

Thursday, 07 April 2016

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By email only

Dear Sir,

**Re: Energy Market Investigation: Provisional Decision on Remedies**

We are incredibly disappointed with the Provisional Decision on Remedies published on 17<sup>th</sup> March 2016. We are not only concerned that the CMA has wasted this opportunity to rectify the many issues that remain in the energy market, but worse that the proposed price cap on the pre-pay market will cause irreparable damage in a sector of the market that is most in need of the benefits from innovation and cost cutting that competition is bringing.

First and foremost the report says nothing about the meddling by government that is forcing ever-increasing costs on the industry. How on earth can we expect a competitive market to evolve when it is constantly subjected to such significant actual and threatened intervention by government? In particular we would draw attention to the proposed £18bn investment in the 3 GW nuclear plant at Hinckley Point C. At £6,000/kW this is neither a cost effective way to produce electricity or to reduce CO<sub>2</sub> emissions. At current prices it will result in detriment of roughly £1.5bn per year – equivalent to the entire sum the CMA has estimated in this report. This comes on top of: (i) several billion pounds of investment in 5 GW of FIT schemes which are similarly uneconomic ways to produce electricity and reduce emissions; (ii) a reported £11bn commitment to smart metering – at least half of which is unjustified; and (iii) many more billions being pumped into subsidies for much larger scale “renewable” schemes of dubious environmental value and no economic value.

However, even this pales into insignificance when one looks at the cost to consumers of under investment in energy efficiency. All of the analysis I have seen points to the fact that typical residential consumers are using 25% more energy than would be the case if they made cost effective decisions about energy saving measures. This could be causing detriment of the order of £7bn per year, and this report makes no mention of this, whatsoever. Clearly such large reductions in energy consumption would have second order benefits in terms of lower wholesale costs and avoided investment in infrastructure, in addition to wider social benefits resulting from reduced Fuel Poverty.

The report has also failed to make sufficiently specific suggestions regarding the administration of the gas and electricity markets that contain unnecessarily divergent processes and charging structures that cause sub-optimal decision making. Primarily we would draw your attention to: (i) the supply point administration processes; (ii) the barriers to half-hourly settlement in electricity; and (iii) the failure to implement sensible gas settlement arrangements (to which we do not see Nexus as a solution). Each of these failings could be resolved at relatively little expense, and would unblock the delivery of benefits to consumers.

What you have achieved is the destruction of competition in the one sector of the market where Utilita has proven that it can be done on a sustainable basis. The sector most in need of benefiting from the efficiency and innovation that competition can bring – the pre-pay market. As you are well aware the proposed price cap will have a significant detrimental impact on Utilita, and is highly likely to cause us to stop competing in the pre-pay market. The CMA's primary objective is to promote competition and this report fails to achieve that.

The CMA has chosen to do this just as competition in the pre-pay market is starting to pick up. Following the innovation that Utilita brought to the sector with its smart meter based offering, we now have British Gas, Eon, and Ovo all offering a smart pre-pay product. We have also seen the emergence of Economy Energy as another dedicated pre-pay supplier.

The proposed price cap will do nothing to stop the differential pricing by the Big Six that is the root cause of the detriment that you have identified. Indeed if anything it will cement it in for years to come because only those able to cross-subsidise from other sectors of the market will be able to participate in the pre-pay market. In addition, since the cap is not proposed to extend to credit metered customers it will also introduce a perverse incentive on the Big Six to maintain credit meters when it is clear that the consumer would benefit from a pre-pay service. Therefore this PDR has ended up supporting the very companies that the CMA was tasked with investigating.

The data available to the CMA clearly shows that differential pricing is worse in the credit market than in the pre-pay market. It also shows that the level of penetration by new entrants is broadly similar, in both sectors. It is therefore wrong to conclude that a price cap has a greater applicability and validity in the pre-pay market than the credit market.

You have failed to consider other remedies that have been used before by the competition authorities in similar situations. In particular forcing the Big Six to give up market share over a period of time. Such solutions would clearly promote competition and avoid adverse consequences for new entrants.

As it stands the reward that Utilita will be given for introducing such an important innovation, smart pre-pay, and at the same time cutting prices to levels below the Big Six for the last 8 years, is to have its business ruined. At the same time inflicting barely a scratch on the Big Six who have been so instrumental in imposing detriment on this market. That is hardly a message to encourage further innovation and competition.

The CMA has previously concluded that the rollout of smart meters into the pre-pay market will address the detriment that has been identified. We agree with that conclusion and would point out that the market is delivering it based on the evidence of the increase in deployment of smart pre-pay meters over the last 12 months. The CMA should encourage that competition to continue rather than stifle it.

If you are determined to go down this route you should at least: (i) specify an unambiguous end date; (ii) initially set the cap at a level designed to immediately curtail the worst excesses of the Big Six **across the entire market**; and (iii) ratchet down over a period of a few years to give companies the opportunity to either develop their businesses to compete more effectively or to withdraw from the market in an orderly fashion.

It is also absolutely essential that a price cap does not impinge upon new entrants more than those suppliers with a more stable customer base, i.e. that it does not disadvantage suppliers that are actively competing and reducing prices for customers. Indexation must be at least quarterly if not monthly. If this is not the case the indexation will impose a significant additional cost on new entrants further raising barriers to entry.

It is absurd to suggest that dual fuel price caps can be operated when consumers all have a different mix of gas and electricity consumption. Single fuel caps on electricity, E7 electricity and gas can be implemented for the entire market with less administration than you envisaged in the report.

The PPM Price Cap Remedy discriminates against Utilita, and any other new entrants that might be considering a similar model, and runs a significant risk of rendering Utilita incapable of trading successfully. It will also, despite the CMA's unfounded and broad-brush assertions to the contrary, lead to a significant reduction in efficient competition, stifle innovation and lead, potentially, to significant adverse spill-over effects into other segments of the energy market with negative consequences for the fuel poor. Such an outcome is inimical to the CMA's guiding tenets as established by the Enterprise Act, 2002 (as amended) and as set out in its own guidance on the subject.

In short the CMA has wasted this unparalleled opportunity to rectify the many issues that remain in the energy market. Having taken two years to get to this point, a vibrant and disruptive business has been given just two weeks to formulate its response. Nonetheless in the attached report we have shown that your analysis and conclusions are simply wrong and extremely harmful to customers in so many respects.

W Bullen

Utilita, CEO

# CMA Energy Market Investigation

## Utilita Response



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# 1. EXECUTIVE SUMMARY

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- 1.1. The main reason for the CMA inquiry into the energy market, the detriment that you have calculated to be around £1.7bn, is because of the inefficiency and differential pricing by the SLEFs and the slow rate of penetration by new entrants over the first decade of competition.
- 1.2. Differential pricing by the SLEFs has continued despite the Retail Market Review (RMR) because they have been allowed to circumvent the tariff restrictions through collective switching schemes, and is far greater in the credit market than in the pre-pay market. The penetration of new entrant supply business is now around 13% in both the credit and pre-pay markets.
- 1.3. Utilita is a textbook example of a disruptive business. By introducing smart pre-pay into the GB residential market in 2008 we have demonstrated that innovation can bring both price and service benefits to energy consumers. It is now widely recognised that smart meters offer a better way to service the pre-pay market, and in 2014 the government challenged the SLEFs to advance the roll-out of smart meters to this sector.
- 1.4. We have consistently out-performed the SLEFs in terms of price despite their obvious economies of scale and the advantage of an inert customer base. Furthermore this has been achieved in a sector of the market where consumption is relatively low and cost to serve is high, and despite having to deal with the inefficient technology and business processes that surround traditional pre-pay meters.
- 1.5. At the end of March 2016 we had over 320,000 customers (90% dual fuel), of whom around 90% have smart meters installed, and we now have three years of profitable operation. Utilita's unique and innovative business model has not only delivered better value to its customers, but demonstrated that a genuinely efficient and well run supply operation can offer a sustainable competitive threat to the incumbent suppliers.
- 1.6. Whilst we understand there is not a direct correlation, there is no doubt that there is a disproportionate number of consumers in the pre-pay sector that are either vulnerable and/or in Fuel Poverty (however it is defined). We are therefore in no doubt that the innovation of smart pre-pay that we introduced into the market in 2008 is an important development in tackling these problems.
- 1.7. Our main concern with the PDR is therefore the proposed price cap on the pre-pay sector, and in particular the damage that it will do to competition. We believe that in the proposed form the price cap is disproportionate, lacks rigour in its assessment of the cost base, is naïve in its construction, and would be impossible to implement effectively.
- 1.8. We understand that price caps are notoriously difficult to set, and hence they are used as a last resort. As an efficient operator it could be expected that a price cap would be beneficial to Utilita, but at the level indicated in the PDR, Utilita would be severely adversely impacted. If a price cap is set at a level that causes an efficient business to exit the market it will have been set too low.
- 1.9. A price cap should be targeted at curbing differential pricing by dominant players. There is clear evidence that there is good competition in the pre-pay market, British Gas, Ovo, Utilita, and Economy Energy are all actively gaining pre-pay customers at prices significantly below those being maintained by incumbent suppliers.
- 1.10. We can see no reason to propose a price cap in the pre-pay market rather than across the entire market. Differential pricing is higher in the credit market and the level of penetration in both markets is broadly similar. The reasons given by the CMA for not imposing a price cap on the

credit market apply equally to the pre-pay market where competition has increased significantly over the last 12 months. Furthermore having a price cap over part of the market may exacerbate perverse incentives and other unintended consequences.

- 1.11. In respect to the cost base, we doubt the SLEFs monitor costs sufficiently accurately to properly determine the cost to serve of their pre-pay customer base, and in any event we are aware that there are some aspects of the cost to serve differential that have not even been considered by the CMA. In respect of the mid-tier suppliers, none has a sufficiently substantial prepayment portfolio to produce costs robust enough to be used to set a cap for the entire industry. Furthermore, loss making businesses, with most of their customers on unsustainable acquisition products, should not be used to form the basis of a sustainable price cap.
- 1.12. We believe that there are a number of other flaws in the CMA's cap and indexation proposals. The concept of a price cap for dual fuel customers is not workable because real customers do not consume energy in the same proportions, and their consumption of electricity and gas are influenced by different factors. The indexation proposals, in particular an annual change in the cap, would not work for any growing new entrant, and would favour SLEFs. These render the cap as proposed untenable.
- 1.13. We also have concerns regarding the other key remedies proposed by the CMA. With regards to the database remedy we believe the CMA has severely under estimated the difficulty and cost of data management, and in any event typical response rates to mailshots are very low. Whilst we agree with the removal of the RMR constraints, we would urge the CMA not to lose sight of the original rationale for their introduction – differential pricing by the SLEFs. We therefore suggest that they should be subjected to a maximum price differential control.
- 1.14. We would encourage the CMA to pursue remedies that have been used previously, most notably a requirement for dominant players to give up market share. This remedy was successful in opening up the gas supply market during the 1990s.
- 1.15. With regards to the non-customer facing remedies, we agree that further reform is necessary and that this has been blocked by market participants. We would urge the CMA to make more specific directions regarding the electricity and gas settlement arrangements. However we also have concerns regarding increasing the power of Ofgem without a right of appeal.
- 1.16. Finally, we have found engaging with the CMA, and with this document in particular, extremely difficult. As a new entrant supplier with limited resource, responding to such documents in such a short time is extremely challenging. This document (including appendices) contained over 1,500 pages of material. We believe that allowing only 13 working days to respond to proposed remedies that may have such a dramatic impact on our business is regrettable.

## 2. GENERAL APPROACH

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- 2.1. In this report, we start with our own assessment of the current status of the market, this is set out in chapter 3.
- 2.2. Our main concern with the PDR is the proposed price cap on the pre-pay sector which we oppose. Due to the restrictions on information provision to those affected by the proposals, we were unable to access the underlying data. We appointed PwC as our economic advisers and an independent legal adviser ('the advisers') to access the post PDR confidentiality ring and prepare a confidential, blind submission on our behalf.
- 2.3. Conversely, we strongly support other parts of the remedies and believe these should be taken forward.
- 2.4. While the CMA has identified a package of remedies which is intended to be taken as a whole, we disagree that this needs to be the case and consider that most of the remedies can be implemented separately even though they may have complementary effects. On this basis we consider all proposed remedies would be implemented on an individual basis unless we explicitly state a link.
- 2.5. In chapter 4 we set out our detailed commentary on all aspects of the cap, in particular the cost to serve and hedging requirements. We also include a section on a number of possible alternatives on which we believe CMA should have published a full impact assessment prior to proposing a cap.
- 2.6. Chapters 5 and 6 set out our views on the various other remedies proposed by the CMA. For ease of reference, we have generally followed the order of remedies in the document.
- 2.7. The advisers' confidential submission (to which we have not had access), is referenced as "Annex 1 – Advisers' submission on behalf of Utilita Energy Ltd" (the Advisers' Annex). The advisers have assisted in any required cross referencing from this document.
- 2.8. The Advisers' Annex provides confidential analysis to the CMA on the impact of the proposed price cap remedy on Utilita. It does not, in the light of time constraints, relate to any other part of the submission.
- 2.9. We have found responding to this document very difficult. The CMA process has lasted two years and has generated enormous amounts of paper. As a small, new entrant supplier with extremely limited resource, responding to such documents is always challenging.
- 2.10. This document (including appendices) contained over 1500 pages of material. For a small supplier to respond in such a timescale is so difficult it brings into question the quality of consultation on this document. We appreciate that due to earlier slippage in the project, CMA is now time constrained. However, the short response time has adversely impacted both our ability to respond effectively and the quality of our response.
- 2.11. Due to the lack of time we have only been able to use sources available to us, however, we have verified as well as we can under the circumstances.
- 2.12. If you have any questions or would like to follow up any points in more detail, please contact Alison Russell, Head of Regulatory Affairs, at [alisonrussell@utilita.co.uk](mailto:alisonrussell@utilita.co.uk).



### 3. INTRODUCTION AND STATE OF THE MARKET

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#### INTRODUCTION

- 3.1. Utilita is an independent supplier of gas and electricity to the residential market focused on delivering a smart pre-pay service (99% of our customers are pre-pay). Utilita launched its product in 2008 and now has over 300,000 dual fuel customers, of whom around 90% have smart meters installed. Since the outset we have maintained a price point below that of the SLEFs. We have done this using a simple and unambiguous pricing strategy using one main tariff, offering the same rates to all our smart customers – whatever their payment method - while delivering a high quality flexible service for the modern pay as you go customer.
- 3.2. It is now widely recognised that smart meters offer a fundamentally better way to service the pre-pay market than traditional card and key meters. This is both in terms of the cost to serve (and hence price), and the convenience to the customer. Utilita's unique and innovative business model has not only delivered better value to its customers, but demonstrated that a genuinely efficient and well run supply operation can offer a sustainable competitive threat to the incumbent suppliers.
- 3.3. In essence Utilita is a text book example of a disruptive business, that through innovation has brought both price and service benefits to consumers. And in particular has done this in a sector of the market that most suppliers see as undesirable and expensive to service. The pre-pay market is characterised by customers with lower incomes, it is therefore the sector of the market that is most in need of the benefits being offered. Whilst we understand there is not a direct correlation, there is no doubt that there is a disproportionate number of consumers in the pre-pay sector that are either vulnerable and/or in Fuel Poverty (however it is defined). We are therefore in no doubt that the innovation of smart pre-pay that we introduced into the market in 2008 is an important development in tackling these problems.

#### STATE OF THE MARKET

- 3.4. Despite the fact that during the first decade following deregulation in 1998 there was very little competition in the residential market, over the last 5 years competition in the energy market has been increasing dramatically. The table below shows the share of the market now being supplied by new entrant suppliers.

*Table 3.1 – Prepayment and Credit Market Shares – SLEFs vs new entrant suppliers*

	SLEFs '000	New Entrant suppliers '000	Penetration
Credit	19,955	3,060	13%
Pre-pay	4,000	550	12%

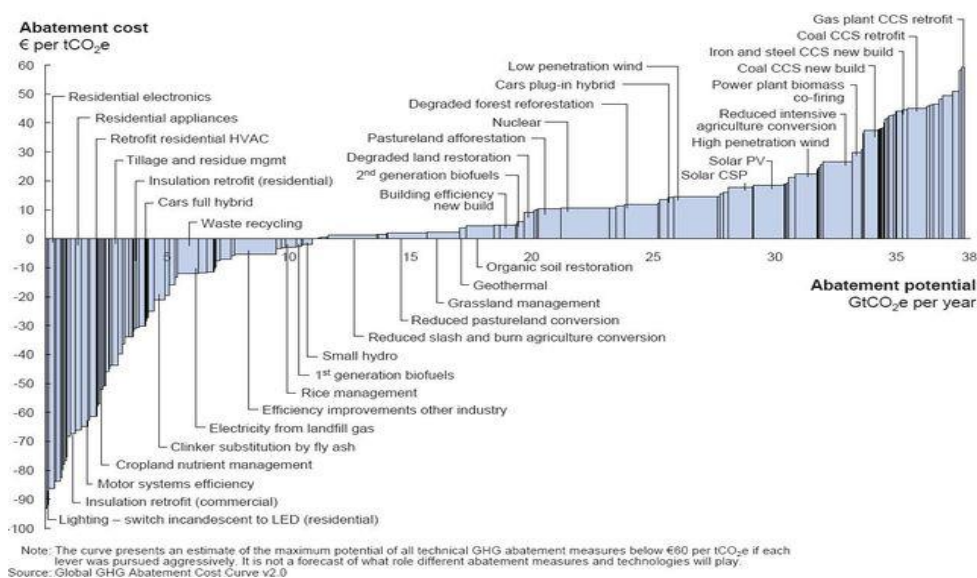
*Source: Utilita estimate*

- 3.5. Nonetheless, as the CMA rightly concludes, there is still evidence of significant detriment to residential customers. This primarily manifests itself in differential pricing by the SLEFs. Customers that have engaged in the market have been able to access significant price reductions,

whilst the inert customers being supplied by the SLEFs are paying much higher rates. The fact that the additional revenue that the SLEFs have generated from this has not shown up in excessive profits indicates that they are inefficient businesses.

- 3.6. With its RMR regulations, Ofgem attempted to address the problem of differential pricing by restricting the number of tariffs suppliers were allowed to offer. Unfortunately they allowed two routes to circumvent these regulations: (i) special tariffs for collective switching projects; and (ii) preserved tariffs for uncommon metering configurations. These have ensured that the SLEFs have been able to restrict the penetration of new entrants whilst at the same time preserve their revenues. We asked our advisers to assess the level of differential pricing by the SLEFs and from CMA data they have calculated that the ratio of the highest and lowest prices for medium consumption are 197% for credit meters and 145% for pre-pay meters.
- 3.7. Competition, and more importantly lower prices for the bulk of customers, has also been restricted by the actions of the government. In particular the government has imposed a growing cost of policy measures to address environmental issues, and to a far lesser extent fuel poverty. They have clearly indicated their intent to continue these policies despite the fact that supply side options are not the most cost effective way to address environmental issues.
- 3.8. We estimate that policy costs are currently costing energy consumers in Great Britain over £2bn per year. This is greater than the detriment identified by the CMA. The vast majority of this money is being spent on inefficient supply side options rather than on far more cost effective demand side measures.
- 3.9. The graph (figure 3.1) below shows an assessment of the costs of reducing CO<sub>2</sub> emissions. It is immediately apparent that the government has focused on a number of measures that have positive costs to reduce CO<sub>2</sub> emissions (e.g. nuclear, solar photovoltaics, and carbon capture and storage), rather than on programmes to reduce CO<sub>2</sub> emissions through energy efficiency that tend to have negative costs (i.e. they save money).

Figure 3.1: Illustrative graphic on CO<sub>2</sub> Abatement



- 3.10. We are particularly concerned that the government plans to impose a large nuclear plant on the industry. Hinkley Point C is a 3.2 GW power station and if operational would account for at least 5% of the electricity demand in Great Britain. It is therefore a very significant intervention, and at the estimated cost it would increase energy bills by £1.5bn per year. This is very nearly equivalent to the detriment estimated by the CMA and is in addition to the estimate of detriment given above (paragraph 3.9).
- 3.11. We are also concerned about the government's smart meter programme and the adverse impact it is having on pre-pay customers. The programme was first announced in Dec 2009 about 6 months after Utilita installed its first smart pre-pay meters. It has suffered a number of delays, and there remains uncertainty about the go live date of the DCC later this year.
- 3.12. The CMA identifies smart pre-pay as a way to address its concerns about detriment in this sector. The impact that the government programme has and is still having is to delay the roll out of smart meters to the prepay market. It has done this in a number of ways:
- 3.12.1. Delaying the publication of the SMETS1 specification;
  - 3.12.2. Allowing SMETS1 meters to be replaced by dumb pre-pay meters;
  - 3.12.3. Increasing the stranded asset risk of SMETS1 meters post the SMETS1 end date;
  - 3.12.4. Delaying the enrolment and adoption of SMETS1 meters.
- 3.13. By delaying production and then undermining the funding of SMETS1 meters the government has slowed down the adoption of smart pre-pay, and therefore had the effect of maintaining higher prices to the pre-pay market. It has also given a green light to the SLEFs to continue to exploit pre-pay customers with their inefficient dumb technology.
- 3.14. We are further concerned that the specification of SMETS2 meters and the associated communication network (DCC) do not allow for functionality that we believe is critical to the effective and efficient use of smart meters to address the pre-pay market.
- 3.15. We believe the government has over-estimated the interoperability issue regarding SMETS1 meters c/w SMETS2. In practice the SMETS2 technology remains untested, whereas the increasing interoperability of SMETS1 is being proven in the field.
- 3.16. Irrespective of the choice of the technology it is clear the programme to rollout smart meters is running behind schedule and is highly unlikely to be completed by 2020. This is relevant to this report because the CMA has an assumed reliance on the successful roll-out of smart meters in relation to both the proposed cap on pre-pay prices and on faster switching.
- 3.17. In its plan published in 2014 the government assumed that by December 2015 circa 6 million SMETS1 meters would be installed, whereas in fact only 2.3 million have been installed. According to the latest data published by DECC.
- 3.18. Table 3.3 below gives our estimates of the number of households with smart meters split between credit and pre-pay. The table shows that smart pre-pay is being adopted by the market at a faster rate than smart meters for credit customers.

Table 3.2 – Change in Penetration of Smart Meters

Market Sector	2015	2016	Penetration
Credit meters	450k	1,000k	4.3%
Pre-pay meters	100k	300k	6.6%

Source: Utilita estimates

- 3.19. From the government's statistics we estimate the current installation rate for smart meters to be 2,200 households per day. This number needs to rise to 13,000 households per day in order to achieve 100% installation by 2020. This seems unrealistic given that the DCC systems have not yet completed testing, and there are no SMETS2 compliant meters available to suppliers. We believe that even 80% coverage (the agreed EU level) would be a very challenging target for 2020.

#### FASTER SWITCHING PROGRAMME AND PROJECT NEXUS

- 3.20. The government has recently announced a faster switching programme to be implemented by Ofgem by 2018<sup>1</sup>. This appears to be predicated on smart meter roll-out. Since there will not be 100% coverage of smart by 2018, this would require an extension to the DCC specification to cover dumb meters.
- 3.21. The main reason suppliers struggle with switching is that the gas and electricity supply point administration (SPA) processes are completely different. What is required therefore is a relatively simple project to align the two SPA processes and use one data transfer network rather than two. It should also be noted that the electricity SPA process already allows for next day switching. Aligning the two processes would cut costs and allow easier entry to the market.
- 3.22. The gas and electricity energy settlement processes also differ widely. Indeed the gas settlement process still relies on estimates for the residential sector which potentially has adverse impacts for suppliers of pre-pay customers. Rather than adopt the model already developed for electricity, the gas industry has designed a completely new settlement process. Project Nexus has now been running for 8 years, is likely to be delayed again, and has fundamental flaws in its design.

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<sup>1</sup> Current Ofgem is targeting 2019 in the programme

## 4. PREPAYMENT PRICE CAP REMEDY

- 4.1. Utilita does not support a cap. It is a blunt remedy that will not achieve the desired outcome and we believe will fundamentally damage competition. We set out below our views on each section. Our advisers have also separately provided a confidential submission.
- 4.2. If a cap is to be utilised, it must be viable and allow for effective competition, the cap as proposed does neither. We set out in table 3.1 below our six key outcomes that the cap must deliver. The proposed remedy fails on all counts.

*Table 4.1 – Key outcomes from the cap*

Requirement	Explanation	Pass/Fail	Reason for failure
1. Cap to be practical and workable	Needs simplicity and consistent application to all customers	Fail	Dual Fuel cap distorts treatment between customers, cannot define a standard dual fuel customer.  <i>Solution: 3 single fuel caps – gas, electricity and economy 7</i>
2. Treat all customers fairly	More vulnerable and fuel poor on DD and Credit than Prepayment	Fail	Cap only applies to prepayment customers  <i>Solution: Cap to apply to all SVT customers of SLEFs</i>
3. Suppliers able to manage risk	Customers benefit by suppliers' ability to smooth prices and share benefit	Fail	Current cap assumes annual indexation and removes supplier ability to hedge cost effectively.  <i>Solution: Index monthly or allow £20 more headroom per year (above £50)</i>
4. Customers have range of competitive offers and choice of suppliers	Suppliers allowed to recover efficient cost to serve without cross subsidy	Fail	Current cost to serve inadequate and does not reflect genuine costs of serving prepayment customers.  <i>Solution: Cost to serve to be increased by £16 (above £54).</i>
5. Healthy long term competition in all elements of the market	Competitive benchmark selected fairly, comparing like with like	Fail	Current benchmark does not reflect appropriate basket of tariffs.  <i>Solution: Broaden basket of tariffs to include all mid-tier suppliers and exclude fixed term acquisition tariffs</i>
6. Maintain downward pressure on prices	Drive efficiency and competition in the sector	Fail	Approach fails to allow for development of supplier approach over time.  <i>Solution: Apply ratchet approach to cap, reducing over a period of 3 years to proposed level.</i>

## A PRICE CAP WILL BE BAD FOR THE MARKET, BAD FOR CONSUMERS AND CARRIES A HIGH RISK OF UNINTENDED CONSEQUENCES

- 4.3. Utilita does not support the introduction of price caps. Applying a cap to only one segment of the market simply risks rebounding on other sectors of the market which are not protected.
- 4.4. The CMA approach of a highly interventionist action with the potential to inflict long term damage on the market, at the same time as seeking to invigorate and clarify Ofgem's focus on competition is contradictory.
- 4.5. CMA recognises in the PDR (paragraph 7.6) the potential for adverse consequences in implementing a cap, and also considers whether a cap should be implemented more broadly, 'notably all SVT customers'.
- 4.6. Having noted the risks inherent in remedies which seek to control outcomes, CMA concludes that the costs of attempting to address the detriment of all SVT customers through a price cap would likely be disproportionate. In paragraph 7.16, CMA notes in particular the belief "...that attempting to control outcomes for the substantial majority of customers (approximately 72% of electricity customers and 69% of gas customers of the SLEFs were on the SVT as of 30 June 2015) would – even during a transitional period – run excessive risks of undermining the competitive process, potentially resulting in worse outcomes for customers in the long run. This risk might occur through a combination of reducing the incentives of suppliers to compete and reducing the incentives of customers to engage."
- 4.7. We agree with the CMA on these points, however, the option chosen – to implement a cap only for prepayment customers is worse – combining the worst elements of an intervention with protection for only a subset of those exposed.
- 4.8. Credit customers on the SVTs are at least as exposed as prepayment customers. A potential effect of the inappropriate cap would be to leave the credit customers paying higher rates, incentivising the SLEFs to transfer prepayment customers to credit payment methods, rather than using prepayment meters which will help them to budget and manage their costs. It is not clear that there would be anything to prevent the SLEFs cross subsidising between payment types, meaning that in the long run, the SLEFs may be only choice of supplier for prepayment customers.
- 4.9. We expect a cap to adversely impact challenger suppliers more than the SLEFs. Not only do they lack the ability to spread cost over a wider portfolio, but they may well lack resource to address the regulatory consequences of a cap, leading to at best reduced market entry and at worst market exit.
- 4.10. Challenger suppliers also have tighter credit cover and hedging requirements – their portfolios are less diversified and unlike larger players, cannot carry the additional risk associated with infrequent indexing (see below). The outcome is that CMA is applying significant adverse consequences to the very sector of the market it needs to be keen to enter and compete for prepayment customers.
- 4.11. CMA uses as justification that prepayment as a payment method functions as a proxy for vulnerability. This is clearly not the case. Ofgem in its report: Energy: The Debate, Ofgem Roundtable Report – Payment Differentials (March 2015) noted that in fact far more fuel poor customers pay their energy bills by direct debit or standard credit than by prepayment (72.9% of electricity customers and 59.7% of gas customers - a further 18.2% of customers are noted as having no gas).



- 4.12. If an annual cap is to be implemented early next year, it is likely that suppliers, to manage their risk, will adopt an approach of 'wait and see' in terms of changing prices outside of this cycle. This may be expected to lead to annual contracts for most prepayment customers.
- 4.13. It is important to note that given the change of tenancy rate in the prepayment market, which is generally above what would be expected in the general population, this may not suit the customers. Many fixed term contracts carry termination fees for early exit, and hence such customers prefer variable contracts.
- 4.14. The annual indexation risks customers having a reduced range of competitive offers to choose from during the year other than when the latest cap has been announced. This would be expected to be a customer detriment to this population.
- 4.15. While all suppliers with over 50,000 customers will indeed have to offer terms as noted by the CMA, we believe that the majority of these offers may meet only minimum requirements given the disproportionate nature of the cap.
- 4.16. The cap may result in low user prepayment customers paying more for their energy relatively, as given the low consumption and the cap, suppliers would be expected to utilise different charging structures to ensure that their fixed costs are recovered up to the limit of the threshold for that consumption.
- 4.17. Many vulnerable credit customers are exposed to differential pricing by the SLEFs. Differential pricing and its impacts was a primary cause of the EMI, and in failing to address this issue, we consider that the CMA has not addressed a core part of its brief. The proposed cap, far from protecting such customers does nothing to address the issue. This is a fundamental failure given that more fuel poor vulnerable customers are supplied on credit or DD SVTs than prepayment.
- 4.18. There is a risk that the cap, by applying only to prepayment customers will mean that SLEFs have a perverse incentive on payment mode, and may result in customers being moved to credit or direct debit, or not returned to prepayment mode on transfer. In these cases there is a risk that those on credit may end up paying more for their energy, and the financially vulnerable may end up in debt as well, due to inability to budget.
- 4.19. All parties agree that there are additional costs in serving prepayment customers, and while these incremental costs will reduce when the smart rollout is complete, we still expect there will be some additional costs. Prepayment customers generally have a high propensity to contact the supplier call centre rather than self-serve if they have an issue, and still tend to dislike online only tariffs.
- 4.20. Utilita is a prepayment specialist, geared to operate efficiently with smart prepayment meters as our core business. We pride ourselves on our efficient business model and prepayment expertise but we have fundamental concerns on the CMA's approach to the cap which we set out below. The fact that we are right to be concerned is supported by the recognition of the potentially damaging impact on our business by the CMA.
- 4.21. CMA has calculated the differential between direct debit and PPM meter customers primarily using SLEF data. The mid-tier suppliers do not have sufficient prepayment customers for a robust prepayment specific analysis. The fact that the CMA has not sought reference or validation of its cost analysis from an acknowledged prepayment expert such as ourselves is a fundamental flaw in the CMA process.
- 4.22. In the section on "assessment of effectiveness" in the PDR, the CMA states that its remedies, and the PPM Price Cap Remedy in particular, must be "clearly defined, transparent, non-

discriminatory, verifiable, and guarantee equal access” (*emphasis added*) and goes on to say “[i]n this context, we have considered the likely impact of the PPM Price Cap Remedy on suppliers and note, in this regard, that the PPM Price Cap Remedy would treat all suppliers’ prepayment customer bases in the same way, and would not lead to companies with similar customer bases being treated differently”.

- 4.23. What, however, the CMA has not considered, however, is whether its remedy might have a significantly more deleterious effect on an asymmetric supplier, such as Utilita, that has a 99% PPM customer base and which has a smart-meter reliant offering.
- 4.24. Whilst it is true that rules concerning non-discrimination require the CMA to treat “like situations in a like manner” the obverse is also a requirement (i.e. the CMA needs to consider whether it has failed to recognize the need to treat “unlike situations in an unlike manner”). The CMA has effectively just allocated Utilita to the same category as its competitor suppliers in circumstances where it is clearly not like anyone else.
- 4.25. This is a material omission and means that the PPM Price Cap Remedy cannot be described as being non-discriminatory.
- 4.26. We set out below our detailed views on the price cap remedy.

## THE METHODOLOGY IS FLAWED – UTILITA’S CONSIDERATION OF THE SPECIFICS OF THE PROPOSED CAP

### Availability and access to data

- 4.27. There is a lack of data in the public domain on the detailed calculations underpinning CMA’s proposed cap. To assess the impact on our business we have had no alternative but to instruct advisers (at substantial cost) who have been given access to the post PDR confidentiality ring on our behalf. We have supplied detailed information on our own costs to our advisers to enable them to conduct a comparison of the CMA’s proposals.
- 4.28. Our advisers have provided limited information to us for inclusion in this submission (approved for release by the CMA). They have also prepared a full report for the CMA. The report has been provided directly to the CMA and forms Confidential Annex 1 to this submission, not appended. Utilita has not had access to the full data underlying Confidential Annex 1.
- 4.29. We note paragraph 7.143 in the PDR. Which states “...If a party feels that the price cap is inappropriate, either in general or in respect of its application at a particular time, then it is able to challenge the CMA’s final report. We consider that this provides sufficient scope for the PPM Price Cap Remedy to be challenged by interested parties.”
- 4.30. Based on our experience under the PDR, we fundamentally disagree. The CMA’s assumption, it would appear, has taken no account of the type of challenge mechanisms available and whether every size/type of supplier has the same capacity to prosecute.
- 4.31. The Enterprise Act, 2002 (as revised) establishes an onerous “judicial review” type remedy that would need to be commenced before the Competition Appeal Tribunal within two months of the publication of the CMA’s final report or after the time when a party was notified of the disputed decision, whichever is earlier. Judicial review is a notoriously onerous and risky undertaking. This is, of course, magnified for new entrant energy businesses that are resource constrained in every sense of those words.
- 4.32. We have real concerns with the process employed by the CMA. We have had to submit a report, based on data and analysis we have not had access to, in order to make detailed representations

on proposals of paramount importance to our business. The quality of analysis has been further constrained by the timescale applied which included Easter. It is unreasonable to expect suppliers to review and comment on such proposals on these terms.

#### **Methodology of the cap**

- 4.33. The submission sets out the difficulties with caps, and why they are problematic and undesirable. It is notoriously difficult to set them at the right level; caps are either excessively susceptible to changes in the underlying conditions, or if the parameters used in construction are flawed, they may be insufficiently responsive to changes in underlying conditions. This burden should also be seen in the context of the limited ambition that the CMA has attributed to the cap which seems to have been deliberately designed by the CMA to cover a "...relatively restricted proportion of consumers...with milder and more limited...consequences" (i.e. the effort in introducing the cap may well be disproportionate to the positive benefits it is designed to deliver)
- 4.34. Caps are difficult to administer as well as resource intensive and costly to maintain, both for the parties setting the cap and those operating under them. These issues have clearly raised problems for the CMA in proposing the cap and we believe account for the limited information and incomplete view in the document.
- 4.35. Based on the information that is available, we have concluded that the methodology used to set the price cap is flawed on a number of grounds. From these sources, we conclude that the operation of the proposed cap would have a significant detrimental impact on Utilita.
- 4.36. The cap has a high chance of creating its own AEC on competition in the prepayment market in the long term and may actually start both driving competitors out, and discouraging new entry.
- 4.37. If a cap is to be implemented, the hybrid approach allows for a degree of indexing and movement over time. Any cap must be set for the minimum period possible, and have a documented end date which can only be extended by Order rather than being criterion based.
- 4.38. Significantly, the cap is not, as declared by the CMA, "strictly time-limited" which is an essential prerequisite for an intrusive and regressive remedy of this kind. The CMA has suggested that the cap should stay in place until such time as the roll-out of SMETS 2 is complete which is currently scheduled for 31 December 2020. Paradoxically, the CMA concedes that the actual smart meter roll-out end-date is, currently, contingent and unknowable and, according to many experienced commentators, cannot be finished in accordance with the government's current timetable.
- 4.39. To address this the CMA has suggested a focused mid-term review in January 2019 which, of course, will simply add to the regulatory burdens that the cap is going to impose on suppliers and disproportionately on the smaller and newer entrants.
- 4.40. Conducting a review, however, is not the same as having an end-date and cannot be considered to be anything other than aspirational.
- 4.41. The approach selected by the CMA is high risk in several ways:
  - 4.41.1. If the base tariffs and allowances are wrong, the indexation cannot protect the market from fundamental damage.
  - 4.41.2. Indexation will only help suppliers manage their risk if it is frequent enough to be effective or the headroom allows enough leeway to cover cost shocks.

- 4.42. In this case, we believe there are errors in the underlying competitive benchmark; the number of caps to be applied; the cost to serve and the frequency of indexation; which means the headroom is inadequate.
- 4.43. All of these errors in the cap construction are significant and each would have a serious adverse effect. Taken together, without mitigation of any of the impacts and based on a hard cutover, the cumulative impact has the potential to be highly distortionary and detrimental to consumers.

#### **The form of the cap**

- 4.44. The CMA has proposed five variants of cap, each multiplied by the number of regions. We do not support this approach.
- 4.45. Having a dual fuel cap that is different to the sum of the single fuel caps is impractical, unenforceable and encourages gaming by suppliers.
- 4.46. Currently, the sum of the single fuel caps is greater than the dual fuel cap. Suppliers are therefore likely to categorize two supply points at the same property as two single fuel contracts rather than a dual fuel contract to avoid the more stringent dual fuel cap.
- 4.47. The CMA indicates the dual fuel price cap must apply at three prescribed levels of gas and electricity consumption and all levels between these points, and non-compliance will result in sanctions on the supplier. It is not apparent that the CMA has considered the bivariate distribution of dual fuel customer gas and electricity usage, which does not vary linearly between these points.
- 4.48. A customer may have, for example, annual electricity usage of 5,000 kWh and annual gas usage of 8,000 kWh, and consumption pattern which does not fall between the three prescribed levels. The dual fuel cap would therefore have to be calculated at all possible combinations of gas and electricity usage to determine whether a supplier's tariff is compliant. This would be impractical, unclear and difficult to enforce. The only practical and enforceable method of ensuring compliance at multiple levels of energy usage is to treat gas and electricity price caps separately, as consumption does vary in a linear way on a single fuel basis. Consumption for the same customer can vary year on year.
- 4.49. The more robust approach, with less incentive to perverse outcomes, would be to operate three single fuel caps on gas, electricity and Economy 7. This would also have the benefit of being administratively simpler and more transparent.

#### **The competitive benchmark**

- 4.50. The CMA has strictly limited the choice of suppliers for the competitive benchmark tariff. There is no adequate justification for this approach.
- 4.51. The CMA has chosen to use only First Utility and Ovo as the basis, neither of which has a significant prepayment portfolio and both of whom have direct debit acquisition tariffs designed to be of most benefit to larger residential users. The other mid-tier suppliers have been excluded. At a minimum, we would expect the competitive benchmark to consist of a wider range of tariffs. We would also expect that in order for the benchmark to be viable it has to include suppliers who have a reasonable proportion of engaged customers with low consumption in their portfolio and the associated tariffs for them as would give a better proxy for prepayment customers.
- 4.52. We have used the CMA figure of £755 for the two single fuels competitive benchmark as the starting point. Our advisers have considered the impact of using the four mid-tier suppliers that

CMA have data available for and as noted above, single price caps. This results in an increase in the competitive benchmark of £75.

- 4.53. The CMA has also included fixed term tariffs in its analysis. Fixed term tariffs are not appropriate as part of the competitive benchmark because of their wider use for acquisition purposes and the restrictions often contained as to termination fees and notice periods which can be difficult for customers to value. This impact of excluding fixed term tariffs from the analysis while continuing to use all four mid-tier suppliers is a further £8.
- 4.54. As we note above, the tariffs of the mid-tier suppliers, given their portfolio make up are clearly weighted toward acquisition. Tariff design will naturally take into account the attributes of the customers the suppliers would like to attract and tariffs would be optimised accordingly. Prepayment customers differ from this pattern of consumption. For example, our average prepayment customer (based on high quality smart data) consumes 3,800kWh of electricity and 9,500kWh of gas. The Ofgem medium TDCV is 3,100kWh of electricity and 12,500kWh of gas.
- 4.55. As a consequence of the lower consumption per customer in the pre-pay sector we assess the impact on a gross margin compared with higher consuming direct debit customers is a loss of at least £7.

#### **Cost to Serve**

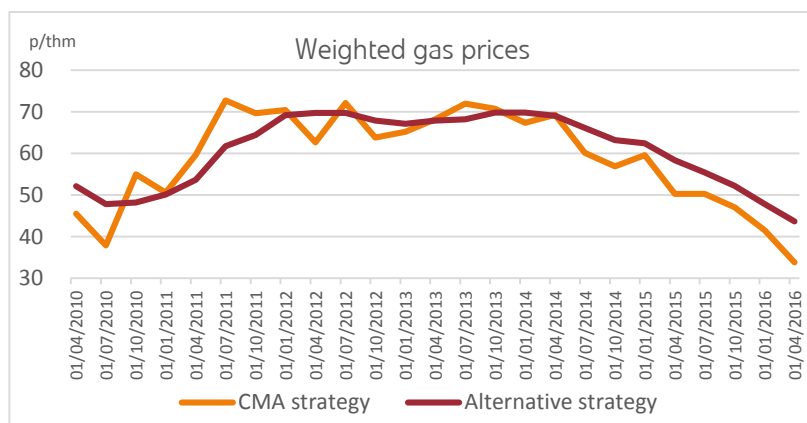
- 4.56. The CMA has assessed the direct debit to prepayment cost to serve differential as £54. Utilita believes that as an efficient prepayment specialist (albeit lacking some economies of scale due to portfolio size), we should be at or near the efficiency frontier for prepayment operation.
- 4.57. We supplied detailed information to our advisers on our cost to serve in the form they requested from us.
- 4.58. We note from the PDR appendices that a number of the SLEFs do not separately cost their call centre provision for prepayment and credit customers. Our portfolio gives an almost pure view of prepayment cost to serve. We assessed our cost to serve based on our view of the additional cost imposed by prepayment customers at different stages of the lifecycle. We also excluded costs of acquisition and meter installation as we treat this as cost of acquisition.
- 4.59. On the basis above, we expect the differential of direct debit and prepayment cost to serve to be approximately £70 per customer. Our advisers have also performed a detailed examination of the CMA's costs in the Advisers' Confidential Annex 1.
- 4.60. Drawing conclusions from the information in the PDR, we believe that the difference between the CMA and our observations is most likely to relate to the CMA's analysis of differential call centre cost. If a prepayment customer has a difficulty of any type (from how to use the emergency credit to inability to top up due to no money) they tend to call the supplier. Change of tenancy is also higher. We therefore consider the cost to serve given by the CMA to be understated by at least £16 per customer.
- 4.61. It is important to note that a disproportionately higher number of prepayment meters are new, and, due to the Smart Meter roll out deadline, are likely to be in situ for a shorter period, which leads to higher meter rentals.

#### **Indexation**

- 4.62. The indexing methodology exposes prepayment suppliers and customers to risk and additional cost that has not been considered by the CMA.

- 4.63. The indexation of the price cap has an implicit forward purchasing and risk hedging strategy, as indexation will be based on forward prices at a specific point in time. Smaller suppliers may struggle to hedge out for a 12 month period, or to fund the associated collateral requirements. In the long run it is unlikely that expected value of returns can be increased by diverging from this implicit forward purchasing strategy, but as retail prices are fixed for an annual period, divergence from this forward purchasing strategy will increase the variability of returns (and therefore costs of capital) without increasing long run expected value. A rational, risk minimizing, approach would therefore be to buy all anticipated volume for prepayment customers for the year ahead at the date used for price cap determination. As a result of the CMA's hedging strategy, energy suppliers attempting to compete for new prepayment customers are exposed to additional risk, as retail prices are fixed on an annual basis. It will also be relevant to consider timing (with an annual indexation), in terms of when in the year people are most inclined to switch. More frequent indexation mitigates this exposure.
- 4.64. An energy supplier competing to gain prepayment customers could buy forward contracts for anticipated customer growth and accept the risk that growth targets may not be met, or not hedge price risk and accept greater variability of gross profit. Using the Black Scholes formula, it is possible to price this risk in the form of an option for a typical customer. Utilita calculates the premium for an Ofgem defined medium user to be £21.73 (assuming a frictionless and perfectly liquid market, and therefore an underestimate of the true cost). The premium under normal circumstances, assuming prices cannot be increased without 30 days' notice, is £1.30. The additional risk premium imposed by the annual price cap is therefore £20.43. This additional risk premium resulting from the price cap has not been considered by the CMA and unless the price cap can reflect this risk premium, competition in the prepayment sector will be inhibited. If the cap could be varied on a quarterly basis the risk premium would reduce to £5.01, which is £3.71 more than the normal premium.
- 4.65. By using forward prices at a point in time, the CMA is exposing prepayment customers to price shocks when revising the price cap. Figure 4.1 below demonstrates the difference in weighted average cost of gas using the CMA's proposed methodology and an alternative methodology using weighted historical forward prices (assuming volume is progressively purchased in 25% increments on a quarterly basis). In order to avoid forcing prepayment customers to be exposed to the risk of volatile changes when revising the price cap, some consideration should be given to historical forward prices.

Figure 4.1 Chart of weighted gas prices





- 4.66. The indexation of the cap is to be weighted using changes in costs as a proportion of a typical bill. The weightings used in the indexation do not consider the constitution of a prepayment customer's bill. As prepayment customers on average use less energy, particularly gas, wholesale costs are a proportionately smaller part of total cost. Conversely, network costs and operating costs are proportionately higher. If the basis of the weightings of the indexation is flawed, suppliers of prepayment customers will be exposed to greater risk as retail prices will not move in the same way as underlying costs. Similarly, for the dual fuel price cap, the weightings of gas and electricity as a proportion of the dual fuel bill must accurately reflect prepayment customers. Currently, it appears that electricity is given an unduly high weighting, which again will expose prepayment suppliers to greater risk as changes to underlying costs may not be accurately reflected in retail prices.

#### Headroom

- 4.67. The CMA has allowed only very limited headroom of £25 per fuel. However, it is clear that this must be linked to indexation and the frequency with which the indexation takes place. If the indexation is completed monthly, it will provide for a reasonably smooth path of prices and allow suppliers to make efficient decisions on price changes, where required, to manage costs to the benefit of both the customer and the supplier.
- 4.68. The less frequent the indexation, the more chance of cost shocks and forcing all changes into one quarter. We believe that this would not be beneficial to customers overall. We consider that customers should have a wide range of competitive offers to choose from, including fixed term of variable contracts, with or without exit fees at all times. By forcing price changes into a short period, this risks frustrating the intention of removing RMR and stifling innovation in a different way. There will also be costs and physical issues with tariff updates, which may well adversely impact challenger companies relative to the SLEFs. This again reduces the level playing field, though the impact is a much lower order of magnitude than the issues set out above.
- 4.69. One approach that may mitigate the worst impacts of the cap would be to implement a Ratchet mechanism to bring the PP cap down gradually. The initial benchmark would be set just below the combined prepayment SVT prices of the SLEFs in the first year. An RPI-X type regulatory approach could then be applied to the benchmark tariff over the next two years – this would allow challenger organisations to update their business plans and models and make controlled choices on how best to respond.
- 4.70. We believe this would improve customer experience - gradual changes without rapid rebounds in price are valued by customers. Such a controlled approach is also less likely to have adverse consequences on investor confidence and hence not have such a damaging impact.
- 4.71. Our advisers indicate that the required headroom, including the fair value option of £20 per customer due to annual rather than monthly hedging, would be £70.

#### Summary of Utilita views on the methodology of the price cap

- 4.72. Table 4.2 below summarises the impact on the initial cap that has been calculated on behalf of Utilita by its advisers. In view of the difficulties we have set out in the ongoing operation of a dual fuel cap, we have assumed that the cap will be based on single fuel caps for gas and electricity, starting from the CMA figure from the document of £755.
- 4.73. In Table 4.2, for both fuels, the customer is supplied under two single caps, assuming a profile class 1 (not economy 7) electricity meter.

Table 4.2 – Summary of impacts on the cap

Issue	Associated Value (£ per annum)
CMA competitive benchmark for two single fuel caps	£755
Use four mid-tier suppliers not two (single fuel caps)	£75
Exclude fixed term acquisition contracts (single fuel caps)	£8
Delta of consumption	£7
Cost to Serve	£15
Additional headroom (assuming annual indexation)	£20
Revised cap	£880

Source: Utilita Advisers' analysis of CMA data, aggregated and approved for inclusion and Utilita's own data.

- 4.74. In this section, and in the Advisers' Annex, we have set out our concerns with the methodology and parameters of the cap, based on the information available to us and within the time constraints.
- 4.75. We accept that creating a robust and viable cap, which allows for healthy competition while constraining the impact of differential pricing is extremely difficult. However we have concluded that there are a number of flaws with the proposals. We have provided data and with the aid of Advisers we have proposed amendments to improve viability, though we consider the fundamental risks remain.

#### THERE ARE BETTER WAYS TO ADDRESS THE ISSUE – WHICH HAVE NOT YET BEEN EXPLORED OR WHICH HAVE BEEN NEGLECTED

- 4.76. As set out above, Utilita is disappointed that CMA has not considered more thoroughly other options to support prepayment customers and address the Prepayment AEC. We believe that CMA has unfortunately decided to recommend the most interventionist of remedies, to be implemented in a way which we do not believe will meet the objective of securing robust competition for prepayment customers.
- 4.77. Utilita believes that there are several options which should be explored fully before applying a cap.

##### Option 1: Prioritise prepayment customers in the smart meter rollout.

- 4.78. While it is not in Utilita's interests to argue for increased competition in the smart prepayment space, we believe that the right answer for prepayment customers – based on fundamentals – is to prioritise the installation of smart meters for these customers.
- 4.79. CMA identified this as an option earlier in the process but has not carried it through to the logical conclusion. Indeed, the CMA has stated, in terms, that smart meters are an appropriate way to "address the specific barriers to engagement experienced by customers on legacy meters" and that "...fully functional smart meters are likely to have substantial, positive impact on both competition and engagement...". Oddly, having reached those conclusions and others, the CMA

has still chosen to promote a sub-optimal, and most probably anti-competitive, option in the form of an open-ended cap.

- 4.80. The press and some other parties have asserted that the installation of SMETS1 meters risks customers losing smart functionality on transfer. While this may be the case, the right solution is not to refuse installation, but to require the DCC, by CMA Order, to adopt and enrol all SMETS1 meters they are asked to by the SMETS1 end date. If necessary, to facilitate this step, CMA should issue a complementary recommendation or Order to DECC to link the SMETS1 end date to the completion of adoption and enrolment by the DCC.
- 4.81. It is also worth noting in this regard that it is by no means certain that SMETS1 meters will present the obstacles to switching suggested by the CMA. This means, therefore, that SMETS1 meters may well provide part of the solution to the CMA's PPM AEC and not the reverse.
- 4.82. The industry has made significant progress on SMETS1 installation, with around 2m meters installed. What has become clear to us as a smart prepayment specialist is that SMETS1 smart meters, with keypads, offer significant advantages to prepayment customers. In particular, additional functionality based on UTRNs in no WAN scenarios, over that offered by SMETS2.
- 4.83. The CMA has the ability to bring real advantage to these customers, bringing them into a more competitive market without resorting to anti-competitive interventions such as price caps. We believe that failure to consider this option fully would be a missed opportunity by the CMA.

#### Option 2: Implement relative pricing for all suppliers

- 4.84. Utilita is fundamentally opposed to the imposition of a price cap on one sector of the market. However, as we have set out above in previous submissions, we are equally concerned by the abuse of customers which results from differential pricing by suppliers.
- 4.85. RMR and now the CMA EMI have both arisen at least in part due to the effects of differential pricing on customers. RMR, for all its highly prescriptive rules failed to address the fundamental issue. Regrettably, it appears the CMA may do likewise.
- 4.86. The CMA has in its power the ability to address the issue of differential pricing and obviate the perceived need for a price cap in one move.
- 4.87. CMA should issue an Order to take immediate effect, that no tariff offered by a supplier can be more than [10%] more in per unit terms (standing charge or unit rate) than the cheapest tariff of any type that supplier offers. For example – the most expensive prepayment standard variable tariff can be no more than [10%] more than the same supplier's cheapest acquisition tariff.

#### Option 3: SLEF SVT > 3 years non-compete/non-winback clause

- 4.88. If customers (of any payment method) have been on the SLEF SVT or its equivalent for 3 years as at 30/06/2016, then CMA should direct that these customers are placed on a database and be subject to an 18 month non-compete clause by the existing supplier.
- 4.89. While this seems at first draconian and would undoubtedly be energetically opposed by the SLEFs, there is a precedent during the initial roll out of competition.
- 4.90. The issue of customers being retained by SLEFs on uncompetitive tariffs is so serious that competition can truly be described as not having begun for these customers. A major remedy is required, and this one has the merit that it utilises competitive forces to generate a solution.

- 4.91. Once the customer has been supplied by a party other than their original supplier for at least 18 months, the original supplier may then try and win them back as a new customer. An interval of this duration is required to ensure the customer is won, taken live, has the opportunity for a smart meter and has the chance to select and renew a 12 month contract if they wish to do so.

Option 4: Customer auction

- 4.92. In this option, the SLEFS would be required to auction customers (of any payment method) who have been on the SLEF SVT or its equivalent for 3 years as at 30/06/2016.
- 4.93. We would propose that monthly tranches of customers should be considered. The aspirant supplier would price according to acquisition costs and factoring in the risk of not retaining the customer.
- 4.94. As above, the original supplier would not be able to seek to winback the customer for at least an 18 month period for the same reasons as above.
- 4.95. Once acquired, the new supplier would be required to offer the new customer their choice of contract – we suggest a minimum of a fixed or variable contract and also their choice of payment terms.
- 4.96. Customers acquired by auction should also be prioritised for smart meter installation if they would like a smart meter, which would perhaps act as an incentive to stay with the new supplier.
- 4.97. We suggest the auction would be a pay as bid auction. The SLEF would receive a sum equal to the efficient costs of the customer loss process plus a modest additional compensation for a lost customer. The balance from the pay as bid auction, less the SLEF payment could be used to reduce any bad debt for vulnerable customers or to contribute to the WHD funding for the broader group.

## 5. NON CUSTOMER FACING REMEDIES

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- 5.1. We have grouped in this chapter the remedies to address the identified AEC's which are not directly retail facing.

### CONTRACTS FOR DIFFERENCE

- 5.2. Utilita supports the remedy that CfDs awarded outside an auction process should have undergone a clear and thorough Impact Assessment. When awarding CfDs outside an auction process, DECC should also make clear whether these are being awarded to reduce the cost of further deployment of this technology.
- 5.3. Utilita would also welcome a thorough review of the CfDs that have been awarded outside a competitive auction process in the past. The CfDs awarded for Hinkley Point C at the proposed strike price would have an immediate detriment of £1.5 billion to all consumers. As the CfD was awarded without any thought to wholesales costs during 2012 and 2013 reducing.
- 5.4. Utilita also agrees that a thorough assessment of the pots to which CfDs are awarded is necessary. This will need to be supported by an audit of the value of money being offered to the consumers.

### LOCATIONAL PRICING

- 5.5. Utilita has mixed views on the remedies associated with this AEC. The CMA notes in the document generally the difficulty associated with implementing this change. We believe that rather than being due to industry intransigence, this reflects the fact that the decision is one that is very finely balanced. The chances of significant increases in costs to consumers which are not compensated by consequential benefits from the locational signals to generation are at least as high as the opposite. We believe that this risk underlay Ofgem's rejection of P229 and that they reached the right decision.
- 5.6. Utilita does not support the introduction of locational transmission losses. We oppose this remedy on that basis that we do not believe that it can be done with sufficient accuracy and granularity to have a locational signal.
- 5.7. Generation, once sited, does not move and commercially is at the mercy of changes to the regime such as this one. The signal to generation can only sensibly be given at the connection offer stage. Once a decision is made and construction commenced, the generator cannot respond to the signal. We therefore believe that the signals to site generation should be accurately targeted as part of the connection process not ex post, following construction.
- 5.8. In the same way, consumers, other than the very largest, are not going to respond to locational transmission losses, once the siting decision has been made.
- 5.9. On this basis, we believe that while locational transmission losses should not be implemented, it does make sense to recover 100% of losses from generators.

## ELECTRICITY SETTLEMENT

- 5.10. Utilita agrees that there is a significant AEC on electricity settlement which should be addressed to improve the quality of settlement. We support the principles underlying the proposed remedies.
- 5.11. The clear statement from CMA that prior to the implementation of mandatory half hourly settlement (HHS), Ofgem should conduct rigorous cost benefit analysis, including mitigating measures, is helpful.
- 5.12. Utilita has argued previously that the main issue preventing greater uptake of elective half hourly settlement is the associated cost. If this issue addressed, we would expect to see an increase in elective half hourly settlement.
- 5.13. The CMA should, in addition to requiring Ofgem to do full impact analysis prior to implementation of mandatory HHS, make an Order to update the Balancing and Settlement Code to alter the charging arrangements to a £/MWh charge. This proposal will facilitate elective HHS.
- 5.14. The main step required on the path to HHS is to institute cost reflective charging. The current approach unfairly favours large supply points, which pay a minimal amount relative to their size for the benefits of half hourly metering. At present, a profile class 1 supply point electing HHS would pay a similar amount to a mandatory half hourly site many times its size. A £/MWh approach would have the merit of being simple and transparent, ensuring that all customers for whom HHS would bring benefits would be able to choose a supplier who could accommodate this for them, once they have had their smart meters installed.
- 5.15. If suppliers are able to elect HHS on an economic basis, the majority of customers for whom HHS would be beneficial will be able to move to tariffs supporting this as their smart meters are installed without mandation.
- 5.16. If a mandatory approach is still required, that first maximising elective HHS would minimise additional cost and may remove or at least delay the requirement for mandation. The industry is managing massive change at present, and implementing further, major change (however thoroughly assessed) without first trialling a much simpler, cheaper approach is disproportionate.
- 5.17. In our previous responses we also stated our firm opposition to the introduction of a monopoly data collector/aggregator. We do not believe that introducing a further body into the industry arrangements which is not subject to competitive pressure will result in long term efficient costs.
- 5.18. We support the recommendation to DECC to address the provisions of the Smart Energy Code which prohibit data collection by suppliers at granularity below daily without a specific opt in.
- 5.19. The supply licence conditions also contain such provisions. In order to achieve the desired outcome, this recommendation will need to also apply to Ofgem to remedy through the licence condition change process.



## GAS SETTLEMENT

- 5.20. Utilita agrees there is a gas settlement AEC. Our concerns relate to the fact that the CMA appears to consider Nexus will resolve the majority of the issues. This is not so, though we believe that Nexus as originally conceived would have delivered significantly more benefit than is now the case.
- 5.21. The time taken to implement Nexus is excessive, in particular given that the system will not deliver a quality product as was specified. The electricity model for settlement is robust and we do not understand why this was not used as an exemplar for gas settlement, with a reduced settlement period of 1 day.
- 5.22. Xoserve has been unable to deliver to the required timescales which has resulted in a reduced version of the system due to repeated descoping. Development continues to be a rocky road with shipper testing time being repeatedly squeezed and functionality (such as retrospective adjustments) being descoped to leave any chance of delivery by October 2016.
- 5.23. Ofgem has now been forced to take control of the project. Ofgem acknowledges that even with the scope reductions and extensive assistance from PwC, delivery remains extremely challenging for October 2016.
- 5.24. Ofgem has committed to the importance of the customer outcome in Nexus delivery. The most important objective in this programme at this stage must be a seamless delivery of consumer benefit, we believe that CMA must make the same commitment. CMA must not insist on delivery of Nexus for 1 October 2016 if in the view of Ofgem and industry this imposes unacceptable risk to consumers or shippers – whether of additional cost or poor service outcomes.
- 5.25. The PDR suggests Nexus is a panacea, which is not the case. The CMA considers that the reforms of project Nexus will remove the risk of inaccurate settlement currently experienced by gas shippers. The project Nexus reforms, however, will continue to expose prepayment customers to inaccurate settlement.
- 5.26. While the new settlement regime will allocate correct volumes to gas shippers based on actual meter readings, the prices used to charge shippers will not be accurate. Initial allocation will still be determined using an annualised quantity and a profile for a domestic customer, which is heavily influenced by credit customers. Shippers are incentivised to purchase volume initially allocated rather than volume used by customers as punitive prices will be charged on imbalance volumes. Once volume is correctly allocated based on meter readings, any volume change from the initial allocation will be charged at a system average price. This means that if a shipper buys the exactly the volume of gas used by its customers, it will still be subject to balancing costs. As a prepayment customer's usage profile differs significantly from a credit customer's, prepayment customers will experience greater reconciliation volumes than credit customers, and because of

### **Illustrative example:**

*A major section (RGMA) of the new system related to crucial functionality on asset updates and other supply point administration fundamentals is not yet available for testing. This functionality also feeds through into and directly impacts invoicing. The testing period allowed for this needs to be at least 3-4 months to ensure that post asset updates, the new invoices correctly reflect the adjustment(s) made and the resulting billing is accurate.*

*At the date of this submission, the industry has not been advised by xoserve when this functionality will be available for testing, or how much of it will be descoped. Ofgem and PwC are also currently unable to provide a firm date for delivery, indeed, they report a large number of outstanding critical defects with the functionality. Xoserve has also failed to provide dates for when the defects will be fixed.*

*While at a detail level, these points illustrate clearly the potential level of risk to the industry associated with Nexus and poor project implementation.*

the prices used in initial allocation and reconciliation, energy suppliers are unable to hedge price risk on this volume difference.

- 5.27. As price risk on reconciliation volume cannot be hedged for prepayment customers, returns for a prepayment customer will be more variable. This will increase the cost of capital associated with supplying a prepayment customer, which will in turn will increase the margin required to generate normal profit. This will be reflected in permanently higher retail prices for prepayment customers. Pricing signals will also incentivize gas shippers to purchase inefficiently i.e. if every gas shipper knows exactly how much volume will be used by all customers on a particular day, the cheapest option for shippers would be to buy the volume initially allocated by the profiling mechanism, even though this volume is inaccurate.
- 5.28. The electricity settlements system does not encourage such inefficiency or affect the cost of capital associated with supplying prepayment customers. Initial imbalance is charged at punitive balancing prices, but reconciled volume is charged using the same prices i.e. buying the correct volume will result in zero balancing cost. The system of cash out pricing for electricity should be closely replicated for gas settlement.
- 5.29. Utilita secured implementation of a modification to introduce a prepayment profile into the UNC to be used for the initial allocation. The profile, while inadequate, did better represent the consumption pattern of a prepayment customer than a standard domestic consumption profile.
- 5.30. Although this modification was approved, the prepayment profile adjustment will be removed on introduction of Nexus. The initial allocations in respect of prepayment customers will be worse than they are now – adding cost into the prepayment space particularly for suppliers such as Utilita. We are working with Ofgem to try and address the issue in time for Nexus go live.
- 5.31. The combined cashout/profile risk is one that we as a shipper can neither predict nor hedge, leaving us and our customers exposed to the potential variation.
- 5.32. This issue has been raised repeatedly with xoserve, but no solution has been proposed hence seeking the support of Ofgem.

## 6. CUSTOMER FACING REMEDIES

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- 6.1. This chapter addresses those remedies identified and directed towards domestic customers. They are considered in the order reflected in the document.

### REMEDIES SPECIFIC TO THE PREPAYMENT AEC

#### *Allocation of gas tariff pages*

- 6.2. The review of the prepayment AEC and consideration of remedies has been useful and we believe several of the proposed remedies will be helpful.
- 6.3. We support the recommendation that improved administration must be put in place in respect of gas tariff pages. If this can be achieved by undertakings from the Six Large Energy Firms (SLEFs) that would clearly be the most efficient and cost effective approach. However, Utilita in common with other smaller players has requested and been refused additional tariff pages. We understand that the SLEFs were approached to request release of unused pages and this was rejected.
- 6.4. Allowing the SLEFs to retain 12 pages each leaves only 27 pages between all other suppliers. We do not understand this approach. All unused pages should be surrendered and managed through the new, Ofgem controlled process. We can see no reason for SLEF suppliers to continue to retain unused or inefficiently used pages. CMA should consider that all suppliers should be permitted to request up to the same number of pages in the first instance to permit all suppliers to offer a range of tariffs if they wish.
- 6.5. In addition to the point above, CMA should require the creation of more tariff pages to address the underlying issue.
- 6.6. We also support the interim approach to enforcement on this element of the licence conditions.

#### *Debt Assignment Protocol*

- 6.7. We support the attention given to the Debt Assignment Protocol (DAP) by CMA and the conclusions set out. We continue to work with the DAP and are pleased to see a gradual increase in numbers.
- 6.8. However, as an almost entirely prepayment supplier, we have repeatedly noted a number of issues. The three main ones are:
- 6.8.1. Lack of automation of the process – it is currently manually intensive and inefficient
  - 6.8.2. Objection reason codes are not used – if a debt reason code was implemented, this would ensure that a DAP is only triggered where debt genuinely exists.
  - 6.8.3. Not all suppliers use the POA model - mandating all prepayment suppliers to engage fully in the POA model on an automated basis would maximise debt assignment for consumers.
- 6.9. In making recommendations on the DAP and omitting to address improvements in these areas is a deficiency in the PDR.
- 6.10. The points noted by CMA are important, but we believe that addressing these additional points will bring significantly greater benefit for prepayment customers and enable more prepayment customers with debt to transfer more smoothly.

- 6.11. Utilita considers CMA has missed an associated opportunity to offer real benefit to prepayment customers.
- 6.12. When prepayment customers change supplier, they are always concerned to ensure that they receive the full value of any credit balance remaining on the meter as promptly as possible. Any refunds of credit balances required should be transferred between suppliers in the same way as debt and we suggest the CMA should make this recommendation in addition to the points above to automate the DAP process and improve the use of reason codes.
- 6.13. We have previously sought to improve the transfer of credit balances to no avail. This is a particular issue to new entrant supplier who are struggling to manage scarce working capital. In our experience, forcing transfer of credit balances away from SLEFs to challenger suppliers via an automated process would require the impetus of an Order from the CMA.

## **REMEDIES CONCERNING THE RMR AEC**

- 6.14. Utilita welcomes the detailed review of the Retail Market Review (RMR). While Ofgem undertook RMR with the best of intentions, and some of the changes it brought were beneficial, it did generate an AEC and a post implementation review is overdue.
- 6.15. While CMA has addressed the simpler choices provisions in the PDR, in our view the proposals with respect to clearer information are not adequate.
- 6.16. Utilita was very disappointed that when implemented, RMR failed to address one of the fundamental reasons for the review – the impact on customers of differential pricing.
- 6.17. CMA has also failed to address this issue, which as we set out above, we believe to be a fundamental failing in the PDR. The proposed remedy of prepayment price cap – while disproportionate as a remedy in itself – still will not address the issue of differential pricing.
- 6.18. As set out below, we believe the proposed approach of removing the restriction on the number of tariffs risks tariff proliferation by the SLEFs. The anti-proliferation measure was a real benefit of RMR. We believe that relaxation rather than removal would be a more proportionate remedy.

### ***Proposals around RMR – Simpler Choices***

- 6.19. This proposed remedy relates to the tariff elements of RMR. We have reviewed the proposed changes and generally support them.
- 6.20. We welcome in particular the removal of the rules relating to complex tariffs. We have long argued that prepayment customers in particular dislike standing charges. With the consumption patterns exhibited by many prepayment customers, a simple two (or even three) rate tariff is better for them financially and much preferred.
- 6.21. The relaxation of rules around discounts and bundling is also a positive remedy. The requirement to remove modest cash based discounts or benefits from customers under RMR was not well understood or received by prepayment customers - the revised approach will be beneficial and better received by customers.
- 6.22. We understand that such proposals must be considered in detail to understand how to present key information such as the TCR for customers under the revised arrangements (including whether the TCR should be removed as well).

- 6.23. As we set out on Chapter 3 and above, Utilita remains concerned that the proposals do not address the issues associated with differential pricing. We believe that robust action such as the implementation of relative pricing for SLEFs to address this point would be of greater benefit to all consumers (especially vulnerable and fuel poor consumers) than the prepayment price cap. It would also have a less damaging effect on the competitive market being applied at a supplier level, in a way which is within suppliers' own control and which uses strong competitive forces to protect consumers.
- 6.24. CMA should also take measures to ensure undue tariff proliferation does not recur. While we support suppliers being able to make a range of innovative offers to suit a range of customers, we would not wish to see a return to the pre RMR tariff numbers.
- 6.25. CMA should make a recommendation to Ofgem to monitor closely and promptly reinstate a restriction if required. This should be through a Special Licence Condition applicable only to those suppliers who are causing the problem rather than penalising all suppliers.
- 6.26. In chapter 4, we set out our thoughts on a relative pricing mechanism. We believe that this would be the simplest way to address the issue of differential pricing to benefit of all consumers. It would also obviate the need for a prepayment price cap, and hence mitigate the potential damage to the competitive market.

#### ***Proposals around RMR – enforcement***

- 6.27. Utilita welcomes the pragmatic approach suggested by the CMA with respect to licence enforcement activity by Ofgem.
- 6.28. Where the CMA has by recommendation or Order set out that licence conditions should be removed or amended, we agree strongly with the proposed approach to deprioritise enforcement. This is a sensible measure which should allow for the time needed to execute detailed licence changes safely and without unintended consequences.
- 6.29. Utilita would suggest further that the CMA should make clear, as part of its recommendations if a cap is introduced, that the restrictions on tariff structure should be removed or explicitly deprioritised by CMA order in advance of the cap taking effect to ensure suppliers are able to offer customers the most efficient tariffs within the cap restriction.

#### ***Proposals around RMR – whole of market requirement***

- 6.30. Utilita does not oppose the removal of the whole of market requirement from the Confidence Code. We agree that it would be crucial, if this is the case, to require all PCWs to be completely transparent on coverage and that this must be easily available to all users.

### **REMEDIES CONCERNING THE PREPAYMENT AEC AND THE DOMESTIC WEAK CUSTOMER RESPONSE AEC**

- 6.31. Utilita supports the proposed recommendation on Ofgem to test thoroughly changes to information provision and measures taken to improve customer engagement.
- 6.32. We agree that the content of bills should be reviewed and tested. However, prepayment customers do not receive bills. They receive Annual Summaries and may receive top up statements.

- 6.33. The current Annual Summaries contain inconsistencies, impose unnecessary restrictions and are often found confusing by customers. We consider these should also be removed and hence that these should be prioritised for review along with bills.
- 6.34. CMA should also ensure that the proposed remedies in this section do not result in ever more prescriptive rules for communications with customers. Suppliers are specialists in communication with customers, and should be allowed to innovate to meet their customers' preferences.
- 6.35. It is sufficient for the main outputs required to be specified and suppliers should then be able to research and innovate in terms of presentation under a principles based approach to regulation. The current provisions round these documents result in micromanagement of the industry to an unproductive degree by Ofgem. This diverts resource from more far more important issues for customers than whether a number is or is not in bold.

#### ***Randomised controlled trials***

- 6.36. Utilita generally supports the proposed recommendation that Ofgem should establish a process of randomised controlled trials (RCTs). The purpose of this would be to ensure that future customer facing remedies should be fully tested in advance of implementation.
- 6.37. While we support this proposal, we do not support the full list of proposed measures. If Ofgem is to update specific messaging on tariff change, we agree this should be tested, as should the naming convention for default tariffs.
- 6.38. In place of market wide tariff messaging, a full review of the licence requirements associated with the bills and annual summaries should be completed. These documents are currently overly complex and confusing for the customer. This should be prioritised.
- 6.39. We agree that if possible suppliers should be asked to co-operate via undertakings. However it is important to remember that RCTs are hugely costly both in time and resource. While challenger suppliers will undoubtedly struggle to fund the activity, the greater burden is likely to be on scarce resources. CMA should require Ofgem to bear this in mind on the demands they make of suppliers under this provision. We set out our views on cheapest tariff messaging below.

#### ***Market-wide cheapest tariff message***

- 6.40. CMA prioritises Ofgem researching changes to the information in domestic bills and how this is presented, including a market-wide cheapest tariff message. Utilita is fundamentally opposed to this concept. We do not believe that it is reasonable to require suppliers to advertise their competitors' products on their bills.
- 6.41. CMA has identified some issues and potential options, for example, that Ofgem might need to play a role in the collation of pricing information and providing suppliers (and customers) with an indication of average levels of savings rather than requiring suppliers to advertise each other's tariffs. We do not believe that this would sufficiently remove the issues.
- 6.42. The objective is to encourage customers to engage effectively in the market. They will not do this if Ofgem or suppliers take over this activity and allow them to abrogate responsibility for their own choices. Providing customers with all relevant information to support a switch and a reminder is a more effective and more competitive option.
- 6.43. Ofgem's resources would be better spent maximizing the value of information to customers rather than taking over the role of a price comparison service. It is also not clear who would bear

responsibility for error and customer loss in the case where the data is provided by Ofgem and customers make financial decisions based on the information, which later turn out to be flawed.

- 6.44. If suppliers were to take on this activity, the sheer difficulty of managing the tariff activity required and keeping it up to date would be prohibitive, and the scale of duplication across the industry would be uneconomic and add costs to customers' bills. This is not a supplier role, and is better undertaken by comparison websites.

### ***Extension to scope of Midata***

- 6.45. Currently, Midata is a voluntary programme. We understand the logic of the proposal but believe that this approach may carry many of the same data issues as the proposed database remedy.
- 6.46. Many customers prefer not to use automated data provision even via QR codes. Amending the annual summary to include the MPAN/MPRN<sup>2</sup> would achieve much of the benefit for these customers.
- 6.47. We therefore do not support mandation of participation of all suppliers in the Midata programme. If CMA continues with this proposal, we consider a number of key protections are required.
- 6.48. For customers, it is essential that PCWs are confined to a one off access to customer data. If PCWs are required to offer at least 2 options, one to be an annual option, it is likely that they will not offer a one off access option.
- 6.49. Once PCWs have gained customer consent to repeated access to their data, there are perverse incentives on such PCWs to prioritise offers which will lead to repeat use by users, whether or not these are best value for consumers. If a customer has signed up once via the PCW, the PCW already can remind a customer of their renewal approaching, and could equally prompt on the basis of prior consumption. There is no need for further access, this remedy as drafted is therefore disproportionate.

### ***Ofgem managed Customer Database***

- 6.50. While Utilita recognises the merit of CMA's concerns around customers on standard variable tariffs, this proposed remedy is too diffuse. This illustrates the point made previously that a remedy should be proportionate and no more onerous than it needs to be.
- 6.51. We believe in this case it may simply be an issue of understanding/wording rather than an intention by the CMA to penalise challenger suppliers unnecessarily.
- 6.52. The customers which need to be protected are those who remain with SLEFs on SVTs. The current drafting risks capturing customers who have moved to a challenger supplier and are happy with them and the tariff they have chosen.
- 6.53. Some challenger suppliers such as ourselves operate only one or two tariffs which are variable with no exit fees or termination charges. Our customers value the simplicity of this approach and lack of obfuscation. It is essential to ensure that this does not result in such tariffs resulting in us having to put any customer how is happy with us and has stayed for 3 years on a database for competitors. We believe that based on the current drafting, our approach means that, however

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<sup>2</sup> The QR code contains the MPAN/MPRN, but the annual summary does not separately allow. Prepayment customers do not receive bills so Utilita prints the MPAN/MPRN on the annual summary to assist prepayment customers who prefer not to use QR codes. Ofgem has asked us to remove the information and we have requested a derogation to permit us to supply this key piece of information to customers on the annual summary.

unintentionally, our best tariff, available to all our smart customers could be deemed to be a standard tariff. CMA must explicitly exclude such competitive tariffs from this remedy.

- 6.54. We believe this proposal is flawed and will cause customers more inconvenience than benefit. If CMA is intent on implementing this remedy, it should apply only to customers on SLEF SVTs, who were on those tariffs and had been so for 3 years at the date of publication of the CMA final report.
- 6.55. CMA has stated that Ofgem could implement a secure cloud database for £50-100,000. All supplier costs are discounted. In the absence of a detailed and robust IA being published by CMA on this matter, we can only assume that one has not been conducted. This approach is untenable and flawed.
- 6.56. CMA states that of the order of 70% of the 'sticky' customers have been on a SLEF SVT for 3 years. It is proposed that based on the French experience and the ICO's advice that suppliers should send special opt out letters to all customers. This information would then need to be managed and optouts recorded. Suppliers would also be required to update status every six months presumably also by letter.
- 6.57. This implies up to 30million additional letters could be sent out per year – at between £0.60 and £1.30 each (depending if required to do freepost replies or electronic communication is permitted). All affected suppliers would have to institute mechanisms to carry out the resulting data collection and data management/maintenance which would also include additional cost as would managing the inevitable calls to the call centre.
- 6.58. CMA should not continue to propose this remedy without publishing a detailed IA. The costs associated would not be associated with the normal supplier costs of doing business and so cannot be discounted in this way.

## **REMEDIES CONCERNING THE MICROBUSINESS WEAK CUSTOMER RESPONSE AEC**

- 6.59. In general, as a domestic supplier, Utilita has no major points to make on this section. However, as under the domestic section, we strongly oppose the implementation of a database remedy.
- 6.60. For the reasons set out earlier in this document, we oppose the proposed database remedy.

## **GOVERNANCE AEC**

- 6.61. Utilita is supportive of the review conducted into Ofgem's role and duties, but has had limited time to devote to this section. We agree that section 1C in the relevant acts leads to competing interpretations. We support the removal of 1C from 4AA and 3A and trust this will be completed in the most expeditious way.
- 6.62. We agree that communications on published government policy proposals by Ofgem should be transparent and published in a proper manner as part of a controlled process. This should require all such communications to be public. However, the process provisions should enable early confidential communication ahead of publication to enable DECC to seek private views to assist proposal development. We believe that where the final proposals do not reflect such early informal consultation with Ofgem, this should be noted in a section of the Opinion.
- 6.63. If Ofgem is to provide formal Opinions, there should be supported by robust criteria, requirement for evidence and clarity on the impact of the Opinion.



- 6.64. We noted with interest the proposal for the creation of a new unit within Ofgem to support a chief economist – understand logic, indeed, as an economic regulator, we had assumed such a role already existed. We would like further clarity on the additional benefits the CMA expects to be afforded by such a role and how to avoid the issues attendant on the creation of such a ‘sub office’.

## **CODES AEC**

- 6.65. Utilita has a number of concerns in this area, but in the time allowed has not been able to consider fully the potential impacts. We therefore briefly record our concerns based on this initial review.
- 6.66. In general, we see the logic in a party such as Ofgem providing strategic direction and cross code/code specific workplans. However, this would only be appropriate so long as Ofgem is required to consult industry meaningfully on proposals and take due account of submissions. In the context of increasing powers for the regulator - such as those mentioned here and in the proposed legislation currently undergoing scrutiny – we remain concerned over due process and access to code modification processes and time for all parties and proposals.
- 6.67. Utilita has concerns over giving Ofgem general powers to intervene and implement code changes directly. Not only does this effectively remove merits based appeals, but the route for checks and balances is unclear. Generally, the regulator performs this ‘oversight’ function, but this is clearly inappropriate where Ofgem is intervening directly. To take this approach with only JR as an option.

## ANNEX 1 – ADVISERS' SUBMISSION ON BEHALF OF UTILITA ENERGY

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Provided directly to the CMA under  
separate cover by the advisers.