BGL Group Limited

Energy Market Investigation

Response to the CMA's Second supplemental notice of possible remedies (and addendum to provisional findings)

1 Introduction

1.1 This response sets out the views of BGL Group Limited (**BGL**) on certain remedies proposed by the CMA to address an additional adverse effect on competition (**AEC**) identified by the CMA in respect of the domestic retail supply of gas and electricity to the prepayment segment (**PPS**) (also referred to as prepayment meter or **PPM** customers) (**the PPS AEC**). For the CMA's reference, BGL owns and operates one of the UK's most popular price comparison websites (**PCW**s), Comparethemarket.com.

2 Summary

2.1 Competition in the retail energy market is weaker than it should be. This trend is even more pronounced in the PPS. Too many domestic energy customers are inactive, particularly in the PPS, where customers are perhaps less certain of their rights and options. This dampens competitive pressure on suppliers. There are considerable gains to be made by such customers from switching tariff and/or supplier; however, these gains go unexploited too often, not simply because underlying choice is limited, but also because certain features of these markets constrain the ability and appetite of PPM customers to use PCWs to the customers' best advantage.

2.2 In BGL's view, not all PPM customers are financially vulnerable; indeed, some may simply prefer to use a PPM for their own budgeting purposes. That said, according to research conducted by the Department of Energy & Climate Change (**DECC**)[1] the number of PPM customers on low incomes is disproportionately high:

> *Households who pay for their gas by direct debit have the lowest fuel poverty rate (6%). Those paying by standard credit have a higher incidence (16%), whereas those paying by pre-payment have the highest incidence (21%).*[2]

2.3 According to Ofgem, in 2014 approximately 60% of the newly-installed PPMs (around 175,000 electricity PPMs and around 195,000 gas PPMs) were installed to manage debt.[3] That said, while most PPMs are installed due to debt, only 7% of electricity PPM customers and 10% of gas PPM customers are currently in debt to their energy supplier.[4]

2.4 Finally, research published by Citizens Advice in 2014, which focused on the experience of self-disconnection among PPM customers, also highlighted that:

2.4.1 PPM customers who self-disconnect are in the lowest socio-economic group (**SEG**) and therefore likely to have the lowest incomes.

2.4.2 Three-quarters (74%) of self-disconnecting PPM customers received one or more state benefit(s) as part of the household income.

2.4.3 Over a third of PPM customers were renting their home from a local authority (44%, compared to 18% of the overall population renting social housing).

---

[1] DECC: Annual Fuel Poverty Statistics Report 2015
[2] Ibid, page 46
[3] Ofgem: Domestic Suppliers' Social Obligations, 2014 Annual Report, page 7
[4] Ofgem: Prepayment review: understanding supplier charging practices and barriers to switching (23/06/15), page 5

2.4.4 More than half (54%) of PPM customers who had been temporarily disconnected had responded to the survey that keeping their PPM topped-up and connected was a major concern of their daily lives.

2.4.5 Around half (47%) of PPM customers had children in the household, reinforcing the need for light, warmth and cooking facilities.

2.4.6 Consumers with mental health issues or learning difficulties were often on PPMs (56% either had, or had someone living with them that had, a physical or mental health condition).[5]

2.5 It follows that it is of the utmost importance that PPM customers (at least those who are able to exercise choice[6]), who are often the least able to cope with higher energy costs, are able to access a better range of clear and competitively-priced energy tariffs and are treated fairly.

2.6 When one combines the above factors with the disproportionately higher prices applying to PPM tariffs (see **section 3** below), BGL considers that the PPS AEC merits further investigation.

3 Price differentials

3.1 The CMA is concerned that the domestic retail supply of gas and electricity in Great Britain to PPM customers is not as competitive as it should be. The CMA considers that certain market features, in combination, reduce energy companies' incentives to compete for PPM customers (particularly those customers with outstanding debt or poor credit histories) or to innovate by offering tariffs that meet those customers' demands.

3.2 In BGL's view, the CMA is right to focus part of its attention on the PPS, particularly in view of the fact that the proportion of customers on PPMs has doubled in recent years, from 7% in 1996 to 15% in 2014.[7] Further, in May 2015, the BBC reported that *'half a million pre-payment energy meters have been forcibly installed in people's homes over the last six years'* - prompting an Ofgem investigation.[8]

3.3 According to CMA assumptions (based on research and analysis conducted by Ofgem[9]), PPM customers are (unlikely to be materially higher than) £80 per customer more expensive to serve than those who purchase energy on credit under a direct debit arrangement (**DD customers**). The CMA, quoting Ofgem, attributes these higher costs to renting and maintaining PPMs and their associated infrastructure, although it notes that these costs have already declined from *'about £140'* for dual fuel since 2009 and that:

[5] Citizens Advice: Topping-up or dropping-out: self-disconnection among prepayment meter users, Dhara Vyas, October 2014, pages 13 and 14

[6] For example, although a clause in a tenancy agreement preventing a tenant from switching supplier or payment option is, subject to certain conditions, an unfair term (according OFT/CMA guidance – OFT365), a proportion of PPM customers are still barred from switching by their landlords. In 2013, The Guardian newspaper, quoting Uswitch research, reported that 10% of tenants were illegally prohibited from changing their supplier and, more importantly, that *'fewer than a third of private renters (31%) were aware they could switch energy suppliers, subject to their rental contract'* – The Guardian, 23/08/12 'One in 10 tenants barred from changing energy supplier'. This highlights the need for better and clearer information to be provided to such PPM customers by incumbent and prospective energy suppliers

[7] CMA: Provisional findings report (07/07/15), page 21

[8] BBC: Ofgem to investigate 'forcibly installed' pre-pay meters, 26 May 2015

[9] CMA: Addendum to provisional findings (16/12/15), page 4 footnotes (Ofgem) 6 & 7

…Ofgem expects to see price differences fall [further] with the roll-out of smart meters, for example because the meter can operate in both smart and prepayment mode, removing the need to install and maintain a PPM.

3.4 BGL would be interested in understanding the basis for attributing a higher cost-to-serve to PPM customers. Such customers should, in principle, be lower maintenance (no meter readings required, no quarterly bills, no cash-flow delay, negligible bad debt risk etc). Indeed, the savings associated with PPM customers should, to some extent at least, off-set (unspecified) infrastructure costs attributable to PPMs, which should nevertheless diminish over time.

3.5 In any event, the CMA considers that even allowing for this cost-to-serve differential, tariffs on offer to PPM customers are not priced competitively when compared against those available to DD customers looking to switch. Indeed, the CMA observes that if similarly priced tariffs were offered to PPM customers (based on the most competitively priced tariffs available to DD customers, as adjusted to reflect the higher cost of serving the PPS), such PPM customers would be able to achieve cost savings of between £150 and £250.

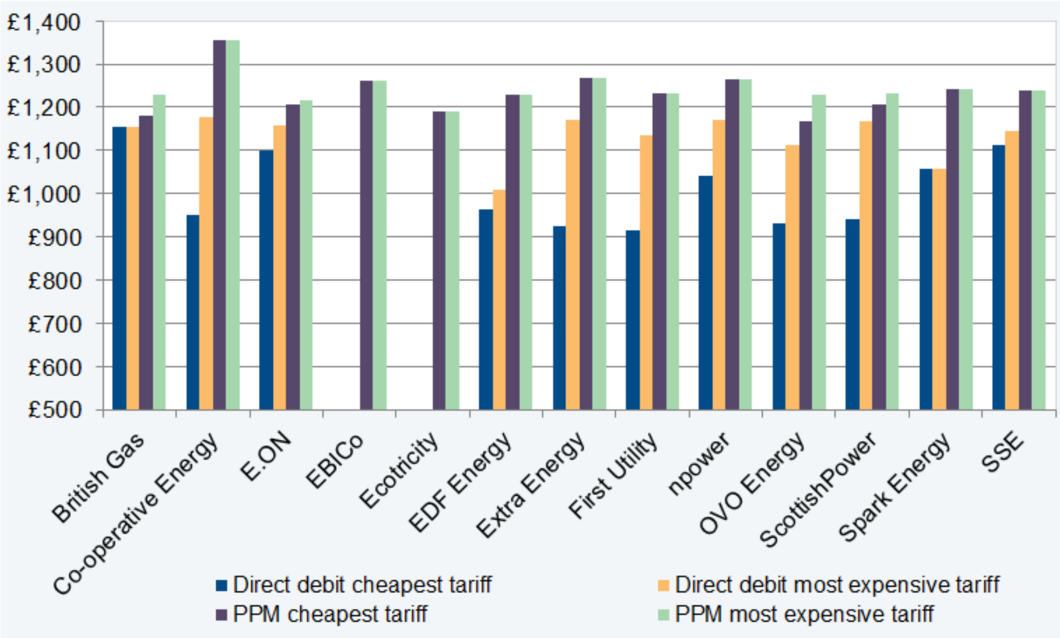
3.6 [*Deleted*]

3.7 Notwithstanding the pronounced difference between the tariffs available to PPM customers and DD customers, according to the CMA only a negligible proportion (3%) of PPM customers switched to credit meters (i.e. became DD customers) in 2014,[10] which is – for the reasons highlighted above - the means by which customers currently using PPMs can theoretically achieve the best savings.

3.8 Indeed, the CMA has not in its 'Addendum to provisional findings' focused in any detail on whether PPM customers could achieve savings by switching to another PPS supplier (possibly because, unlike tariffs for DD customers and as highlighted in the table below, there appears in most instances to be less difference in PPS tariffs based on supplier).

[10] CMA: Addendum to provisional findings (16/12/15), page 7

Citizens Advice: Comparison of the cheapest and most expensive tariffs for online direct debit and prepay (08/07/15)[11]



3.9 In summary, the evidence gathered by the CMA would seem to support a finding that features of the markets for the domestic retail supply of gas and electricity in Great Britain to the PPS give rise to an AEC.

4 Causes

4.1 The CMA contemplates that the above-mentioned AEC is attributable to certain features, namely a combination of:

4.1.1 technical constraints (although this may be resolved as part of the eventual roll-out of smart meters);

4.1.2 actual or perceived higher costs of engagement with PPM customers; and

4.1.3 low prospects of successfully completing the switch of a proportion (15%) of indebted PPM customers.

4.2 According to the CMA, these features work to reduce suppliers' incentives (and possibly their ability) to compete to acquire PPM customers (particularly those with outstanding debt or a poor credit history) and to offer tariffs that meet such customers' demands.

4.3 Indeed, BGL believes that customer rejection rates are, for example, markedly higher in the context of PPM customers seeking to switch. Customer rejection can arise after a switch application has been completed (but before the energy supply has been transferred) as a result of, say, a customer failing a credit check. Based on data from one of BGL's service providers (Energyhelpline) between April 2015 and August 2015 average switch application go-live rates (indicating a successful switch) were only 79% for PPM customers as against an average of 89% for other payment options, suggesting that it is more difficult for PPM customers to address the problem of an already overly expensive tariff.

[11] https://www.citizensadvice.org.uk/about-us/campaigns/current_campaigns/recent-campaigns/fair-play-for-prepay-campaign/price-differences/

4.4 In any event, according to BGL, while each of these features may contribute to reducing competition in respect of the PPS, the focus on supplier disincentives potentially underplays the vulnerability and attendant inertia of customers in that segment.[12]

4.5 In other words, BGL agrees that more should be done to encourage suppliers to offer more choice to PPM customers, so such customers have meaningful alternatives. At the same time, the CMA should also look at ways to encourage PPM customers, many of which are vulnerable, to consider their options and engage with suppliers and third party service providers, such as PCWs, rather than being resigned to a single PPM option offered or indeed imposed by their incumbent supplier. In some instances, a more concerted effort may be required – beyond that which the CMA contemplates it would need to introduce to address the weak customer response associated with non-PPM customers (referred to as the Domestic AEC).[13]

4.6 In BGL's view and as indicated above, competition in the retail energy market is too weak. This trend is even more pronounced in the PPS. Too many domestic energy customers are inactive, particularly in the PPS. Large incumbents appear reluctant to innovate and compete for PPM customers, and PPM customers themselves are less able (perhaps because they are less certain of their rights and options) to apply competitive pressure to suppliers. PPM customers should, in principle, be able to achieve considerable gains from switching tariff and/or supplier; however, these gains go unexploited too often. While the eventual roll-out of smart meters may offer better quality information to PPM customers (and others), their effectiveness in enhancing competition is neither assured not does it represent a timely option. Smart metering, although critical to the positive development of tailored customer services, is not a panacea. Other measures as explored by the CMA and amplified in this response are required to empower more customers, particularly vulnerable customers, to secure a better deal.

5 Comments on remedies

5.1 Taking the need to empower PPM customers into account, BGL would recommend that the CMA gives further consideration to the following:

Remedy 19 – Facilitating sharing of data relating to prepayment meter customers

5.2 In BGL's view, the potential vulnerability of PPM customers and the possibility that previously (and notwithstanding any subsequent change in circumstances) a PPM may have been imposed on them by their incumbent supplier, such customers may be less aware of their options. Such customers may also be reluctant to pursue savings, which they are uncertain of securing. As highlighted in a 2007 Ofgem customer workshop on PPMs:

> *Some [PPM customers] are mystified at how quickly their credit runs out: evidence that, although superficially confident in their use, there is much customers do not understand about PPMs and their own patterns of energy use. It is possible some of this is a result of recent steep price rises disrupting their "feel" for how much they are using. There is little awareness of relative unit rates for PPMs; the sums that are meaningful to them are the amounts by which they top up each time – this is their yardstick for energy use.*

[12] On a related note, potential harm arising from barriers to switching can even affect customers wishing to apply for a PPM. For example, a credit customer may find it more difficult to get a PPS account set-up when they are in debt to their supplier, thus making it more difficult for them to manage their bills going forward

[13] CMA: Second supplemental notice of possible remedies (16/12/15), paragraph 15, pages 4 & 5

Few have tried to switch supplier. Many see little benefit in doing so. More (and independent) information is needed on the suppliers and their prices.

In general they assume it is difficult to change payment method away from a PPM (no experience of this). Once a home has a PPM it is likely it will always have one. There is a need for more information on changing payment method.[14]

5.3 It follows that a remedy of the type envisaged by the CMA, which would give rival suppliers the wherewithal (at least by letter if not by electronic means) to contact non-opted out PPM customers to provide them with an alternative personalised tariff offer, is a step in the right direction.

5.4 This remedy could potentially be improved further if, as part of this contact, suppliers were specifically required to advise customers of the possibility of securing further savings through PCW comparison services, or even for reputable third parties, such as PCWs, to access such information and initiate contact.

5.5 Incumbent suppliers could also be required (perhaps annually) to invite their existing PPM customers to opt-in to receiving prompts via electronic means (emails, SMS etc), and to maintain (and make available via the suggested Ofgem database) a separate list of customers who had opted-in, thus allowing other suppliers, and reputable PCWs, to advise such customers of their options electronically.

Remedy 20a – Prohibit the charging of a security deposit in circumstances when a customer is not in debt and has not incurred any fines, charges or interest for late payment in the last six months[15]

5.6 BGL agrees with the CMA that PPM customers face unnecessary impediments to switching. However, some of the solutions proposed by the CMA, such as the requirement on customers switching from PPMs to credit meters to pay a security deposit only in circumstances where the customer is in debt or has incurred fines, charges or interest for late payment in the last six months, are still too broad.

5.7 More specifically, what does the CMA mean by its reference to 'charges'? Further, it is quite conceivable that despite a PPM customer operating his/her meter responsibly generally, the nature of the service (where credit may occasionally run-out without warning) will mean that the customer might incur (albeit very briefly) debt, charges or interest etc, thus triggering the deposit requirement, which inhibits switching.

5.8 The CMA will be aware that any security deposit requirement is likely to be unattractive to a customer who is, in many instances, already financially vulnerable. In BGL's view, the circumstances in which a security deposit is permissible should be cast more narrowly, perhaps only in circumstances where fines have been imposed on the PPM customer for persistent abuse or for a limited period (e.g. 12 months) following the forced installation of a PPM.

Remedy 20c – Require suppliers to provide annual notifications to prepayment meter customers setting out their right to switch and highlighting any potential restrictions or charges that may be payable

Remedy 21 – Reform the protocol for assignment of debt on prepayment meters

[14] Ofgem: Ipsos Mori - Prepayment meter customer workshop, February 2007, Final report published 02/04/07, pages 47 & 48

[15] As regards remedy 20b, BGL has not commented on this remedy (prohibiting suppliers from charging PPM customers the cost of the meter when switching away from prepayment) on the basis that such a practice did not seem prevalent currently and, in the longer term, ought to be addressed through the roll-out of smart meters (provided such devices can accommodate different payment arrangements)

5.9 BGL considers that both of these remedies are connected, because greater clarity and simplicity on the latter (Remedy 21) ought to help more effective and unambiguous communication on the former (Remedy 20c).

5.10 In order for both remedies to be effective it is essential that a PPM customer's appetite to switch is not dampened as a result of receiving confusing 'objection/appeal letters' (sent by their incumbent supplier). PPM customers should have a clear understanding of their rights, based on a straightforward and unambiguous notification from their supplier.

5.11 Moreover, under the Debt Assignment Protocol (**DAP**) the incumbent supplier is currently exposed only to a very limited degree of risk. This is because in the event of a switch where the customer owes up to £500, the incumbent receives 90% of the sum owing from the new provider in full and final settlement of the customer's debt, albeit the customer remains responsible for the entire debt.

5.12 Given the nature of PPM supply (i.e. advance payment), although BGL acknowledges the possibility that small debts (e.g. for emergency supplies) may be incurred periodically, the risk that a PPM customer would incur a level of debt that approximates to several hundred pounds or more seems remote. It follows that any 10% write-off arising from a switch is likely to be negligible.

5.13 Further, provided an incoming supplier is willing to take on the relevant debt – and remembering that there is no advantage to the PPM customer in trying to play one supplier off against another, as the customer's debt remains the same – the presumption should always be that the customer is entitled to switch without any need:

5.13.1 for the complex and arguably redundant 'objection/appeals' process outlined in the CMA's 'Addendum to provisional findings'[16], or

5.13.2 the £500 debt limit, which is likely to be illusory, and potentially adds unnecessary confusion to customer notifications.

5.14 These mechanisms simply serve to slow down what should be a straightforward comparison process, where the PPM customer has a meaningful opportunity to seek and secure more competitive supply from a willing new supplier, in circumstances which do not unduly prejudice the incumbent supplier who, for whatever reason is unwilling to make better tariffs or services available to that customer. If, however, the process is unduly complicated or onerous from a customer's perspective, then regardless of the incentives that the CMA's remedies are able to create for alternative suppliers, they will not be exploited by the customers they are intended to help.

5.15 As regards the other remedies considered by the CMA, namely the price-cap remedy (Remedy 21), BGL would be concerned that:

5.15.1 It might be difficult for such a remedy to distinguish between different categories of PPM customer, such as those who specifically opt for PPMs as against those who are forced to adopt them.

5.15.2 The remedy might operate as a focal point for all pricing to PPM customers, diminishing the already limited incentives to switch between alternative PPM supplies. Indeed, if set too high, any protection conferred on customers would be ineffective.

5.15.3 The remedy would, in any event and as acknowledged by the CMA, probably only be relevant in the shorter term. Indeed, once smart meters were fully rolled-out, any assumption that a price cap should be set at a level somewhere in excess of the prices of competitively priced credit tariffs is unlikely to be sustainable.

[16] CMA: Addendum to provisional findings (16/12/15), paragraph 51(c), page 15

5.16 By way of a final observation, BGL notes that the CMA has indicated that it is minded not to pursue 'Remedy g' which would oblige suppliers to install a smart meter if so requested by a PPM customer with a non-smart meter. This is because the CMA considers that PPM customer take-up would be inadequate to generate a tangible improvement. Nevertheless, BGL would encourage the CMA to reflect on this remedy alongside the others that it has proposed (as and potentially enhanced) in terms of their combined ability to engage PPM customers whose current understanding of their energy consumption and costs may be inaccurate (see **section 5.2** above).

6 Conclusions

6.1 PCWs represent the single most effective means of facilitating customer switching and driving greater competition at the retail level. The fact remains however that they are still significantly underused by energy customers. The CMA has previously noted that this inertia is more pronounced among more vulnerable customer groups (where the use of PPMs may be more prevalent):

> *"About half of survey respondents said that they had never switched and around a third said they either had never considered switching or thought it was impossible. In relation to demographic characteristics, people who were more likely to be in the latter category included: those aged 65 and over; those in social accommodation; those with no qualifications; and those on lower incomes."*[17]

6.2 It follows that if the model for competition in the UK retail energy market is predicated on the idea of consumer pressure through switching (as opposed to regulation), far too many customers, particularly those in the PPS, are disengaged from the process altogether.

6.3 PCWs cannot, in isolation, address challenging market features (whether the practices of suppliers resulting in barriers to switching or lack of transparency etc) which serve to reinforce less competitive retail pricing, render comparison difficult and disenfranchise customers, resulting in high levels of inertia. Data obtained through smart metering, particularly if directly accessible by PCWs, will help drive better deals for customers (including vulnerable customers) in due course; however, much needs to be done in the shorter term to deliver more choice and, importantly, engage those who are ill-informed or disillusioned in terms of the options open to them.

6.4 BGL supports the CMA's findings in principle, but has also outlined in this submission (and previously) some additional measures which ought to help PCWs support customers in switching and, more importantly, getting a better deal as a result.

ENDS

[17] CMA: Updated Issues Statement, page 25, para. 136