Anticipated acquisition by OVO Group Ltd of SSE Energy Services Group Limited

Decision on relevant merger situation and substantial lessening of competition

ME/6854-19

The CMA's decision on reference under section 33(1) of the Enterprise Act 2002 given on 10 December 2019. Full text of the decision published on 23 January 2020.

Please note that [✂] indicates figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

SUMMARY

1. The proposed transaction (the **Merger**) involves the anticipated acquisition by OVO Energy Ltd, part of OVO Group Ltd, (**OVO**) of the domestic retail energy business of SSE plc, SSE Energy Services Group Limited (**SSE Retail**). OVO and SSE Retail are together referred to as the **Parties**.

2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that each of OVO and SSE Retail is an enterprise; that these enterprises will cease to be distinct as a result of the Merger; and that the turnover test is met. Accordingly, arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

3. The Parties' main overlap is in the retail supply of electricity and gas (together, **energy**) to domestic customers in Great Britain (**GB**).

4. The CMA has focused its assessment of the Merger on the retail supply of electricity and gas (each considered separately) to domestic customers using payment methods other than prepayment (**non-prepayment customers**) in GB, and to customers using prepayment (**prepayment customers**) in GB. Within these frames of reference, as part of its competitive assessment, the CMA has also considered whether the Merger gives rise to competition

concerns at a regional level, including regions where SSE has a historically strong presence.

5. The CMA has not found competition concerns in relation to: (i) the supply of gas to domestic non-prepayment customers in GB; (ii) the supply of electricity to domestic non-prepayment customers in GB; (iii) the supply of gas to domestic prepayment customers in GB; or (iv) the supply of electricity to domestic prepayment customers in GB. For each of these frames of reference, the switching data, internal documents and third party evidence showed that the Parties are not particularly close competitors and that there are other suppliers, including large energy firms (British Gas, E.ON/Npower, EDF, Scottish Power) and a number of Small and Medium Suppliers (**SAMS**) (eg, Bulb Energy and Octopus), which will place a sufficiently strong constraint on the merged entity.

6. In addition, while the switching data showed that the Parties were, to some extent, competing more closely in some regions (North of Scotland, Southern, and South Wales), the level of switching between the Parties was relatively low. The analysis showed that remaining competitors in these regions win a substantial number of customers from each of the Parties (with some competitors having a similar or higher level of switching as between the Parties) and will place a sufficiently strong constraint on the merged entity. Therefore, the CMA has found that the Merger does not give rise to competition concerns at a regional level.

7. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in any of the frames of reference set out above.

8. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002 (the **Act**).

ASSESSMENT

Parties

9. OVO is active in the supply of domestic and non-domestic retail gas and electricity and energy-related services and telecoms to customers in GB. It operates through four brands: OVO energy, Spark, Boost, and Lumo. In 2018, OVO generated a turnover of £[✂] million in the UK.

10. SSE Retail is SSE plc's domestic retail energy supply business. SSE Retail is also active in the supply of energy-related services, including domestic boiler

and central heating services, and telecoms services. SSE Retail’s total turnover was £3,584.7 million in the financial year ending 31 March 2019.

11. SSE plc is a FTSE-100 listed vertically integrated energy group parent company, with electricity and gas activities in the UK and Ireland, including: (i) wholesale electricity generation, trading, transmission, distribution and retail supply; (ii) gas production, trading, storage, shipping, distribution and retail supply; and (iii) energy-related and other services. It is active in home phone and broadband telecoms, connection and contracting services.

Transaction

12. The anticipated transaction involves the acquisition by OVO of all the shares in SSE Retail. It is conditional on CMA approval.

13. The Parties confirmed to the CMA that the Merger is not subject to review by any other competition authority.

Jurisdiction

14. As a result of the Merger, the enterprises of OVO and SSE Retail will cease to be distinct.

15. The UK turnover of SSE Retail exceeds £70 million, so the turnover test in section 23(1)(b) of the Act is satisfied.

16. The CMA therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

17. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 24 October 2019 and the statutory 40 working day deadline for a decision is therefore 18 December 2019.

Background

The Energy market

18. The electricity sector consists of generators, grid operators and distribution network operators who transport the electricity to end users, wholesale electricity traders, a system operator (National Grid) and retail supply companies who sell electricity to end users. The value chain for gas operates in much the same way.

19. OVO and SSE Retail are both active in the retail supply of energy in GB.

The CMA's Energy Market Investigation (EMI) and other regulatory measures

20. From 2014 to 2016, the CMA conducted an in-depth investigation into the energy market in the UK, including both the wholesale and retail markets. In the EMI, the CMA found several features of domestic retail energy supply giving rise to adverse effects on competition, including:

    (a) An overarching feature of weak customer response and lack of engagement, giving suppliers the ability to exploit their position through their pricing policies, including through price discrimination by charging their default tariffs[1] (at that time standard variable tariffs (**SVTs**)) materially above a level that could be justified by cost differences;

    (b) Specific features in the prepayment segment, reducing suppliers' ability and/or incentives to compete to acquire prepayment customers and to innovate by offering tariff structures for these customers' demands; and

    (c) Specific aspects of the regulatory regime, including measures introduced under the Retail Market Review (**RMR**) reforms (eg the measure limiting the number of tariffs a supplier is able to offer to four), that reduce suppliers' ability and/or incentives to innovate in designing tariffs to meet customers' demands.[2]

21. Pursuant to the EMI, the CMA implemented or recommended a number of remedies to help address these concerns, including the withdrawal of certain aspects of the RMR reforms,[3] a number of remedies to improve customer engagement, and a price cap on prepayment meter tariffs (**PPM Price Cap**), which is due to expire at the end of 2020.

22. In July 2019, the CMA made a recommendation to the Gas and Electricity Markets Authority (**GEMA**, which is the governing body of the Office of Gas and Electricity Markets (**Ofgem**)) to consider providing protection for prepayment customers after the expiry of the PPM Price Cap.[4]

[1] Default tariffs apply where a customer has not chosen a specific tariff. They are usually SVTs; these continue indefinitely, vary in price over time and do not have 'exit fees.' See also *SSE Retail and Npower – A report on the anticipated merger between the domestic retail energy business of SSE plc and Npower Group Limited* (10 October 2018), (***SSE Retail and Npower* final report**), paragraph 15.
[2] See EMI final report (24 June 2016).
[3] Ofgem also removed the non-price discrimination clause (Standard Licence Condition 25) allowing for regional pricing differences.
[4] See Review of the Energy Market Investigation (Prepayment Charge Restriction) Order 2016, Final Decision, 31 July 2019. The CMA also varied the EMI (Prepayment Charge Restriction) Order 2016 to adopt Ofgem's Default Tariff Cap methodology, adjusted to reflect the specific costs in supplying prepayment customers.

Default Tariff Cap

23. From 1 January 2019, the Government also introduced a price cap for all default tariffs for the supply of energy under domestic supply contracts (**Default Tariff Cap**).[5] This means that suppliers can price to the level or below the cap, but cannot charge more than the cap. The Default Tariff Cap will apply until the end of 2020 and can then be extended annually for a further three years.

24. Ofgem is required to carry out a review (with the first review to take place in 2020, and then for each year the Default Tariff Cap period is extended) into whether conditions are in place for effective competition for domestic supply contracts, before making a recommendation to the Secretary of State on whether the cap should be extended. Currently the Default Tariff Cap can be extended (12 months at a time) until 2023.[6]

Counterfactual

25. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.[7]

26. The Parties submitted that the prevailing conditions of competition is not the relevant counterfactual against which the Merger should be assessed. Instead, the Parties submitted that the CMA should take into account recent regulatory reforms which, according to the Parties, will further intensify competition in retail energy supply. In addition, the Parties submitted that the CMA should take into account two alternative scenarios regarding the Default Tariff Cap as part of its counterfactual.

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[5] The Domestic Gas and Electricity (Tariff Cap) Act 2018 received Royal Assent and entered into law on 19 July 2018.

[6] https://www.ofgem.gov.uk/energy-price-caps/about-energy-price-caps/price-my-energy-bill-capped/default-tariff-price-cap

[7] *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

EMI remedies and other regulatory measures

27. The Parties submitted that the EMI remedies, together with other measures that Ofgem is implementing, will increase customer engagement by all customers. In particular, the Parties submitted that in its counterfactual the CMA should take into account measures such as the roll out of smart meters, the Switching Programme[8], the PPM Price Cap, the Customer Prompt Remedy[9], and the Database Remedy[10] (in addition to the EMI remedies that the CMA took into account in its Final Report in *SSE Retail and Npower).*

28. The Parties referred in particular to trials conducted by Ofgem which, according to the Parties, demonstrate the likely effectiveness of the Customer Prompt and Database remedies.[11] The Parties also submitted that customer engagement has continued to increase.[12]

29. In its written submission to the CMA, Ofgem stated that, whilst Ofgem has undertaken considerable work on trialling the most appropriate measures to create timely and sustainable consumer engagement, a number of remedies are still in the process of implementation and their impact is still uncertain.

30. Moreover, whilst the CMA has recommended that Ofgem consider providing protection for prepayment customers after the expiry of the PPM Price Cap, the CMA considers that there is no certainty that this will be put in place.

31. The CMA considers that all these developments are ongoing and will not be affected by the Merger. Consequently, to the extent that the EMI remedies and other regulatory changes have been implemented, and their effect is reflected in the recent data that the CMA has used as part of its assessment, they will be included in the prevailing conditions of competition. In addition, on a forward-looking basis, the CMA has taken into account the potential removal of the PPM Price Cap in its competitive assessment (given the current uncertainty around its extension on expiry at the end of 2020).

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[8] This involves creating a single centralised switching service, to replace the existing separate gas and electricity switching services, which is due to be rolled out by 2021. See https://www.ofgem.gov.uk/gas/retail-market/market-review-and-reform/smarter-markets-programme/switchingprogramme

[9] The establishment by Ofgem of a programme to provide customers (directly or through their own suppliers) with information to prompt them to engage.

[10] The creation of an Ofgem-controlled database of 'disengaged customers' on default tariffs, which could allow rival suppliers to prompt these customers to engage in the retail energy markets.

[11] See eg https://www.ofgem.gov.uk/system/files/docs/2017/11/cmol_report_0.pdf; and https://www.ofgem.gov.uk/system/files/docs/2018/08/open_letter_collective_switch.v3finalnowm.pdf

[12] See https://www.ofgem.gov.uk/data-portal/retail-market-indicators. The data available on Ofgem's website is from January 2003 to April 2019.

Default Tariff Cap

32. The Parties submitted that the CMA should assess the Merger against a situation where either: (i) the Default Tariff Cap continues to be in place until at least the end of 2023; or (ii) the market is able to provide good outcomes for consumers absent the price cap and therefore the Default Tariff Cap is removed during this period.

33. The Default Tariff Place will apply to 2020 and can then be extended annually for a further three years. As noted above at paragraph 24, Ofgem is required to carry out a review (with the first review to take place in 2020), before making a recommendation to the Secretary of State on whether the cap should be extended.

34. In its written submission to the CMA, Ofgem stated that no safe assumptions can be made at the time of the CMA's assessment of the Merger on Ofgem's or the Secretary of State's decision on the continuation of the Default Tariff Cap at the end of each review year or beyond 2023.

35. The CMA considers that the available evidence does not support departing from the prevailing conditions of competition as the relevant counterfactual. It has taken into account the Default Tariff Cap in its competitive assessment (until the end of 2020 as there is no certainty whether it will be extended beyond that date).

Other measures cited by the Parties

36. The Parties also submitted that, as more customers use new technologies, which are already available on the market (such as smart meters, supplier applications, electric vehicles and in-house storage), this will drive increased customer engagement and increase the demands that customers make from their energy suppliers.

37. The CMA nevertheless found that there is uncertainty regarding the precise impact of these technologies on customer engagement and that the available evidence does not support departing from the prevailing conditions of competition as the relevant counterfactual.

Conclusion on the counterfactual

38. For these reasons, the CMA believes the prevailing conditions of competition to be the relevant counterfactual. It has taken into account the existence of the Default Tariff Cap and the PPM Price Cap (for both, at least until the end of 2020) in its competitive assessment.

Frame of reference

39. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merging parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.[13]

40. The Parties overlap in the retail supply of electricity and gas to domestic customers in GB.

41. The Parties also overlap in the supply of boiler and central heating insurance, the supply and installation of new domestic boilers, and the retail supply of fixed line broadband services to retail customers in GB. However, the CMA has not considered the overlaps in detail because the Parties have very low combined shares of supply in respect of these products and services, with very low increments (negligible for the supply and installation of new domestic boilers, and fixed line broadband services), which do not give rise to competition concerns.

Retail supply of energy to domestic customers

Product scope

42. The UK authorities have considered the retail supply of energy to domestic customers on a number of occasions, including the EMI and *SSE Retail and Npower*, and have generally distinguished between the supply of gas and electricity, given the material demand-side and supply-side differences in relation to these products.

43. The Parties submitted that the Merger should be assessed by reference to the retail supply of electricity and gas (separately) to domestic customers (in each case, regardless of whether the electricity or gas is supplied as a single fuel or as part of a dual fuel tariff). The Parties did not consider it appropriate to further segment by type of tariff, meter or payment method.

44. The CMA has not found any evidence to indicate that the approach previously adopted by the CMA in relation to the distinction between the supply of gas

[13] *Merger Assessment Guidelines*, paragraph 5.2.2.

and electricity as separate frames of reference is not appropriate in the present case.

Customer segmentation

45. The CMA may define relevant markets for separate customer groups if the effects of the merger on competition to supply a targeted group of customers may differ from its effects on other groups of customers, and require a separate analysis.[14] In this case, the CMA has considered two possible segmentations: by type of payment method, and differences in customer engagement.[15]

(a) Type of payment method: in its final report in *SSE Retail and Npower*, the CMA did not find it necessary to define a separate market for prepayment customers having regard to its findings in the phase 1 decision and the PPM Price Cap.[16] The CMA nevertheless stated that '[u]nlike other payment methods, prepayment is not typically a choice on the part of the customer and competition to supply prepayment customers differs significantly from competition to supply customers using other payment methods.'[17] In this case, the CMA found evidence of persistent differences in the competitor set and in supplier interactions, with fewer competitors supplying prepayment customers.[18] The CMA has also taken into account the findings in Ofgem's State of the energy market report, which refers to technical constraints involved in issuing new tariffs for prepayment customers and the higher costs associated with acquiring prepayment customers.[19] This evidence further supports consideration of prepayment customers as a separate frame of reference. Therefore, for the purpose of assessing this Merger, the CMA has considered the retail supply of energy to prepayment customers separately from the retail supply of energy to customers using other payment methods.

(b) Customer engagement: In its final report in *SSE Retail and Npower*, the CMA assessed differences in customer engagement as part of its

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[14] *Merger Assessment Guidelines*, paragraph 5.2.5(c).
[15] Although in previous cases restricted meters have been considered (see the phase 1 decision in *SSE Retail and Npower*), the CMA has not had to consider them for the purpose of assessing this Merger because there is no overlap between the Parties' activities. In particular, OVO does not offer non-Economy 7 restricted meter tariffs to new customers. See also *SSE Retail and Npower* final report, paragraph 7.18.
[16] *SSE Retail and Npower* final report, paragraph 7.20.
[17] *SSE Retail and Npower* final report, paragraph 7.19.
[18] As set out in more detail in the competitive assessment.
[19] Ofgem's State of the energy market report (2019), states that: 'many small suppliers have chosen not to offer [prepayment] tariffs due to technical constraints to issue new tariffs and to the higher costs to acquire [prepayment] customers. As a result, there are typically fewer suppliers active in the [prepayment] segment compared to the overall domestic retail market and only a few [prepayment] specialists have managed to expand beyond the six large suppliers.' Paragraphs 3.58-3.59.

competitive assessment, rather than distinguishing between customers on default tariffs and customers using acquisition tariffs.[20] The CMA has not found any evidence to indicate that the approach previously adopted is not appropriate in this case.

46. For the reasons set out above, and on a cautious Phase 1 basis, the CMA has considered the impact of the Merger by reference to the following frames of reference:

(a) the supply of electricity to domestic non-prepayment customers;

(b) the supply of gas to domestic non-prepayment customers;

(c) the supply of electricity to domestic prepayment customers; and

(d) the supply of gas to domestic prepayment customers.

47. Where relevant, the CMA has considered as part of its competitive assessment whether the effect of the Merger may differ depending on customer engagement (ie between customers using default tariffs and others using acquisition tariffs).

48. However, the CMA notes that it was not necessary to reach a conclusion on the product frame of reference, since, as set out below, no competition concerns arise on any plausible basis.

Geographic scope

49. The Parties submitted that, in line with previous decisional practice of the CMA and the OFT as well as the European Commission, the appropriate frame of reference is GB. The Parties referred to the factors listed in *SSE Retail and Npower*.[21] The Parties submitted that there is no reason to depart from the consistent decisional practice of the OFT/CMA and the European Commission in examining retail energy markets on a GB-wide basis.

50. The CMA has not found any evidence to indicate that a different geographic frame of reference is more appropriate in this case. Therefore, in line with previous decisions, including its final report in *SSE Retail and Npower*, the

[20] *SSE Retail and Npower*, final report, paragraphs 7.21-7.24. Acquisition tariffs are tariffs offered to new customers or existing customers choosing a new tariff. They are usually fixed-term contracts (**FTCs**) which are sold at a fixed price for a fixed period, eg one, two or three years. They may have 'exit fees' where a customer chooses to leave the tariff before the fixed time period has expired.
[21] *SSE Retail and Npower*, final report, paragraphs 7.26-7.33.

CMA has considered the impact of the Merger in the retail supply of energy to domestic (non-prepayment and prepayment) customers on a GB-wide basis.

51. Nevertheless, the evidence suggests that the Parties' pricing may to some extent vary depending on competitive conditions at the regional level and switching rates varied across different areas.

52. Therefore, in line with its decision in *SSE Retail and Npower*, notwithstanding the GB-wide frame of reference, the CMA has also assessed whether the Merger gives rise to competition concerns at a regional level, as part of its competitive assessment.[22]

53. However, the CMA notes that it was not necessary to reach a conclusion on the geographic frame of reference, since, as set out below, no competition concerns arise on any plausible basis.

Conclusion on frame of reference

54. For the reasons set out above, the CMA has considered the impact of the Merger by reference to the following frames of reference:

(a) the supply of electricity to domestic non-prepayment customers in GB;

(b) the supply of gas to domestic non-prepayment customers in GB;

(c) the supply of electricity to domestic prepayment customers in GB; and

(d) the supply of gas to domestic prepayment customers in GB.

55. Within this geographic frame of reference, as part of its competitive assessment, the CMA has taken into account any regional differences.

56. However, the CMA notes that it was not necessary to reach a conclusion on the frame of reference, since, as set out below, no competition concerns arise on any plausible basis.

[22] *SSE Retail and Npower*, final report, paragraph 7.33. '*The evidence does not indicate that the Merger will give rise to adverse effects in one geographic area which would not arise in other areas, although we will consider the possibility that any adverse effects could have a greater impact in some regions than in others in our competitive assessment*.'

Competitive assessment

Horizontal unilateral effects

57. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or to degrade quality on its own and without needing to coordinate with its rivals.[23] Horizontal unilateral effects are more likely when the merging parties are close competitors. The CMA assessed whether it is or may be the case that the Merger has resulted, or may be expected to result, in an SLC in relation to horizontal unilateral effects in the frames of reference set out above.

58. Regarding each frame of reference, the CMA has considered the Parties' and their competitors' shares of supply, closeness of competition between the Parties (in particular, by assessing switching data and third party evidence), competition from other providers, and the impact of the Default Tariff Cap and the PPM Price Cap. While undertaking a separate assessment for each frame of reference, the CMA has combined the discussion of unilateral effects in the supply of electricity and gas in the competitive assessment below.

Horizontal unilateral effects in the retail supply of electricity and gas to domestic non-prepayment customers in GB

Implications of the Default Tariff Cap

59. Information published by Ofgem shows that default tariff prices for the largest suppliers have clustered at the Default Tariff Cap since it was introduced.[24] Prices for default tariffs of other suppliers have been slightly lower since the introduction of the Default Tariff Cap.

60. The CMA has found that, at least until the end of 2020, the Parties' ability to increase prices to Default Tariff customers will be constrained by the Default Tariff Cap. However, the CMA has found that the Default Tariff Cap does not restrict the ability of the Parties or their competitors to increase acquisition tariff prices. This is because prices for acquisition tariffs are currently materially below the Default Tariff Cap.[25] Therefore, the CMA found that the Default Price Cap itself would not, in itself, prevent an SLC from arising in relation to acquisition tariffs.

[23] *Merger Assessment Guidelines*, from paragraph 5.4.1.
[24] See https://www.ofgem.gov.uk/data-portal/retail-price-comparison-company-and-tariff-type-domestic-gb.
[25] This is based on information provided to the CMA during its investigation. See also https://www.ofgem.gov.uk/data-portal/retail-market-indicators

Shares of supply

61. The Parties submitted that the Parties' and their competitors' shares of supply demonstrate that, post-Merger, the merged entity will only be marginally larger than SSE Retail is currently, with a modest share of supply that is smaller than both British Gas and E.ON across all of electricity, gas and dual fuel. The CMA also found that the merged entity will also continue to compete with a wide range of suppliers.

62. Table 1 presents shares of supply of domestic retail energy to non-prepayment domestic customers, separately for electricity and gas, based on Ofgem data.[26]

Table 1: Shares of supply of domestic retail energy to non-prepayment domestic customers in the UK in Q1 2019, by number of accounts

Supplier	**Electricity**	**Gas**
Ovo Energy	[0-5%]	[0-5%]
SSE	[10-20%]	[10-20%]
Combined	***[10-20%]***	***[10-20%]***
British Gas	[10-20%]	[20-30%]
E.ON/Npower	[20-30%]	[10-20%]
EDF Energy	[10-20%]	[5-10%]
Scottish Power	[10-20%]	[5-10%]
Bulb Energy	[5-10%]	[0-5%]
Shell Energy	[0-5%]	[0-5%]
Octopus Energy Ltd	[0-5%]	[0-5%]
Utility Warehouse	[0-5%]	[0-5%]
Avro Energy	[0-5%]	[0-5%]
Green Network Energy	[0-5%]	[0-5%]
Others	[5-10%]	[5-10%]

Source: CMA analysis based on Ofgem data.

63. Table 1 indicates that:

(a) British Gas and E.ON/Npower are particularly large, followed by SSE, EDF and Scottish Power, followed by a relatively long tail of smaller suppliers, including OVO.

[26] The CMA notes that the prepayment segment is a relatively small part of the overall sector and therefore shares of supply for all domestic customers are very similar to shares of supply for non-prepayment customers. On a cautious basis, the CMA has assessed whether including both prepayment customers and non-prepayment customers as part of the supply of energy to all customers made a difference to its assessment. The CMA found that it did not.

(b) The combined shares of supply of the Parties are [10-20%], with a [0-5%] increment. The Parties will be the third largest supplier following the Merger.

64. However, as noted in previous cases,[27] to some extent, shares of supply in the domestic retail energy market are likely to reflect the historic incumbent positions of some of the suppliers and the fact that many customers may have never switched supplier or may have not switched recently. The CMA has therefore placed more weight on its analysis of switching data which is likely to be more illustrative of the current competitive interactions.

Closeness of competition

- *Parties' submissions*

65. The Parties submitted that there is very limited switching between OVO and SSE Retail indicating that the Parties do not compete closely. The Parties also submitted that their pricing strategies [✂] between OVO and SSE Retail.

- *Switching data*

66. The Parties provided details of the customers who had switched away from them and the suppliers to whom those customers switched (separately for gas and electricity).

67. Having reviewed the overall switching between the Parties on a national basis, as well as switching by type of tariff applicable to the customer (ie looking in particular at customers on default tariffs), payment type (other than prepayment) and by region, the CMA generally found that the switching rates between the Parties are consistently low (as a proportion of total switching), providing strong evidence that the Parties are not particularly close competitors.

68. When looking at all customers (including prepayment and non-prepayment customers), the CMA observed slightly higher switching rates to SSE Retail from OVO in SSE's former public electricity suppliers (**PES**)[28] regions (the

[27] *SSE Retail and Npower*, final report, paragraphs 7.10 and 9.61.
[28] The PES were the fourteen regional electricity companies created in Great Britain when the electricity market in the United Kingdom was privatised.

former SSE regions of North of Scotland, Southern and South Wales), although not at a level to indicate any particular closeness of competition.

- *Internal documents*

69. The Parties' internal documents show that they monitor many energy suppliers, [✂].[29] The CMA has found no evidence in the Parties' internal documents to indicate that the Parties consider each other to be particularly close competitors regarding the supply of electricity and/or gas to domestic customers in GB (including at the regional level).

- *Third party submissions*

70. Most third-party responses suggested that the Parties do not compete particularly closely with each other in the supply of domestic retail energy in GB as a whole. Only some competitors indicated that the Parties compete closely. While most third-parties indicated that OVO and SSE Retail were amongst the other party's main competitors, they also indicated at least four other suppliers as OVO's and SSE Retail's main competitors.

71. In their responses, most competitors stated that the Parties do not compete closely in any region. One competitor observed that SSE Retail has a strong presence in North Scotland, Southern and South Wales while OVO has a stronger presence in 'North Western'. One competitor commented that the Merger 'might limit competition in some areas', while also stating that 'it could give an element of stability to the market.' However, as noted above, the switching data did not indicate levels of switching between the Parties that would give rise to concern either nationally or in any specific regions.

72. In its submission to the CMA, Ofgem stated that the highest rates of switching across groups of suppliers are currently observed from the large suppliers towards the medium-sized ones. Therefore, according to Ofgem, the removal of a challenger supplier, like [✂] (or [✂] or [✂]), from the market may lead to the loss of a significant competitive constraint. However, consistent with the evidence found by the CMA during its investigation, Ofgem submitted that its data does not suggest that the Parties are close competitors pre-Merger. Ofgem also observed that OVO is one of a number of medium-sized

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29 For example, OVO' SVT pricing documents seem to track SSE Retail among a number of other competitors, including [✂]. Similarly, the review of SSE Retail's internal documents suggested that SSE Retail monitors a broad range of providers and that its pricing is constrained by a broad range of providers [✂].

suppliers, together with [✂] and [✂], which may be considered challengers to the large suppliers.[30]

- *Conclusion on closeness of competition*

73. On the basis of this evidence, the CMA believes that the Parties are not close competitors for the supply of electricity or gas to domestic customers in GB. In particular, there are low levels of customer switching between the Parties, they do not monitor each other any closer than other suppliers and the large majority of third parties did not identify the Parties as being particularly close competitors.

Competitive constraints

- *Parties' submissions*

74. The Parties submitted that, given the low switching between the Parties and the range of different suppliers to which the Parties' customers are switching, there will continue to be a large number of competitors competing with and constraining the merged entity, post-Merger. The Parties stated that, post-Merger, the merged entity will compete with over 60 domestic retail energy suppliers, including the remaining larger energy suppliers (British Gas, E.ON, EDF and Scottish Power), as well as 56 newer suppliers, including Shell Energy, Bulb Energy, Octopus Energy and Utilita.

75. The Parties also submitted that all suppliers compete vigorously, most notably on price, but also on other parameters of competition such as customer service levels, product and tariff ranges, and availability of renewable fuels.

- *Switching data*

76. The switching data indicates that, on a GB basis, customers switch away from the Parties to a number of other suppliers. There were at least seven other suppliers to whom switching from one Party was greater than switching between the Parties. The data showed similar patterns when considering default tariffs (eg SVTs) and acquisition tariffs (eg FTCs) separately. In addition, the data showed moderate switching from each of the Parties to many suppliers across regions. The CMA found that in the North of Scotland,

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[30] In its State of the energy report (2019), Ofgem observed that '[m]edium suppliers have expanded, increasing their ability to exert competitive pressure on the large six suppliers. […] Bulb, Octopus Energy and OVO each grew significantly in this period. For Bulb and Octopus this growth can be attributed primarily to customers switching away from the six large suppliers although the direct acquisition of other suppliers/white labels was also an important factor for Octopus. OVO mainly grew by being appointed [Supplier of Last Resort] for Economy Energy and Spark.'

SSE Retail was one of the highest destinations of OVO customers. However, this switching was not at a level to indicate any particular concerns.

- *Internal documents*

77. As stated above, the Parties' internal documents suggest that the Parties monitor and compete with a range of suppliers in the market, [✂].

- *Third party submissions*

78. Third party evidence discussed in paragraphs 70-72 indicates that the Parties are constrained by a number of competitors in the market.

79. A number of third parties commented on changes in competition as a result of the Merger. Some third parties raised the concern that further consolidation would reduce competition. One observed there are currently nine established suppliers active in the market (E.ON, British Gas, Scottish Power, EDF, SSE, Octopus, Shell Energy, OVO and Bulb) and that competition in the market was considered less effective when only the 'Big 6'[31] had the scale to compete. Another third party indicated that the Merger could reduce the competitiveness of the market as a result of one of the 'Big 6' (or 'Big 5', based on Npower ceasing to be a Big 6 supplier) suppliers and a 'challenger' supplier combining.

80. Some other third parties did not have a firm view on the impact of the Merger (including because of the uncertainty around the merged entity's future strategy) but commented on possible changes to the market. One third party observed that the Merger could lead to two suppliers controlling almost 50% of the market, as opposed to six suppliers controlling around 70% (or five suppliers controlling just under half the market). Another third party commented that the Merger could produce a 'Huge 2', a 'Big 8', and a smaller group of medium and small suppliers in place of the current 'Big 6' suppliers with a group of medium suppliers and a longer tail of small suppliers.

81. In addition, some third parties were concerned about the merged entity's future strategy, in particular, if some of SSE Retail's activities were no longer carried out post-Merger. One third party was concerned that SSE Retail's removal from the market could damage competition in collective switches (OVO does not compete in collective switches).

82. The CMA, however, found that the increment due to the Merger (and thus change in the market structure) is relatively low (around [0-5%] in both gas

[31] The 'Big 6' refers to British Gas, SSE, npower, EON, EDF and Scottish Power.

and electricity). In gas, the two largest suppliers post-Merger, British Gas and E.ON, would hold a lower combined share than the third party comments suggest ([20-30%], [10-20%] respectively). In electricity, the two largest suppliers post-Merger, E.ON and British Gas would hold a lower combined share than the third party comments suggest ([20-30%], [10-20%] respectively). Moreover, in addition to British Gas, E.ON and the merged entity, EDF and Scottish Power will also have material shares of supply post-Merger (over [5-10%] in gas and [10-20%] in electricity). Lastly, for the reasons set out at paragraph 64, the CMA has placed more emphasis on the analysis of the switching data than on shares of supply. As noted, the switching data indicates that the Parties' customers switch to a range of different suppliers.

83. In its submission to the CMA, Ofgem stated that it did not have concerns when looking at the Merger 'on its own merits'. [See end note 1]

- *Implications of recent supplier exits*

84. As set out in the State of the energy market report (2019), a number of suppliers have exited the market, including those which are larger and more established, such as Spark Energy, Extra Energy and Economy Energy.[32] In its submission to the CMA, Ofgem stated that 20 domestic suppliers have exited the market since January 2018, which contrasts with the entry of ten new suppliers in the same time frame. Ofgem submitted that the subsequent market exit of a number of smaller but also mid-sized suppliers, like Spark, has led to further concentration in the retail energy market. Reasons for exit include cases of poor governance and lack of sufficient investment in systems and processes to support adequate customer service provision. Third parties also commented that the business models of these suppliers was unsustainable, including in the light of the competitive market conditions.

85. The majority of third parties observed that there remain a significant number of competitors in the market and that the Merger will not have an impact on competition. A few third parties stated that these exits reduce trust in small players and that therefore licensing rules need to be strengthened.

86. The CMA considers that, despite some recent supplier exits, there are a significant number of active suppliers. Furthermore, the CMA found no evidence that any of the suppliers accounting individually for a material level of switching away from the Parties were likely to exit in the foreseeable future. Therefore, the CMA does not consider that recent supplier exits, or the

[32] Paragraph 3.7.

possibility of future exits, which are part of the prevailing conditions of competition in this sector, materially affect its assessment of this Merger.

- *Conclusion on competitive constraints*

87. The evidence set out above, in particular the switching data and third party evidence, indicates that the Parties will be constrained by a number of competitors post-Merger, including large energy firms and at least some of the SAMS.

Conclusion on horizontal unilateral effects in the retail supply of electricity and/or gas to domestic non-prepayment customers in GB

88. On the basis of the available evidence and for the reasons set out above, the CMA believes that the Parties are not close competitors and that the merged entity will face sufficient competitive constraints from a number of suppliers regarding the supply of electricity and gas to domestic customers in GB. The evidence indicates that this finding also applies to possible segmentations based on the customer's tariff type (default tariffs (eg SVTs) and acquisition tariffs (eg FTCs)), the payment type (other than prepayment) and at regional level.

89. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to:

    (a) the retail supply of electricity to domestic non-prepayment customers in GB; or

    (b) the retail supply of gas to domestic non-prepayment customers in GB.

Horizontal unilateral effects in the retail supply of electricity and gas to domestic prepayment customers in GB

Implications of the PPM Price Cap

90. The CMA has found that at least until the end of 2020 prices are constrained by the PPM Price Cap, thus preventing Parties (and their competitors) from increasing their prices to prepayment customers. In particular, following the introduction of the PPM Price Cap there has been very limited price competition between suppliers in relation to prepayment meter customers.[33] Instead, competition is focussed on non-price parameters such as the ability

[33] *SSE Retail and Npower*, final report, paragraphs 7.19(c).

to provide smart metering,[34] brand recognition and other aspects of the product offering.

91. However, there is no certainty that this will be the case after the end of 2020. Moreover, the CMA found that the PPM Price Cap would not prevent an SLC from arising on non-price parameters (eg quality of service).

Shares of supply

92. Table 2 presents shares of supply of domestic retail energy to prepayment customers, separately for electricity and gas, based on Ofgem data.

Table 2: Shares of supply of domestic retail electricity to domestic prepayment customers in the UK in Q1 2019, by number of accounts, based on Ofgem data

Supplier	Electricity	Gas
SSE	[10-20%]	[5-10%]
Ovo Energy	[10-20%]	[10-20%]
Combined	***[20-30%]***	***[10-20%]***
British Gas	[20-30%]	[30-40%]
Utilita	[10-20%]	[10-20%]
E.ON/Npower	[10-20%]	[10-20%]
EDF Energy	[10-20%]	[5-10%]
Scottish Power	[5-10%]	[5-10%]
E	[0-5%]	[5-10%]
Utility Warehouse	[0-5%]	[0-5%]
Bulb Energy	[0-5%]	[0-5%]
Others	[0-5%]	[0-5%]

Source: CMA analysis based on Ofgem data.

93. Table 2 shows that, after the Merger, the merged entity would hold a relatively modest combined market share of [10-20%] in supplying gas to prepayment customers and [20-30%] in supplying electricity to prepayment customers. In its submission to the CMA, Ofgem stated that [✂], with [30-40%] in the retail supply of gas to domestic prepayment customers and [20-30%] in the retail supply of electricity to domestic prepayment customers, the Merger would create two large prepayment suppliers, with only [✂] left as a rival having a comparable [✂] market share (around [10-20%] in [✂] gas and electricity). The CMA notes that E.ON/Npower and EDF Energy have shares of supply of [10-20%] in electricity and [10-20%] in gas and [10-20%] in electricity and [5-10%] in gas, respectively.

[34] Smart meters are of particular value to prepayment meter customers because of the additional convenience they provide and the wider range of tariffs they can accommodate.

94. The CMA notes that, as set out in Table 2, the increment would be [5-10%] (in gas and [10-20%] in electricity).

95. As set out in Ofgem's State of the energy market report (2019), many small suppliers continue to choose not to offer prepayment tariffs due to technical constraints in issuing new tariffs and to the higher costs to acquire these customers. As a result, there are still fewer suppliers active in the prepayment segment compared to the overall retail market.[35] In its submission to the CMA, Ofgem stated that only a few prepayment specialist suppliers, [✂], have managed to expand, beyond the largest suppliers.

96. As set out at paragraph 64, the CMA considers that shares of supply are not particularly informative in the retail energy market. This is because they are likely to reflect the historic incumbent positions of some of the suppliers and the fact that many customers may have never switched supplier or may have not switched recently. The CMA has therefore placed more weight on its analysis of switching data, as well as third party evidence and internal documents.

Closeness of competition

- *Parties' submissions*

97. The Parties provided switching data and submitted that the analysis of the switching that occurs between the Parties shows that the Parties are not close competitors in the supply of energy to domestic prepayment customers.

- *Switching data*

98. The CMA analysed the switching data provided by the Parties. The CMA found that switching between the Parties is generally higher for prepayment customers than for non-prepayment customers (this is in part because there are fewer competitors in this segment).

99. On a national basis, switching of prepayment customers from OVO to SSE Retail was low. Moreover, six rivals obtained a higher switching rate than SSE Retail, [✂] (a strong brand in prepayment) obtaining a much higher switching rate. [✂]. However, the switching rate from SSE to OVO was low. The data showed that SSE Retail lost the highest share of customers to [✂], followed by [✂] and a significant proportion of switching by SSE Retail prepayment customers is to other suppliers. The CMA's analysis of the switching data shows that the Parties do not compete particularly closely at the GB level

[35] See footnote 19.

regarding the supply of gas and/or electricity to domestic prepayment customers.

100. The switching data also shows that the Parties compete to some extent more closely at the regional level (compared to the GB level). There are two regions in particular (North of Scotland and South Wales) where the switching data indicate that SSE Retail is a more important competitor to OVO than in other regions. However, the switching rate from OVO to SSE Retail in these regions is still relatively low, which shows that remaining competitors in these regions obtain substantial amount of switching from OVO.

- *Internal documents*

101. SSE Retail's internal documents only discuss prepayment meter competition to a limited extent. SSE Retail documents that discuss monitoring of competitors in prepayment refer to a broad range of providers, one of them being OVO.[36] OVO documents submitted to the CMA do not refer to the monitoring of competitors regarding prepayment.

- *Third party submissions*

102. Over half of the third parties indicated that OVO and SSE Retail were amongst the other party's main competitors. However, several of these third parties typically mentioned at least another three main competitors, while the majority mentioned at least another five main competitors. Third parties did not comment on competition regarding domestic prepayment customers at the regional level.

103. The CMA was told by one third party that the Merger would remove an important competitor in this segment, on the basis that OVO is a specialist provider in prepayment tariffs and that it has significantly expanded its presence in this market since the recent acquisition of prepayment customers from failed suppliers. In particular, through its dedicated white label Boost, and especially after the acquisition of Economy Energy and Spark, OVO has reached a market share, both in the supply of retail gas and electricity to domestic prepayment customers, that is currently around [10-20%], very similar to SSE Retail's prepayment market share. However, this third party did not indicate that the Parties are close competitors. In its submission to the

[36] Competitors that were explicitly mentioned include [✂].

CMA, Ofgem [✂] (which is consistent with the CMA's analysis of the switching data and other third party views). [See end note 2]

- *Conclusion on closeness of competition*

104. On the basis of this evidence, the CMA believes that the Parties are not particularly close competitors for the supply of retail energy to prepayment customers in GB.

Competitive constraints

- *Parties' submissions*

105. The Parties submitted that the same wide set of competing suppliers typically compete for customers across all customer segments, and, as a result, the competitive dynamics are substantially similar in any customer segment, including PPM.

- *Switching data*

106. While the CMA observed a materially smaller number of suppliers operating in the retail supply of prepayment customers as compared to the retail supply of non-prepayment customers, the switching data suggests that a number of suppliers compete across GB to supply prepayment customers. In addition, the CMA found no evidence of material challenges to supply across regions (eg [✂] accounts for a significant proportion of switching and has only recently introduced a prepayment tariff).

107. As regards regional switching, while in a number of regions OVO is the [✂] SSE Retail customer destination, the data shows that there are a number of other suppliers active in each region with material switching rates (eg [✂], [✂], and [✂]). In terms of switching from OVO to SSE Retail, the data shows that in two regions (North of Scotland and South Wales) SSE Retail is one of several competitors with a higher number of switches from OVO, together with [✂] in both regions, as well as [✂] and [✂] in the North of Scotland. Moreover, in these regions there are a number of other competitors ([✂]). In other regions, the switching rate from OVO to SSE is also not at a level that would cause concern.

- *Internal documents*

108. To the extent that SSE Retail's documents discuss the monitoring of competitors in prepayment, they refer to a broad range of providers, one of them being OVO. Competitors that were explicitly mentioned include [✄].

- *Third party submissions*

109. As noted above, although over half of the third parties indicated that OVO and SSE Retail were amongst the other party's main competitors, several of these third parties typically mentioned at least another three main competitors, while the majority mentioned at least another five main competitors

- *Conclusion on competitive constraints*

110. Although there are fewer competitors active in this segment, the evidence set out above, in particular the switching data, shows that there generally exists strong competition to the Parties. While, based on switching data, the Parties appear to compete more closely in some regions (eg North of Scotland and South Wales), there remain a number of other competitors (such as Utilita, Bulb and Scottish Power) and the switching rate is not at a level that would cause concern.

Conclusion on horizontal unilateral effects in the retail supply of electricity and gas to domestic prepayment customers in GB

111. For the reasons set out above, the CMA believes that the Parties are not particularly close competitors and that the merged entity will face a sufficient competitive constraint from a number of suppliers in the supply of electricity and/or gas to domestic prepayment customers in GB. In addition, while the switching data suggests that the Parties compete more closely in some regions, a number of sufficiently strong competitors will remain post-Merger.

112. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to:

    (a) the retail supply of electricity to domestic prepayment customers in GB; or

    (b) the retail supply of gas to domestic prepayment customers in GB.

Barriers to entry and expansion

113. Entry, or expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC. In assessing whether entry or expansion might prevent an SLC, the CMA

considers whether such entry or expansion would be timely, likely and sufficient.[37]

114. However, the CMA has not had to conclude on barriers to entry or expansion as the Merger does not give rise to competition concerns on any basis.

Third party views

115. The CMA contacted competitors of the Parties, as well as price comparison websites, collective switching organisations, consumer organisations, and Ofgem, as sector regulator. Third party comments have been taken into account where appropriate in the competitive assessment above.

116. The CMA received some third party comments regarding the risks of future consolidation in the future. Ofgem [✂].

117. In addition, some third parties commented that the integration process could lead to disruptions to the merged entity's consumer-facing activities.

Decision

118. Consequently, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the United Kingdom.

119. The Merger will therefore **not be referred** under section 33(1) of the Act.

Alex Olive
Director, Mergers
Competition and Markets Authority
10 December 2019

End notes

1. Paragraph 83, Ofgem requested the CMA to publish this fuller sentence which reflects their submission: 'Ofgem did not raise prima facie competition concerns about this Transaction, if reviewed on its own merits, leading to a substantial lessening of competition in the GB retail energy market. However, it highlighted certain areas which it advised the CMA to investigate in more depth.'

[37] *Merger Assessment Guidelines*, from paragraph 5.8.1.

2. Paragraph 103, The redacted text has been removed from the decision following clarification by Ofgem.