (or at the very least quarterly) basis, that they should be required to send consumers a dedicated, clear, and unambiguous communication inviting them to switch to the cheapest alternative tariff available at that time, highlighting the additional savings they would make by doing so.

Remedy 10 – Measures to prompt customers on default tariffs to engage in the market

Remedy 10 makes the assumption that everyone who has not switched recently is inactive and therefore not "engaged" with the market – but this is simply not correct. In many cases, they may be making a conscious choice to remain with their current supplier for any of a number of rational reasons, including satisfaction with the way they feel they are being treated, the convenience and simplicity of the bundle of services they are receiving, the financial strength of their supplier, receipt of non-financial benefits such as loyalty points, guarantees about the size and/or timing of future price rises, etc.

The real issue that needs to be tackled behind 'non-engagement' is the all too frequent scenario where such customers are being charged higher Standard Variable prices so that 'engaged' new customers, taking exactly the same services, can receive lower prices on an introductory fixed price deal.

Effective communication, as discussed in our response to Remedy 9, clearly has an important role to play, but can never be more than a partial solution to this problem.

Our executive summary and our comments in Remedy 11 below include our ideas on an alternative effective remedy to stop this – the 'Maximum Price Delta'. This would mean an end to this exploitation, and eliminate the current unfair price discrimination between otherwise similar customers at each supplier.

If the policy goal is to ensure both a competitive market and lower prices, then we would re-iterate our concerns at the encouragement of excessive switching. Switching is a negative sum game – it simply increases costs for the industry (eg: on-boarding and off-boarding administration, bad debts, commissions to PCW's, marketing, advertising) and therefore for all consumers, and the reality is that the benefits go largely to those who switch, and the costs are largely borne by those who don't.

In conclusion, we believe that implementing our Maximum Price Delta suggestion in remedy 11 (which does nothing to prevent attractive tariffs being offered by suppliers who can afford to do so through better purchasing or more efficient operating costs), provides the most effective solution to this issue.

Remedy 11 – A transitional "safeguard regulated tariff" for disengaged domestic and microbusiness customers.

The CMA clearly states that "Gas and Electricity are extreme examples of homogenous products in that the energy that customers consume is entirely unaffected by the choice of retailer". We disagree.

It is akin to saying that it makes no difference which doctor a patient chooses to visit as they each have access to the same drugs, or which garage a driver chooses to service/repair their car.

The reality is an energy supplier does far more than provide the commodity product on demand. They provide advice, they resolve problems, they manage a complicated on-going relationship which can include debt management, and in many cases they may provide additional services (related or otherwise).

As a result, customers may choose not to switch supplier for extended periods whilst still being fully 'engaged' with the market, for a large number of reasons: they are happy with the levels of service they are currently receiving; they feel that they are paying a "fair price" for their energy; they are with a supplier that they feel is ethical and trustworthy and who treats them well; they like the convenience/simplicity of the bundle of services they are receiving, and/or they appreciate the value-added benefits they receive such as loyalty points.

We believe the evidence from the large number of customers who have switched thus far, and who continue to switch each year, suggests that the level of competition in the energy market is extremely healthy, with over 30 suppliers to choose from and millions of consumers deciding to switch suppliers each year.

In no other sector of the economy (eg: personal bank accounts, insurance, credit cards, broadband, mobile) do all consumers change their supplier each year. It is not considered desirable for them to do so, nor does the fact it doesn't happen mean that these markets are not competitive.

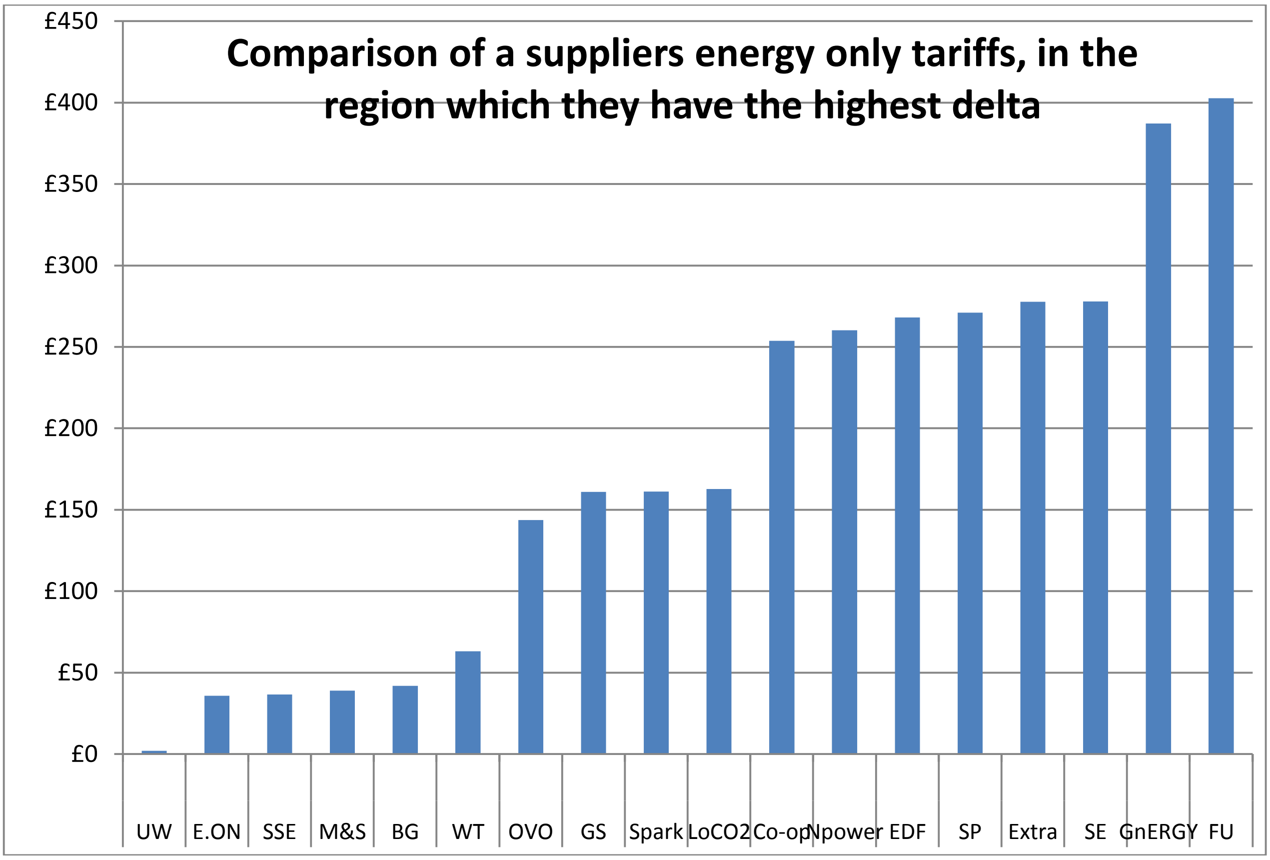
And indeed, excessive switching in fact is highly undesirable due to the additional costs that would be created throughout the industry to the real detriment of all consumers. Also, if everyone were to switch on a regular basis, the reality is that the large headline savings currently available would largely disappear. This must logically be the case, as the maximum level of sustainable savings that can be made by all consumers in aggregate (in the absence of any cost efficiencies that might arise in future), is limited to the current modest aggregate profits being made by the industry – and that maximum level of savings would be on the basis that suppliers were prepared to continue to invest time, resources and capital in these markets for a zero return.

In our view, the best way to lower energy costs for all consumers, is to reduce costs throughout the industry. And perversely, whilst politicians regularly criticise energy suppliers for charging high prices on the one hand, it is their policies (as implemented through DECC and Ofgem license conditions) which are directly responsible for an increasing proportion of each customer's bill. A good example of the way such costs are currently being unnecessarily increased is the smart metering initiative, which could be delivered at substantially lower cost over a longer timeframe compared with the current obligation to replace all meters by 2020.

The CMA are entirely correct in identifying that whilst there is competition, it is not working in the interests of the majority of consumers, particularly the vulnerable and the elderly who are not engaged with PCWs; but this is reality no different to any of the other markets highlighted above where a wide range of prices are available for similar (but not identical) products and services. The two fundamental differences with energy are that gas and electricity are (i) they are essential services that all customers need to buy, and (ii) the significant proportion of the household budget that the cost of these services represents. We believe it is this combination that makes it so important that those consumer segments who are truly not engaged (eg: the elderly) are not exploited by being overcharged for this essential service, in order to provide substantially cheaper deals to a small minority who are prepared to switch on a regular basis in a constant merry-go-round between suppliers to ensure they are always paying the lowest price.

And we re-iterate: each time they switch they create additional costs for the industry as a whole, the vast majority of which will be recovered through the prices charged to customers who have not themselves switched, and thus not received any benefit.

The evidence shows that virtually all energy suppliers (other than ourselves) are taking advantage of the lack of engagement demonstrated by a significant proportion of customers, and use the extra profits they make from such customers to cross-subsidise the introductory fixed-price deals they use to attract new customers. This cross subsidisation of tariffing has been clearly visible amongst the six large energy suppliers for some time, and is now starting to be seen in the pricing strategies of many independent suppliers too as they achieve scale (and the costs associated with it), and seek to balance the need to remain at the top of the PCW tables (in order to continue driving growth) with the need to generate an acceptable level of profitability for their shareholders.



Difference in annual cost (as at 23 July 2015) between the Cheapest Tariff and Standard Variable Tariff for each supplier, available to all direct debit customers, <u>in the GSP where they have the largest variance at average annual spend for a medium household</u>.

It would be entirely unjustifiable to exclude any suppliers – large or small – from any remedy that is implemented to address this issue (as intimated in 95 (i)) as it is the consumer that needs to be protected, NOT the supplier.

The current small supplier exemptions from social and environment levies already distort the markets significantly, because of the pressure they put on larger suppliers to offer cross-subsidised deep-discounted tariffs in order to remain competitive on the PCW's compared with smaller suppliers who do not bear these extra costs. We caution the CMA against adopting any remedies which might further accentuate this situation.

We strongly welcome the proposed transitional Safeguard Regulated Tariff ('SRT') as a practical method of addressing this customer exploitation in the domestic energy supply markets, however we share the concerns on the significant scope for unintended outcomes that the CMA themselves identify, for example relating to the level at which the SRT is set, and the mechanism by which it is maintained.

We expect that virtually every other energy supplier will oppose this proposed remedy as it fundamentally challenges their exploitative business practices. We therefore do not propose to comment on every aspect other than to strongly support the principle behind it, and to suggest a possible mechanism for maintaining the SRT in future of setting it automatically at 5% above the weighted average of the cheapest tariffs available from <u>all</u> licensed suppliers during the previous quarter, with it being re-set on a quarterly basis thereafter.

We are concerned that this protection for consumers is likely to continue to be required for the foreseeable future, and therefore do not agree that it should be introduced solely for a transitional period.

However we recognise the practical challenges in implementing a remedy of this sort, and therefore ask the CMA to reconsider our alternative proposed remedy for dealing with this issue, which you have stated you were not minded to consider further, namely the introduction of price non-discrimination provisions.

As detailed in our executive summary, we believe that the introduction of a maximum differential between the cheapest and most expensive tariff that each individual supplier can offer at any time will achieve the same outcome as Remedy 11, but with considerably less risk of unintended and potentially damaging consequences. It will eliminate the issue of exploitation of any customer by any supplier, it recognises the reality that different suppliers face different cost bases, and it eliminates the need to address the issue that some suppliers only notify existing customers about their cheapest alternative tariff on a very infrequent basis.

Amongst the other advantages of our proposed 'maximum delta' remedy are that, when combined with the other proposed remedies, it promotes the proper functioning of a competitive market, and is entirely self-regulating:

(i) If a supplier wishes to maximise its profits, then it can price at the top of the market and will suffer the consequences as its customers churn away (for example SSE which lost 8% of its customer base in the past 12 months).
(ii) If a supplier wishes to maximise its growth, then it can invest in growth by pricing aggressively and it will attract customers from other suppliers.
(iii) What cannot happen is that an individual supplier can have its cake and eat it, by maximising profits from its SVT base whilst simultaneously acquiring customers by offering cross-subsidised introductory deals.

Remedy 12A – Requirement to implement Project Nexus in a timely manner

As one of the very few suppliers, who has almost completed their internal development work and was on "schedule" to meet the original launch date of 1 October 2015 for the implementation of Project Nexus, we welcome your comment in remedy 12. We are deeply disappointed with both Xoserve and the rest of the supplier community (principally the 'Big 6') for their failure to implement this project in a timely manner when it has been under design for such a long period of time.

The latest modification includes an intended “live” date of 1st October 2016. We think it is important this new live date is not allowed to slip further, and significant financial penalties should be imposed on any industry parties who are not ready in time.

We believe an investigation should be carried out into why some suppliers and the system administrators (Xoserve) have not delivered against the originally agreed timeframes, in what could almost be called a foot dragging exercise, blaming things largely on the slow rate of IT development which has been wholly within their control.

Remedy 14 – Remedy to improve the current regulatory framework for financial reporting

The initial rationale for the introduction of transparency of generators and suppliers revenues, costs and capital employed was to look at the perceived theory that vertical integration was harming the retail market and negatively impacting the price that consumers pay. As the CMA has now concluded that there is no effect on competition by vertical integration, we would argue that most of the reasons for these licence conditions have now disappeared.

As previously highlighted in our submissions to the CMA, as a multi-service utility provider who achieves cost efficiencies by completely integrating many of our business functions, enabling us to spread these costs over all the services we offer, we have real difficulty in allocating these costs accurately between each individual service type. These (and similar) issues will apply increasingly in future as new entrants come into the energy market with innovative and strongly differentiated business models. For these reasons, we believe it is inappropriate, unnecessary, and risks being potentially misleading, for the requirement on financial reporting be extended beyond the current ‘Big 6’ suppliers.

Vertically integrated suppliers already provide Annual Segmental Statements and have done for some years, which provide information around revenue costs and EBITA and the reasons for doing so seem reasonable. However we fail to see what value will be provided as a result of introducing additional reporting requirements on top of the already large reporting overhead faced by all licensed energy suppliers, which are arguably already placing an excessive burden on many independent energy suppliers. And again, the additional costs which will be created by these requirements can only make it more difficult for such suppliers to continue providing better value to their customers.