Promoting choice and value
for all gas and electricity customers

The Retail Market Review – Updated domestic proposals

Consultation

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Overview:

The aim of the Retail Market Review (RMR) is to encourage and equip consumers to get the best deal from the energy market. We are looking to rebuild trust and confidence in the market so that more people are inclined to engage, and to put in place measures so that consumers are better able to choose the deal that suits them. A combination of the competitive pressure this creates and additional consumer protection we introduce should mean that the market better serves the interests of consumers.

This document sets out our updated RMR proposals for the domestic market, following our consultation in December 2011. Our proposals for the non-domestic sector are set out in a separate document we have published today.

We have looked to make best use of our statutory powers to address the concerns we have about the domestic market. If, following consultation, we consider that our proposals do not have a realistic chance of addressing the concerns identified due to industry opposition or otherwise, we retain the option that we have flagged in our previous consultations of referring the market to the Competition Commission for a Market Investigation Reference.

These proposals represent an important development in the functioning of the retail market and it is important to allow stakeholders adequate time to present their views. Our deadline for responses to this consultation is 21 December 2012.

Context

Ofgem's principal objective is to protect the interests of both existing and future energy consumers. The RMR aims to make the market better at serving the interests of consumers and enable individuals to get a better deal from energy companies.

The proposals presented in this document cover seven policy areas, as well as a number of interrelated issues. We summarise their key elements below. Proposals for the non-domestic market are published in a separate consultation document.

In conjunction with this consultation document we also publish a further draft Impact Assessment on the proposals and the draft legal text for new and amended licence conditions. We have also published our latest consumer research undertaken to inform our findings.

The RMR has links with our Consumer Vulnerability Strategy[1], Smarter Markets Strategy[2] and our work on liquidity[3]. We are working to ensure our RMR proposals work in a complementary manner to these initiatives.

Alongside this document we are publishing our decision not to re-insert the undue discrimination licence condition (SLC 25A)[4].

Associated documents

All documents are available at www.ofgem.gov.uk

- Supplementary appendix to: The Retail Market Review – Updated domestic proposals, Reference: 135a/12, October 2012.
- The Retail Market Review – Draft Impact Assessment for the updated domestic proposals, Reference: 135b/12, October 2012.
- Draft domestic licence conditions for the Retail Market Review proposals, Reference: 135c/12, October 2012.

1 For more information see the following link: http://www.ofgem.gov.uk/Sustainability/SocAction/Pages/SocAction.aspx
2 For more information see the following link: http://www.ofgem.gov.uk/Markets/sm/strategy/Pages/Strategy.aspx
3 For more information see the following links: http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/Pages/CompandEff.aspx and http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Pages/rmr.aspx
4 Our decision letter will be published alongside this document, and will be placed at the following location: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Pages/rmr.aspx

- Ipsos MORI, Prompting engagement with and retention of written customer communications, Final report prepared for Ofgem, October 2012.
- SPA Future Thinking, Price Increase Notification Letters, Summary Box on Bills, Tariff Information Labels and Annual Statements, Report of consumer testing to support template development, forthcoming.
- Ipsos MORI, Consumer views on Tariff Comparison Rates, Findings from the Ofgem Consumer First Panel Year 4 and new participants: Fourth workshops (held in August 2012), October 2012.
- SPA Future Thinking, Options for cheapest tariff messaging on customer communications; Report of qualitative research, forthcoming.
- Insight Exchange, Consumer research and collaborative engagement on the proposed Standards of Conduct – Domestic Customers, October 2012.
- Ipsos MORI, Consumers' views of price comparison guides and tariff structures, October 2012.
- Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
- Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
- The Standardised Element of Standard Tariffs under the Retail Market Review, February 2012, Reference: 11/12
- Ipsos MORI, Ofgem Consumer First Panel Year 4, Findings from first workshops (held in October and November 2011), January 2012
- The Retail Market Review: Domestic Proposals, December 2011, Reference: 116/11
- The Retail Market Review: Draft Impact Assessment for Domestic Proposals, Supplementary Appendices, December 2011, Reference: 116A/11
- The Retail Market Review – Non Domestic Proposals, November 2011, Reference: 157/11
- The Retail Market Review – Draft Impact Assessment for Non Domestic Proposals, November 2011, Reference: 157A/11
- Retail Market Review: Energy bills, annual statements and price rise notifications; advice on the use of layout and language. A Research Report For Ofgem, Lawes Consulting and Lawes Gadsby Semiotics, November 2011
- Creative Research, Tariff Comparability Models, Volume 1 and 2 - Consumer qualitative research findings, October 2011

- Ipsos MORI, Consumer reactions to varying tariff comparability models, Quantitative Research conducted for Ofgem, 18 October 2011
- Ofgem's Retail Market Review – update and next steps (non-liquidity proposals), June 2011
- Ofgem's Retail Market Review – update and next steps (liquidity proposals), June 2011
- The Retail Market Review – Findings and Initial Proposals, March 2011, Reference: 34/11
- Ofgem Consumer First Panel, Year 3 2010/11, Findings From The Second Set Of Workshops, Opinion Leader, March 2011
- Ipsos MORI, Customer Engagement with the Energy Market – Tracking Survey, March 2011
- FDS International, Vulnerable Customer Research, March 2011
- Energy Supply Probe - Proposed Retail Market Remedies, August 2009, Reference: 99/09
- Ipsos MORI, Report on the 2009 Consumer Conditions Survey Market research survey conducted for Consumer Focus, March/April 2009
- Ofgem Consumer First Panel, Research Findings from the Second Events – Billing Information and Price Metrics, March 2009
- Ofgem Consumer First Panel, Research findings from first event, January 2009
- Energy Supply Probe - Initial Findings Report, October 2008, Reference: 140/08

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Executive Summary

The energy retail market needs significant reform

Significant investment is required in the energy industry to maintain secure supplies and achieve targets to reduce carbon emissions. As Ofgem highlighted in Project Discovery[5], this combined with increases in global fuel prices, is placing upward pressure on wholesale prices and consumer bills; a trend that is widely expected to continue for at least the next decade. With household budgets under strain, it is more important than ever that the retail energy market[6] works in the interests of consumers and that they are able to shop around to find the best energy deal.

Our Retail Market Review (RMR) aims to encourage and equip consumers to engage effectively in the market. Steps taken to promote such engagement now will also make it easier for consumers to realise the benefits offered by smart metering[7] in the future, allowing households to manage their energy consumption as well as their choice of supplier.

There are a number of factors which limit effective consumer engagement in the energy market. The large number of tariffs and their complexity discourage many from exploring alternative deals. Even the more active consumers can find it difficult to make the right choice. Unlike many other markets, most consumers are on open-ended, evergreen contracts and rarely, if ever, are prompted to look for a better deal or shown the savings they might make. Also a general lack of trust in the industry, arising from poor consumer experience, means that many consumers have disengaged altogether because they believe there is little to be gained from considering alternative offers.

These factors prevent the market from serving consumer interests as well as it could. While there is intense competition between suppliers for the small number of active customers, the six incumbent suppliers can respond by recovering costs from their large 'sticky' customer base. There is little evidence of competition driving down costs or spurring significant improvements in service for consumers as a whole.

In response to our last RMR proposals in December 2011, some suppliers have taken steps to address consumer trust and confidence and to make it easier for them to understand the market. We have seen initiatives to reduce tariff numbers and complexity and improve the clarity of information sent to consumers. We welcome this response to our initiative and encourage suppliers to continue their work on this

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[5] For more information, see the following link: http://www.ofgem.gov.uk/Markets/WhlMkts/monitoring-energy-security/Discovery/Pages/ProjectDiscovery.aspx.

[6] In this consultation document and associated documentation we use the terms 'market' and 'markets' as a shorthand for referring to different segments of the energy sector. For the avoidance of doubt these terms are not intended to describe or otherwise suggest the approach that may be taken by Ofgem for the purposes of market definition in competition law investigations.

[7] A smart meter provides measured gas and electricity consumption data for multiple time periods, and is able to provide the relevant supplier with remote access to such data.

front. However, there remains a role for common and binding requirements on suppliers. Not all suppliers have taken steps to improve their interactions with consumers, and we think much more needs to be done to engage the least active consumers. Putting new arrangements in the supply licence, and exposing suppliers to the risk of penalties if they do not comply, is a necessary step towards regaining consumers' trust in the market.

Our updated retail market reform proposals

Building on our last proposals and the subsequent consultation responses, we have developed a far reaching package of reforms which we are confident will be successful in improving consumer engagement. These aim to make it easier for those that are already engaged in the market to make good choices. For those that are not, we aim to build their confidence to get involved in the market, prompt them to explore alternative deals and give them the tools they need to choose the best tariff.

Simpler, clearer, fairer

Our proposals require suppliers to provide consumers with: simpler choices; clearer information about products, prices and available savings; and fairer treatment in all their interactions with them.

Our key proposals are to:

- Limit each supplier to 4 tariffs per fuel, per meter and per payment type;

- Put an end to complicated multi-tier tariffs, requiring all tariffs to be set out in a simple standing charge and unit rate structure;

- Require suppliers to give consumers personalised information on their bill of the estimated savings they could make if they switch to their supplier's cheapest deal;

- Introduce a Tariff Comparison Rate: a 'common currency' to allow customers to compare tariffs across the market;

- Require suppliers to give all customers a new, improved Annual Statement with the personalised information a consumer needs to engage in the market, and to provide other 'calls to action' on bills and in the letter notifying consumers of price increases;

- Introduce new licence conditions to require suppliers to treat their customers fairly and to embed this principle throughout their business.

Personalised market best deal information

We are confident these proposals will bring real benefits for engaged consumers in the market and, by rebuilding trust and confidence, that they will widen the pool of engaged consumers. However, these proposals do not provide consumers, particularly those who do not have internet access or may be vulnerable, with easy access to personalised information on the best deal across the market. Our research suggests that without additional help, many consumers will not enter the market of their own accord. This could leave these consumers individually at risk and threaten our broader aim of providing an effective competitive constraint on suppliers.

In our December document we looked to achieve 'at a glance' comparisons for standard variable tariffs by setting a uniform national standing charge and limiting suppliers to one such tariff per payment method. We have listened carefully to the concerns raised by consumer groups and other stakeholders about these proposals. We have also uncovered practical difficulties in achieving this aim through this route. We have therefore decided we should look to achieve our 'at a glance' objective through other means.

We now plan to give further consideration to a proposal that would require suppliers to give the least active and most vulnerable consumers direct and personalised information about the cheapest deals across the whole market. This would enable these consumers to choose, with confidence, the best deal for their own circumstances without the need for complex calculation or the use of a switching site. There are many practical and other considerations which would need to be addressed before this idea could be implemented. We therefore propose to trial such a proposal in conjunction with the suppliers to see whether providing such personalised information would prove effective in engaging 'sticky' customers and how this could best be done.

Facilitating the role of intermediaries

These proposals are focused on placing new requirements on suppliers. However, switching sites and other intermediaries have an important, and potentially growing, role to play in assisting consumer engagement in the industry. We shall consider what more we can do to facilitate this role.

We will be looking to facilitate collective switching initiatives, consider how best to operate the Confidence Code which applies to price comparison sites and consider how best to protect consumers when they use brokers and other third party intermediaries.

Way forward

Ofgem operates within a statutory framework that requires us to consult fully with stakeholders ahead of implementing changes to licences and market arrangements. The process of consultation and engagement with stakeholders is an important step in ensuring that any measures are effective and fit for purpose. Although it is important that these reforms are implemented at the earliest opportunity, it is also important to allow full time for consultation. However, companies have already made important improvements in the way they treat customers in response to our previous proposals, and there is no reason why they cannot make further improvements consistent with our proposals before any licence conditions become effective.

We aim for these reforms to come into legal effect in the supply licence from summer 2013, subject to responses to this document and the outcome of a statutory consultation in spring 2013. We propose to require suppliers to introduce some of these measures on 'day one', with time given for them to make the back office system changes necessary for other measures. Our proposal is that all measures should be in place by winter 2013. We would aim to start the trials of the Market Cheapest Deal initiative within 6 months after day one.

Following implementation, we will monitor the direct impact the RMR package is having on consumer engagement and the impact that this engagement has on the market. If our reforms come into effect according to the above timetable, and assuming there is no clear reason to delay, we will review the package in full no later than 2017.

We are consulting on the proposals in this document until 21 December 2012. To assist stakeholders, we will hold a workshop on our proposals at the end of November. If you would like to attend this workshop please contact rmr@ofgem.gov.uk.

1. Overview of the package

1.1. This chapter sets out the background to this document and provides an overview of the package of RMR proposals. We explain how our RMR project relates to other work Ofgem is doing and set out the next steps and a draft implementation timetable for the project.

Background

1.2. Since the Energy Supply Probe ('the Probe') in 2008, Ofgem has been concerned that the market is not working in the best interests of consumers. The Probe found that there were a range of features in the market that weakened competition. These included structural features reinforced by the behaviour of suppliers and the lack of engagement and poor decision making by consumers.

1.3. Through the Probe we placed a range of specific requirements on suppliers (for example on how they conduct their marketing and the price differentials between payment methods) and we also presented them with a challenge to improve their conduct towards customers, through voluntary standards of conduct and rules on the information they provide to customers. These high level requirements were put in place with the expectation that they would help consumers become more engaged in the market.

1.4. In late 2010, we launched the Retail Market Review (RMR). While we had seen some improvements in the information provided to consumers since the Probe as a result of our new licence conditions and their enforcement, we concluded that many of the problems with consumer engagement identified in the Probe remained. Since then we have been working on a range of proposals to place specific and binding requirements on suppliers to address our concerns. We consulted on an initial set of proposals in December last year. This document sets out our updated proposals, following extensive consultation and further consumer research and policy development.

1.5. The overall objective of the RMR is to improve effective consumer engagement so as to increase competitive pressure on suppliers' pricing and other practices. Within this we aim to improve the choices that individual consumers make, widen the pool of customers who have the confidence to engage in the market and address the specific needs of the most disengaged consumers. In this way we aim to reduce the scale and instance of individual consumer harm resulting from insufficient or ineffective engagement.

The RMR proposals

Overview of the updated package

1.6. Building on the proposals we published in December last year, and responding to points made by consultees, we have designed an updated package of proposals. The resulting package addresses the concerns that stakeholders raised about our December proposals, takes account of suppliers' recent actions to rebuild trust and reduce tariff complexity and, we believe, is at least as effective as our December proposals.

1.7. We are looking to meet three objectives through this package within the overall aim of improving effective consumer engagement. Firstly, we aim to present consumers with **simpler** choices when they are looking for alternative offers. Secondly, we aim to give consumers access to **clearer** information on products, prices and savings. Finally, we are also looking to provide consumers with **fairer** treatment in all their interactions with suppliers.

Simpler choices

1.8. Many consumers tell us they are confused by the large number of complex tariffs which can deter them from engaging in the market and make it harder for them to choose when they do. Despite voluntary standards of conduct introduced through the Probe which included an 'expectation that suppliers take all reasonable steps to not offer products that are unnecessarily complex and confusing' we did not see a reduction in the number or complexity of tariffs in the market. While some suppliers have taken steps this year to reduce tariff numbers and to simplify their structures, more needs to be done to address this key barrier to engagement.

1.9. We propose to place a cap on the number of tariffs and introduce further rules to make tariffs simpler. We propose that each supplier is allowed to offer to any customer at any time only 4 tariffs per fuel. Our simplification rules include requiring:

- all tariffs to have a simple two part structure (no multi-tier tariffs[8]);
- tariffs can have a range of payment types but there needs to be the same differentials between payment types across all tariffs;
- dual fuel discounts to be the same across all tariffs and expressed as £/annum, not as a percentage, and

[8] Time of use tariffs will be permitted as long as there is only one unit rate applicable for any particular time period.

- a prohibition on suppliers offering loyalty bonuses for customers on evergreen tariffs[9] as these are equivalent to exit fees, which are not currently permitted.

1.10. Suppliers will need to ensure that any customer who is currently on an evergreen tariff which is no longer open to new customers (a 'dead' tariff) is migrated to their cheapest live evergreen tariff, unless the dead tariff is cheaper for the customer than any of the current live tariffs on offer.

1.11. More detail on these proposals is set out in chapter 4 of part B of this document.

Clearer information on products, prices and savings

1.12. Despite the Probe reforms which placed new rules on the information suppliers should provide to their customers, consumers tell us that they do not receive the information they need to make informed decisions about their tariff. Nor are they given enough information about cost savings to stimulate engagement.

1.13. For this reason the RMR proposals go further than the Probe and prescribe the content and, in some cases the format of: a summary box on bills; Annual Statements; End of Contract Letters; Price Increase Notifications (PINs); and Tariff Information Labels (TIL) containing the key terms and conditions of each tariff.

1.14. We propose that suppliers must provide clear prompts to consider switching supplier, and information on the routes they can use to explore alternative offers, in all of these communications. Between the summary box on bills and the Annual Statement, consumers will regularly receive all the information they need about their current tariff and their own consumption so they can compare the cost of their current arrangements with alternatives. We will introduce standardised definitions for key terms to be used in the documents noted above to make them easier to understand. We will also publish information on suppliers' customer service performance so that consumers can consider this, alongside the information on the TIL, when they are exploring their options.

1.15. More detail on these proposals to provide clearer information is set out in chapter 5.

1.16. Alongside improvements in the content, language and layout of the information sent by suppliers to consumers, we propose to require suppliers to:

- provide each of their customers with personalised information on the supplier's estimated cheapest tariff. This information will need to be on the bill, the Annual Statement, PINs and End of Contract Letters;

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[9] An evergreen tariff is any tariff that is for an indefinite length.

- introduce a Tariff Comparison Rate (TCR) for each of their tariffs. This will establish a single figure 'common currency' for expressing all tariffs and allow like for like comparison of tariffs across the market. This information will need to be used in all marketing materials. Suppliers will need to inform their customers of the TCR for their current tariff on the bill, in the Annual Statement and in the PIN, and

- provide each of their customers with regular 'personalised projections' of what the customer might spend over the next year on its current tariff. This information will need to be on the bill, the Annual Statement and in PINs. Suppliers will be required to use the rules we prescribe for calculating the personalised projection as far as possible when providing estimates to prospective customers.

1.17. Further detail on the Supplier's Cheapest Deal proposals is set out in chapter 6 of Part B with more detail on the TCR and the personalised projections in chapter 7.

Fairer treatment

1.18. Even if consumers are prompted to engage and are given all they need to access market information and assess alternatives, they may be put off engaging if they do not trust the information suppliers give them or are anxious that they will end up paying more if they switch. As part of the Probe we introduced voluntary standards of conduct to encourage suppliers to improve consumers' trust and confidence in engaging in the market. However, we saw little evidence of suppliers complying with the spirit of these standards. Trust in energy companies is low and consumers continue to tell us that poor experiences with the suppliers can reduce their confidence in engaging in the market. Indeed, a 2009 survey of a number of performance indicators showed consumers had the worst perception of gas and electricity companies across the range of market sectors surveyed[10].

1.19. We propose to rebuild consumer trust through measures to ensure fairer treatment by introducing:

- Enforceable Standards of Conduct (SOC) covering all interactions between the supplier and their customers. This new licence condition will essentially require suppliers to treat their customers fairly and will make it clear they are responsible for embedding this fairness objective in their business, and

- New rules, including on the contract terms around fixed term tariffs to prevent price increases and other unilateral changes to their contracts and prevent consumers rolling over onto further fixed term contracts that may impose termination fees.

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[10] Ipsos MORI, Report on the 2009 Consumer Conditions Survey Market research survey conducted for Consumer Focus, March/April 2009.

1.20. Together these rules will provide clarity as to what consumers can expect from their supplier in their ongoing interactions with them, as well as improving and clarifying the terms and conditions of their tariffs. These measures should ensure individual fair treatment as well as help improve consumer confidence in engaging in the market.

Market Cheapest Deal

1.21. We are confident that the above reforms will make it easier for active consumers to choose the best deal and will widen the pool of engaged consumers through further prompts and building trust and confidence. These proposals are therefore justified in their own right. However, our consumer research suggests that for many sticky customers, these reforms will not be sufficient to encourage them to enter the market of their own accord. The market would need to be significantly further simplified to achieve this aim. This could undermine our overall objective of making the market sufficiently competitive to constrain the pricing behaviour of suppliers and incentivise improved efficiency and service.

1.22. In December we proposed to address this issue through a range of measures aimed at allowing consumers to compare offers across the market 'at a glance'. Our proposals included limiting suppliers to only one evergreen (standard) tariff per payment method and fuel, with Ofgem setting the standing charge of these tariffs so that consumers would only need to look at a single figure (the unit rate) to compare tariffs.

1.23. Stakeholders raised significant concerns about these proposals, for example that they would limit scope for innovation and competition and remove some products which consumers value. There was a concern that our proposals to cap the number of tariffs in the evergreen but not the fixed term market would lead to further segmentation of the market and a proliferation of fixed term products and further consumer confusion. There was also a concern that a uniform national standing charge may harm particular groups of customers. We considered these responses in detail. We have also considered and consulted on how we would implement these proposals and this has raised further questions about our ability to meet our objectives through these proposals.

1.24. Rather than further reducing the number of tariffs in the market and removing some of the products which consumers value, we propose some consumers should be given information about how much they could save by switching to the cheapest deals in the market, based on their personal circumstances and their actual consumption. We are concerned that unless more is done to make the market more accessible for these consumers, they could be left vulnerable and we could undermine the achievement of our broader aim of providing an effective competitive constraint on suppliers.

1.25. Our proposal is to develop a scheme to provide the most sticky and vulnerable consumers with personalised information about the estimated cheapest deals for them in the market, perhaps on an annual basis. These consumers are the least likely to use the information in the RMR package to assess the offers available and are most likely to need direct and personal information about savings to raise awareness.

1.26. We propose that we undertake further work to develop the details of the scheme, including looking at a range of approaches for getting this information to consumers. We think it would be in line with best practice to work with suppliers and other parties as appropriate to trial the scheme before any decision is taken on whether or not to implement it. This will allow us to understand the practical issues associated with the scheme and its effectiveness in encouraging engagement.

1.27. More details on the initial thoughts we have had on how the scheme might work are set out in chapter 10 in Part B of this document.

Market review

1.28. If, following consultation, the RMR package is introduced, we would monitor on an ongoing basis its direct impact on consumer engagement and track the impact that this engagement has on competition in the market. This will enable us to monitor how suppliers and consumers respond to our RMR remedies. A set of the market indicators we propose to use in this monitoring is set out in annex 8 in the supplementary appendices to this document.

1.29. In line with best regulatory practice, we are committed to conducting and publishing a more comprehensive review of the effects of our remedies at an appropriate time. If our reforms come into effect in summer next year, and assuming there is no clear reason to delay, we will review the package in full no later than 2017. We will conduct this review earlier if we consider our reforms are, for whatever reason, not having the expected effect. Importantly, this review will also enable us to consider whether amendments to the arrangements are needed to ensure consumers benefit from the government's smart meter programme.

1.30. Our ongoing monitoring of consumer engagement will not be limited to monitoring switching rates. Switching numbers can reflect a range of factors unrelated to the effectiveness of consumer engagement, such as the activity of sales agents or price differentials between suppliers' offers. Moreover, our 2012 tracking survey[11] shows that 28 per cent of gas customers who switched to save money[12] and 27 per cent of equivalent electricity customers are not confident they saved money. Where consumers switch to poorer deals it may not contribute to increasing the competitive pressure on suppliers.

1.31. The OFT[13] has noted three requirements for consumer engagement, which include characteristics beyond consumers following through with a switch of supplier.

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[11] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[12] 28 per cent of gas customers who said they switched to save money; and 27 per cent of electricity customers who said they switched to save money – Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[13] OFT 2010, ―What does behavioural economics mean for competition policy?, p.15-16

According to this framework, engagement requires consumers to be able and have an incentive to:

- **Access** relevant market information;
- **Assess** the offers available to choose what is best, as well as,
- **Act** on their assessment of the information.

1.32. We think that in the energy market, where most consumers are on evergreen tariffs and are rarely, if ever, required to consider alternative providers, effective engagement also requires consumers first to be **Aware** that they could find a better deal if they take the trouble to shop around. Our RMR package focuses on ensuring that consumers are aware of choices, and *able to* access information, assess alternatives and act. We will look to monitor this on an ongoing basis, and to track the impact our measures have on different customer groups. We are not primarily looking to address the *incentive* consumers have to engage in the market to the extent that this is driven by factors such as consumers' sensitivity to prices and brand loyalty. However, we do think that lack of trust and perceptions of complexity are factors which strongly disincentivise consumers from shopping around even if they have information on the other deals on offer. We have looked to address this as part of our package of proposals and will monitor the effectiveness of our proposals in improving consumers' trust and confidence.

Vulnerable consumers

1.33. Early in the RMR process we asked an open question about whether we should do more to advance the interests of vulnerable consumers, reflecting our analysis that vulnerable consumers are over-represented amongst sticky customers. Consultation respondents said that we should concentrate on getting the core proposals right for all consumers and then consider whether more needs to be done for those who are vulnerable.

1.34. We consider that the package set out in this document should particularly benefit vulnerable consumers. They are most likely to be discouraged from engaging in the market by a lack of trust and confidence which our proposals seek to address. Our package will allow vulnerable consumers, who may be amongst the least confident in changing supplier, to gain regular and personalised information about their supplier's cheapest deal. And our proposal to explore the Market Cheapest Deal idea is specifically targeted at providing personalised market wide information to vulnerable consumers. Finally, our proposal to introduce binding standards of conduct should ensure fair treatment even for those consumers who choose not to engage in the market.

1.35. Where possible, we will design our enhanced monitoring work to track the direct impact of our proposals on vulnerable as well as other customer groups.

1.36. Beyond our intention to do further work on the Market Cheapest Deal scheme, and to track the impact on vulnerable consumers, the package does not make any specific proposals relating to vulnerable consumers. Instead, further work will be undertaken beyond the boundaries of the RMR as part of the Consumer Vulnerability Strategy.

Related work

Collective switching, TPIs, Confidence Code

1.37. Our overall aim of improving consumer engagement in the energy market will also be supported by improving consumer access to, and confidence in, the intermediaries that help customers to switch. Our research and findings more generally from the Big Switch[14] suggest that many consumers need to be given assistance in comparing deals and switching tariffs if they are to be encouraged to engage. Therefore we are making a commitment to launch a parallel piece of work to help facilitate collective switching, to adopt the Confidence Code (which governs the switching sites) and to ensure that consumers have access to, and can have confidence in, Third Party Intermediaries (TPIs).

1.38. In the first half of next year we will publish an issues paper on the regulatory framework and the activities of TPIs. We will use this publication to help us assess whether the current regulatory framework remains fit-for-purpose given the various, and evolving, roles and activities of TPIs. It will consider current issues such as Ofgem's stewardship of the Confidence Code, and future issues such as the potential for new types of intermediation services associated with smart meter or smart grid deployment. We will also use the document to consider the specific issue of whether current regulation provides an appropriate framework for collective switching services.

Liquidity

1.39. Effective wholesale energy markets are important to ensuring effective competition in the retail market. We have concerns that the wholesale electricity market is not currently providing the products and price signals that independent suppliers need to compete effectively. Ofgem's liquidity project seeks to address these concerns.

1.40. In our February 2012 consultation document, we set out our liquidity objectives and launched a road-test on our proposals for a Mandatory Auction, through which the incumbent suppliers would be required to sell 25 percent of their generation volume. Since February, we have continued to monitor the wholesale market to track progress towards our objectives. We have also continued to develop our options for intervention, taking into account feedback from stakeholders. Based

[14] The Big Switch was a collective switching initiative in May 2012. Similar initiatives have subsequently taken place.

on this work, we will provide an update on the next steps on the liquidity project before the end of the year.

Smarter markets

1.41. By the end of the decade, the government's aim is that all domestic consumers should have smart gas and electricity meters. This roll-out can transform the consumer experience of retail energy markets. Consumers will have ready access to data on their consumption that can help them to make informed choices about how they buy and use energy. Smart metering can also enable improvements to customer service, facilitate new entry and provide opportunities for innovation in business models and products.

1.42. Positive engagement from consumers will be critical to realising the benefits of smart metering. However, our analysis shows that many consumers find today's market difficult to navigate and some are disengaged altogether. Our RMR proposals focus on addressing existing issues. By building trust and engagement today, our proposals will lay the foundation for a market with widespread deployment of smart metering.

1.43. Over time, arrangements designed to help consumers engage in today's market may need to adapt to the opportunities and risks that the roll-out presents. Ofgem is committed to playing a leading role in helping to deliver the changes to existing market arrangements that will be necessary to support market development from the platform of smart metering. We recently published an initial programme of work setting out how key reforms should be developed, together with Ofgem's role in securing these reforms[15]. This programme included work to put in place regulatory arrangements that empower and protect consumers to participate effectively in smarter retail energy markets.

Way forward

1.44. We are consulting on the proposals in this document until 21 December 2012 and will take responses into account in designing our final proposals. Subject to issues raised in response to our consultation document, we envisage publishing final proposals and statutory licence consultation in spring 2013, allowing the requisite 56 days for challenge before implementation.

Further research

1.45. In parallel with this consultation we will undertake further work to assess the impact some of our proposals have on effective consumer engagement. In particular, ahead of reaching a final decision on the RMR package, we are looking to trial the effect of our improved Annual Statement. This statement includes prompts

[15] Ofgem, Promoting smarter energy markets: a work programme, July 2012.

to switch as well as information on the Supplier's Cheapest Deal, the Tariff Information Label and personalised information on projected annual energy costs. We will be looking to assess the impact the Annual Statement has on: consumers' awareness of alternative offers; their ability to access relevant information; assess offers; and their ability to act in terms of switching to alternative deals with their supplier or to a new supplier. This will also help us get a better understanding of the differential impact these interventions might have on more active and on more disengaged consumers. This should help us understand better the case for the Market Cheapest Deal scheme discussed above.

Implementation timescales

1.46. We anticipate our proposals could be implemented from summer 2013, on a phased basis, with certain elements of the package needing more time than others for associated systems changes and communication with customers to take place. We are seeking views on the potential implementation lead times for our package of proposals, and would welcome views from respondents to this consultation. Similarly, we believe suppliers should consider whether they are able to move ahead with any of these proposals ahead of potential implementation.

1.47. We expect suppliers to do all they can to ensure consumers are given clear information about any changes in the terms and conditions of their tariffs which are required in implementing our reforms. We are proposing to allow a longer lead time for implementation of our proposals that will require customers to have their contractual terms changed and/or transitioned onto alternative tariffs.

1.48. We propose the following implementation lead times:

- The day after the 56 day implementation period has elapsed ('**Day 1**') – the new licence conditions for our Standards of Conduct come into effect. New fixed term contracts that are signed on and from this date will have to comply with our rules. Whilst there would be a transitional period for existing fixed term contracts to comply with the rules on unilateral variation, suppliers would be required to comply with the autorollover and price protection during switching windows from this date, including in respect of contracts entered into before day 1;

- **Day 1 + 2 months** – the cap on live tariff numbers and associated simplification rules, new Price Increase Notification (PIN) letters proposals and end of contract letter proposals come into effect. All live tariffs must have a Tariff Comparison Rate (TCR) for inclusion on marketing materials and a Tariff Information Label (TIL);

- **Day 1 + 4 months** – new summary box on the bill and new style Annual Statement come into effect, including Supplier Cheapest Deal and personal projections messaging;

- **Day 1 + 6 months** – all evergreen consumers (except where derogated) will need to become subject[16] to one of the supplier's live tariffs, and the day by which all fixed term tariffs entered into before 'day 1' will need to comply with our rules on unilateral contract variations.

1.49. We would aim to start the trials of the Market Cheapest Deal initiative by the end of the 6 month period. An illustration of the proposed implementation timetable is set out in annex 9 of the supplementary appendices to this document.

Stakeholder events during the consultation period

1.50. We will hold a stakeholder seminar in later November/early December on our RMR proposals, giving interested parties the opportunity to express their views and discuss the proposals with us, the industry and consumer bodies.

1.51. Before our final proposals document, and commencing in late November this year we intend to engage further with the industry and consumer groups, and will convene:

- A further workshop on implementation issues associated with our RMR package.
- A roundtable discussion on the proposed tariff cap and associated rules, leading to more detailed implementation workshops.
- A roundtable discussion on establishing a trial of the Market Cheapest Deal initiative.

1.52. Please contact rmr@ofgem.gov.uk if you would like to receive details of our stakeholder seminar or participate in any of our workshops or roundtable discussion groups noted above.

Structure of this document

1.53. This document is split into two parts:

- Part A, comprised of chapters 1 to 3, explains why we think the retail energy market needs reform, the evidence we have for barriers to effective consumer engagement and how our proposals will address them. This part of the document explains how we have addressed the concerns raised to our previous proposals and discusses the alternatives we have considered.

[16] Suppliers would need to decide on the appropriate methods of achieving this, which could potentially include: bespoke marketing with a view to customers agreeing new contracts; variations to contractual terms to convert existing contracts into live tariffs; or ending existing contracts with the result that customers became subject to a deemed contract with identical terms to an appropriate live tariff.

- Part B, which from chapter 4 onwards describes in detail each of the 7 specific proposals we are putting forward. These chapters are designed to help respondents understand in detail what suppliers will need to do to comply with our proposals.

1.54. Alongside this document we are publishing 'Supplementary appendix to: The Retail Market Review – Updated domestic proposals', (Reference: 135a/12), which includes the appendices referred to in this document:

- Proposed templates – information improvements.
- Current voluntary Standards of Conduct.
- Recent consumer research.
- Addressing key concerns.
- Enhanced monitoring.
- Implementation timetable.

1.55. We are also publishing:

- 'The Retail Market Review: Draft Impact Assessment for the updated domestic proposals', (Reference: 135b/12).
- 'Draft domestic licence conditions for the Retail Market Review proposals', (Reference: 135c/12).

1.56. Finally, accompanying this document, we will be publishing:

- The reports setting out the findings of the recent consumer research we have undertaken.
- Reports to us from the large suppliers on what they have done in response to our last RMR document.

2. Why the market needs reform

Chapter Summary

This chapter summarises the key problems we see in the energy supply market, and provides the evidence we have collected that supports our views.

Question 1: Do you agree with our characterisation of the problems in the retail energy market?

Question 2: Do you agree with the findings of our evidence base?

Problem statement and the evidence base

2.1. Several respondents to our December document were not convinced that we had provided adequate evidence of barriers to consumer engagement or that we had sufficiently demonstrated how this engagement impacts on competition and the outcomes for consumers. In this chapter we set out the key evidence of the barriers to engagement which consumers face which we have gathered through extensive consumer research, including the key finding from research we have conducted since December.

2.2. We also provide an overview of the arguments we set out more fully in the Probe. In the Probe we argue that low consumer engagement combines and contributes towards other market features (such as the large customer base inherited by the incumbent suppliers and their vertical integration) to constrain the strength of competition and prevent the market from working as well as it could in serving the interests of consumers. This section does not provide a comprehensive review of competition in the market, but does provide updated figures for a range of market indicators.

2.3. In some cases the consumer harm arising from the lack of competition exacerbates the barriers to effective engagement in the market, thus creating a vicious circle which we aim to address through our RMR proposals.

Barriers to effective consumer engagement

2.4. We have found three key barriers to effective consumer engagement, as follows:

- A large number of tariffs, many of which have complex structures and discount arrangements. This makes the prospect of engaging in the market unattractive for many consumers, and means it is often difficult for consumers who do engage to choose the best deal for their circumstances;

- Gaps and lack of clarity in the information given by suppliers to consumers which means they are not prompted to engage or given the full set of information they need to assess options in the market, and

- Lack of trust and poor supplier conduct which further reduces the confidence of some customers to engage in the market and has contributed to the permanent disengagement of others.

2.5. Together, these barriers limit the competitive pressure that consumers can put on the energy suppliers through their engagement.

Complex tariffs

Problem

2.6. In our December 2011 consultation document we stated that since 2008 the number of tariffs on offer had increased by 70% to around 400 tariffs in 2011, albeit this only includes tariffs available on switching sites, and is thus an underestimate. Whilst some suppliers have taken steps this year to decrease the number of tariffs, and make them easier to understand, the total number has changed little since publication of the March 2011 RMR document. Using the same methodology, our current estimate is that the full suite of tariffs stands at 410.

2.7. However, in September 2012, we asked the suppliers to provide us with information on the number of tariffs they currently offered. This shows that using our definition of a tariff, as at the end of August 2012, there were around 900 tariffs in the market, including White Label offerings and those offered by small suppliers. We note that since this date, some suppliers have continued to reduce the number of tariffs they offer.

Evidence from our consumer research and analysis

2.8. A consistent message from our consumer research over recent years is that people find and/or perceive the number of tariffs to be too high and the structure of tariffs often too complicated to allow them to properly assess their options. There is a widespread perception that reviewing energy options is a time consuming and complicated process, which may not necessarily result in a long term and tangible financial saving. Therefore many choose not to engage, and those who do engage often lack confidence in their decision making. The evidence suggests complex tariffs limit consumers' effective engagement in the energy market in the following ways:

- **It puts off many consumers from searching for better tariffs in the first place**, especially if they also doubt whether switching will achieve a financial saving that outweighs the search costs involved (i.e. time and effort), and there are other competing priorities in their lives.[17]

- **It leads some consumers to abandon their search** if they do decide to shop around. For example, some participants of our Consumer First Panel[18] have described engaging to a point and then 'giving up' because it becomes too difficult (e.g. because they do not understand their energy options or what represents a better deal for their circumstances).[19]

- **It may result in an increased frequency of poor switching decisions** by consumers. Our most recent survey shows that around one in four of those who have switched with an expectation of saving money are not confident that they have saved money by switching: this accounts for 28% of those who switched gas supplier to save money, and 27% of equivalent electricity customers.[20]

- **It contributes to a lack of trust in suppliers and the industry**. Many consumers feel that suppliers are deliberately making it difficult for consumers to assess different tariff options[21]. This reinforces a widely held perception that energy suppliers are guilty of 'excess profit' making.[22] Furthermore, given that energy is not seen as a purchase from which consumers can easily 'opt out', many experience a sense of powerlessness at being subject to price rises, while not feeling they can easily 'shop around' to help reduce their costs.

2.9. Our 2008 consumer engagement survey showed that 70% of consumers agree the number of different tariffs is confusing[23]. While any individual consumer looking to assess their options may not be faced with the full array of tariffs available in the market (i.e. a consumer undertaking a manual search amongst a couple of suppliers will not see 900 tariffs for example), this large number has created the impression that this is a complex market which is difficult to engage in. Our analysis shows that currently, any individual customer looking to compare the market would be faced with 161 core tariff[24] choices from the incumbent suppliers, including White Labels but excluding small suppliers, if they paid by direct debit. Our proposal would reduce this number to 48, a reduction of around 70 per cent. Most of these suppliers

[17] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
[18] The Consumer First Panel is a deliberative forum comprising of approximately 100 consumers from around Great Britain who are chosen to be broadly representative of energy customers.
[19] Ibid
[20] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[21] Insight Exchange, Consumer research and collaborative engagement on the proposed Standards of Conduct – Domestic Customers, October 2012.
[22] Ibid and also http://www.ofgem.gov.uk/Sustainability/Cp/CF/Documents1/Ofgem%20Consumer%20First%20Panel%20Year%204.pdf
[23] For more information see the following link: http://www.ofgem.gov.uk/Sustainability/Cp/CF/Documents1/Customer_Engagement_Survey_FINAL1.pdf
[24] In this context, we are referring to non-time of use tariffs.

offer an individual consumer a choice of nine or more tariffs for electricity and eight or more tariffs for gas.

2.10. The complex structure of tariffs adds to this confusion. We have heard directly from consumers that a lack of standardisation in how tariffs and tariff information are presented is a cause for confusion as they are unable to establish whether they are comparing 'like with like', and are generally confused by the range of technical terms used[25]. Over the course of several years of Consumer First Panel discussions, many consumers who have attempted to engage in the market have said that they are confused by the number of components of energy tariffs such as standing charges, tiers, unit rates, discounts, cash back, termination fees, loyalty bonuses and bundled products. Similarly, in our qualitative research on tariff comparability models in October 2011[26] we found that in general consumers thought it should be easier for consumers to compare tariffs and identify the most suitable tariff for their circumstances.

2.11. While again there have been moves from some suppliers to address this, we still see a number of features which make it difficult for consumers to assess how much they would pay under a particular tariff, or make choices unnecessarily complex. These include, but are not necessarily limited to:

- Complex multi-tier unit rate tariff structures;
- Discounts expressed as percentages of the total bill, or percentage discounts combined with an absolute cap;
- Discount structures which vary across tariff type, meaning the consumer has to take this into account when choosing between tariffs.

2.12. While arguably price comparison and switching sites have the potential to help consumers make sense of these choices - and increasingly they are one of the most popular ways for more active consumers to research and make a switch[27] - we know they cannot be easily used and accessed by all consumers. Research shows that comparison websites are used most by those on direct debit, more affluent socio-economic groups, the 35-64 age group and, naturally, those with internet access[28]. Even some more active and engaged consumers find price comparison sites confusing and some are sceptical of their independence[29]. While switching sites can make the market more accessible, our research shows that very few consumers use

[25] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
[26] Tariff Comparability Models, Volume 1 and 2 - Consumer qualitative research findings, Creative Research, October 2011
[27] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[28] Ibid.
[29] Ipsos MORI, Consumer First Panel Year 4: Findings from first workshops (held in October and November 2011), January 2012.

these sites with around 17[30] per cent of switches[31] occurring through them. Moreover, around 5 million[32] homes in the country do not have internet access and access to switching sites will be difficult for these householders.

2.13. The OFT's 2010 survey[33] on customer attitudes to advertising of prices in different markets shows that complex pricing was found most notably in the markets for energy, mobile phone and media packages, with 71 per cent of those surveyed saying they had seen a price which was 'complicated or difficult to compare with other prices'. Of the consumers in the survey who said they had experienced a complex price, 43 per cent said they objected to this occurring in gas or electricity supply. More generally 75 per cent of consumers said they objected to complex prices in gas or electricity[34], and 61% said they found it difficult to choose a supplier. Of those customers that found it difficult to choose an energy supplier, 40% said the market was too confusing and complicated, 37% found it was difficult to choose because suppliers use different terms to describe the same thing, and more than one-fifth considered there were too many options.

2.14. Behavioural economics suggests that consumers have a tendency to exhibit a 'status quo bias', loss aversion and that they value their leisure time to a high degree[35]. Therefore, for many consumers, if they lack a clear incentive and trigger to engage (e.g. because of poor or unclear information about how they could personally benefit from engagement) and also face additional barriers associated with complexity, their likely default behaviour is to take no action[36]. Because of these consumer biases, the OFT[37] states that firms may have an incentive to increase search or switching costs, in order to deter them from engaging in the market.

Inadequate information

The problem

2.15. As set out in chapter 1, for consumers to be engaged in the market, they need to be **aware** that they could find a better deal if they went to the market, be able to **access** market information and **assess** alternative offers before they **act** to switch to the best deal for them (or decide they are on the optimum deal already). This suggests clear prompts to engage and easy access to key pieces of information are likely to be key enablers of engagement. In the energy market, many consumers rarely receive prompts to engage, especially if they are on an evergreen tariff which

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[30] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[31] In this context a 'switch' could mean a change of tariff or payment type.
[32] For more information, see: http://www.ons.gov.uk/ons/rel/rdit2/internet-access---households-and-individuals/2012/stb-internet-access--households-and-individuals--2012.html
[33] OFT, Advertising of Prices, December 2010, main report and annex N of the same.
[34] From a base that excluded those consumers who said they had experienced complex pricing.
[35] Ofgem, What can behavioural economics say about GB energy consumers? March 2011 http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Behavioural_Economics_GBenergy.pdf
[36] Ipsos MORI, Ofgem Consumer First Panel Year 4: Findings from first workshops (held in October and November 2011) January 2012 .
[37] OFT —What does behavioural economics mean for competition policy?, p 15-16, 2010.

requires no consumer action. Even when consumers are informed of price rises - which potentially presents a key trigger to engagement - the supplier rarely gives information on what the rise will mean for them in terms of their annual bill. Furthermore, percentage increases which are cited in isolation may not be easily understood by the individual consumer.

2.16. Whilst the Probe remedies improved the information given to consumers, more needs to be done to make this information more readily identifiable and useful. Information which is presented is often found to be confusing and difficult to understand, with the consumer rarely pointed to the most important information they need to engage.

Evidence from our consumer research and analysis

2.17. Semiotics and language experts commissioned by Ofgem concluded that a lack of standardised language across the energy industry further compounds the belief among consumers that the energy market is confusing. Their report states that in general terms communications from suppliers are not consumer-friendly, and consumers cannot be relied upon to automatically know the meaning of kWh, unit rate, standing charge, or any other energy-related terminology that is not part of their day-to-day vocabulary.[38] These findings are echoed in qualitative research with consumers carried out this year, in which many respondents were unsure or only had a limited understanding of how their energy bills were made up.[39]

2.18. Therefore many consumers - and particularly those in circumstances which make them vulnerable - are likely to face a barrier in not being able to easily engage with the information sent to them by their supplier. This is important, because findings from the Consumer First Panel earlier this year[40] suggest that information from suppliers has the potential to act as a 'trigger' for engagement. For example, receiving a high energy bill from their existing supplier or notification that a fixed term contract would be coming to an end were identified as potential triggers. If these kinds of communications are not easily understood then they present a missed opportunity for prompting engagement. This highlights the importance of there being regular and effective prompts to engage, with user-friendly simple language and presentation.

2.19. The same research[41] shows that all but the most disengaged consumers are aware that, following an initial trigger or prompt to engage, a consumer requires a whole suite of information to help them review their energy options. This includes

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[38] Lawes Consulting & Lawes Gadsby Semiotics; Retail Market Review – energy bills, annual statements and price rise notification advice on layout and the use of language; A research report for Ofgem; November 2011.
http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Lawes_Language_Report.pdf

[39] SPA Future Thinking, Price Increase Notification Letters, Summary Box on Bills, Tariff Information Labels and Annual Statements, Report of consumer testing to support template development, forthcoming.

[40] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.

[41] Ibid.

information on: the cost and features of their current tariff; their energy consumption; details of alternative tariffs; and other information which will help them decide which tariff is best for their circumstances, and ultimately whether a switch is worth their while. It concludes that consumers need to have access to clear information that enables them to make accurate decisions about their energy options at each stage of this 'customer journey'. It also concludes that currently consumers are not necessarily aware of, or may not trust, what information and support is already on offer, and may 'give up' at any point if processing the available information becomes overwhelming[42]. This view was echoed in our March 2011 Consumer First Panel in which less engaged panellists thought there was insufficient information and support available to help them choose suppliers and tariffs[43].

2.20. Survey research also shows that key customer communications from suppliers are not having the desired impact. In our latest customer engagement survey[44], over half of consumers (52 per cent) either believed they had not received, or were not sure if they had received, information from their supplier about the name of the tariff they are on in the last year. An even greater proportion (56 per cent) either didn't know if they had received, or believed they hadn't received (within the last year), information from their supplier about the forecast cost of their energy consumption over the coming year.

2.21. In the same survey, for those consumers who had not switched in the last year, 28 per cent said they did not know they could switch. The same indicator shows a more acute lack of awareness in potentially vulnerable consumers, as 41 per cent of those in social grade DE, who had not switched in the last year, were unaware they could do so. Again from this survey, for those consumers who say they have never switched, around 16 per cent did not know they could. This indicator reaches 33 per cent for the potentially more vulnerable, in social grade E.

2.22. Provision of improved information in isolation is unlikely to prompt all consumers to engage. We know a small minority of consumers do not open written documents such as bills at all, many consumers look only for the information that is directly and immediately relevant to them (e.g. how much is owed), and there are other challenges regarding consumers who are billed online (i.e. online bills are less likely to be opened than paper bills)[45].

2.23. It is important to note that different consumers are likely to face barriers to engagement to varying degrees, depending on their knowledge, skills, experience or circumstances. For example, our Consumer First Panel[46] asked Panellists to discuss the steps they would take if they wanted to explore their energy options, and what

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[42] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
[43] Opinion Leader, Ofgem Consumer First Panel Year 3, Report from the second set of workshops, March 2011.
[44] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[45] Ipsos MORI, Prompting engagement with and retention of written customer communications, Final report prepared for Ofgem, October 2012.
[46] Ibid.

information they would require at each stage and from which sources. This showed that different types of consumers would react to information in different ways. However, those Panellists who were engaged with the market took an active interest in the energy market and had past experience of shopping around. Disengaged consumers who are apathetic towards the market said they would not be interested in receiving or using certain information. Others lacked the confidence or inclination to find this out themselves and preferred to make contact with their supplier and be told about their tariff details. Friends and family were also seen as useful sources of information and advice. This appeared to be especially true for older and some more vulnerable consumers.

2.24. However the evidence does suggest that many consumers think there is scope for key communications from suppliers to be improved: they want information to be short, succinct, easy to navigate, to avoid technical language and jargon, and to be personalised to them[47]. This will mean any prompts to engage (e.g. stating how much they could save by switching), or provision of information that will support them in reviewing their options (e.g. information on their current tariff), is more likely to be understood, considered personally relevant, and ultimately more effective in prompting and supporting engagement.

Lack of trust and poor supplier conduct

The problem

2.25. Even if consumers are prompted to engage and are given the information they need to access the market and assess options, they will not have an incentive to engage in the first place if they:

- Think all suppliers are the same: as mentioned above, among a broad cross-section of consumers there is a widely held belief that all energy suppliers are engaged in 'excess profit' making, and think there is little to differentiate them in terms of price and customer service.[48]

- Do not trust the information suppliers provide them with (in marketing or other activities), and therefore suspect they may be misled into buying a product that is not an improvement on their current one, or that a mistake may be made if they move to another offering, leaving them worse off.

2.26. We are concerned that problems with misselling and the generally poor reputation of the industry could have a significant impact on consumers' trust in suppliers and their confidence and incentives to engage. A 2009 survey commissioned for Consumer Focus showed that consumers have the least confidence

[47] SPA Future Thinking, Price Increase Notification Letters, Summary Box on Bills, Tariff Information Labels and Annual Statements, Report of consumer testing to support template development, forthcoming.
[48] Insight Exchange, Consumer research and collaborative engagement on the proposed Standards of Conduct – Domestic Customers, October 2012.

in gas and electricity companies across all the market sectors surveyed[49]. Again, we have seen a number of suppliers looking to rebuild consumers' trust and this is a welcome step. However, research conducted this year shows that it will take time to rebuild this trust and that a lack of trust is still having an impact on consumer engagement.

Evidence from our consumer research and analysis

2.27. Only about one-third of consumers say they trust energy suppliers to be open and transparent with their customers, and just 6% of consumers say they completely trust them.[50] Our most recent piece of qualitative research exploring trust found the overall perception of the energy industry is fairly negative and rarely rises above neutral.

2.28. As mentioned above, the broad evidence base suggests there are a number of potential drivers of mistrust including a view that suppliers are making 'excess profits' from selling an essential service, a belief that suppliers deliberately make it difficult for consumers to 'shop around', direct experiences and/or word of mouth accounts of poor switching decisions, and experiences of bad customer service or poor supplier conduct.

2.29. Qualitative research suggests that vulnerable customers are likely to be particularly mistrustful of some aspects of supplier practice - such as interactions with sales representatives. They are also fearful of processes such as the switching process going wrong, e.g. leading to double billing[51], although this concern also extends to many other customers too.[52].

2.30. Many consumers do not have frequent interactions with their energy supplier, but when they do, our research suggests that consumers want to be able to contact suppliers easily and inexpensively, have their issue dealt with efficiently, and be treated decently (i.e. treated with empathy and as an individual). At the moment the industry is inconsistent in meeting these expectations. In the research we commissioned to look at consumer reactions to the concept of mandatory standards of conduct, we found good and bad consumer experiences reported across all the large suppliers, and overall more were bad than good[53].

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[49] Ipsos MORI, Report on the 2009 Consumer Conditions Survey Market research survey conducted for Consumer Focus, March/April 2009.
[50] This compares to about two in five (39 per cent) who distrust suppliers, and 26 per cent who are neutral. Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[51] For more information see the following link: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Ofgem_vulnerable_customers_research_Final.pdf
[52] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012
[53] Insight Exchange, Consumer research and collaborative engagement on the proposed Standards of Conduct – Domestic Customers, October 2012.

2.31. More positively, a number of consumers feel that the treatment of consumers has improved since the phasing out of doorstep selling.[54] Also some research suggests poor experience of an existing supplier can in fact be a trigger to engagement and switching for some consumers[55]. However, if those poor experiences are combined with a belief that no other supplier will be able to offer a better alternative, then it is evident how this could reinforce mistrust and engender a sense of powerlessness.

Impact on competition

2.32. The barriers to effective engagement discussed above have detrimental impacts on competition. We see a large majority of 'sticky' customers, some of whom have disengaged completely from the market, which means that the incumbent suppliers still retain a high proportion of the customers which they inherited at privatisation, and even those that may have switched in the past are disinclined to do so again. This means that:

- The incumbent suppliers have relatively stable market shares which exacerbates the poor liquidity in the wholesale market and undermines the ability of new entrants to compete, and

- Incumbent suppliers are able to segment their customer base and respond to competition by recovering costs and margins from sticky customers.

2.33. Thus while 'churn' or switching rates may be equivalent to those seen in other markets, and may appear comparatively healthy compared to switching in energy markets in other countries, the levels of engagement we experience at the moment are not sufficient to support effective competition.

A large 'sticky' customer base

2.34. Our most recent 2012 customer engagement tracking survey showed that nearly two thirds of consumers (63 per cent of gas customers, and 65 per cent of electricity customers) claim they have never switched. We acknowledge that people's ability to recollect past events is imperfect, and our analysis of trends over time suggests the tendency to under-report previous switching behaviour is increasing[56]. Therefore the actual proportion of those who have 'never switched' is almost certainly smaller than this. Nevertheless it does suggest that a majority of consumers perceive themselves to have been largely inactive in the market.

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[54] Ibid.
[55] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
[56] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.

2.35. The same survey suggests that although most that don't change tariffs are aware it is possible to do so, awareness is poorest among those groups often considered more 'vulnerable' including less affluent socio-economic groups, BME[57] ethnic groups, those in rented accommodation, those with no internet access and those on standard credit payment terms or prepayment meters.

2.36. One of the main reasons cited for never switching supplier, continues to be that consumers are 'happy with their current supplier' (78 per cent of consumers who claim they have never switched supplier). At face value, this suggests that many sticky consumers are happy to remain so. However, our qualitative consumer research has also shown that:

- Some sticky consumers assume incorrectly that their supplier has already put them on the most appropriate tariff;
- Many have very little interest in energy and few interactions with their supplier which suggests they are 'happy not to think about it', rather than happy with their supplier in a more active sense, and
- They are also likely to cite other broader reasons for a lack of engagement[58].

2.37. We are concerned that the proportion of passive customers is growing. Since 2008, the number of customers switching both gas and electricity has been in decline. This is shown in figures published by DECC on domestic electricity and gas transfers in Great Britain[59]. Similarly our consumer engagement tracking survey also shows that switching is in decline. The most recent survey, conducted in March 2012, shows that just 13 per cent of gas customers and 14 per cent of electricity customers switched their supplier during 2011; this compares with 20 per cent (gas customers) and 19 per cent (electricity customers) in 2007.

2.38. A main driver of this decline in switching rates may have arisen from the reduction in outbound sales activity over the last few years and the recent cessation across the incumbent suppliers. Our April 2012 tracking survey[60] shows that there has been a year on year decline in the proportion of consumers who say they switched having used a doorstep salesperson of eight percentage points for gas and seven percentage points for electricity.

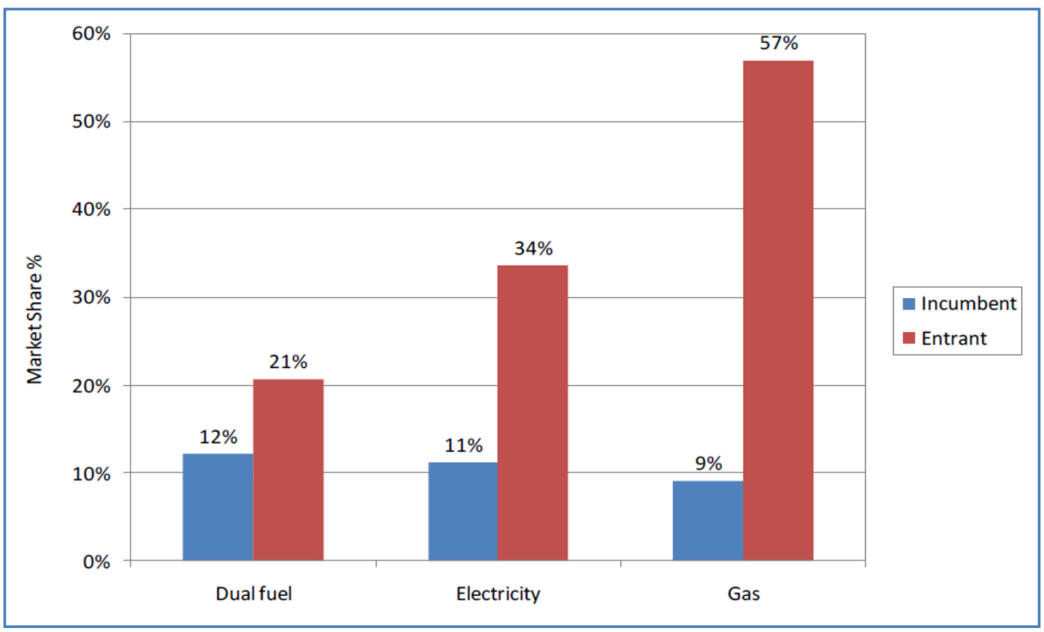
2.39. Through both our Consumer First Panel and our vulnerable consumer research in 2011 it was apparent that only a small proportion had switched on a proactive

[57] BME stands for Black and Minority Ethnic groups.
[58] Including lack of trust of suppliers, status quo bias (e.g. 'better the devil you know'), limited capacity to engage ('I don't have time'), sense of powerlessness as prices rise, loss aversion ('what if it [switching] goes wrong?'), complexity ('it's all too difficult'), difficult/inconsistent language ('I don't understand it'). Low literacy and numeracy skills, no access to the internet and debt issues may also present additional barriers, especially among vulnerable customers.
[59] Please see the following link: www.decc.gov.uk/assets/decc/statistics/source/prices/qep271.xls
[60] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.

basis, with the remainder switching after being approached by sales agents, or 'inheriting' a supplier when they moved home. Indeed we have evidence from our January 2011 tracking survey that consumers who may be vulnerable[61] are more likely to say they have never switched[62].

2.40. As shown in figure 1 below, the proportion of customers switching supplier is markedly different between the incumbent and new entrant suppliers. Electricity customers of new entrant suppliers switch at three times the rate of the incumbents' customers and gas customers of new entrant suppliers switch over six times the rate of the incumbent's customers. This further suggests a proportion of active customers who regularly shop around and take up offers by new entrants - our most recent tracking survey[63] shows that there has been a year on year increase in the proportion of consumers who say they have switched four or more times (this is true of both electricity and gas) - with others tending to remain with the incumbent supplier. This combined with our survey response that 63 per cent for gas and 65 per cent of electricity customers say they have never switched demonstrates that there is a significant cadre of sticky customers.

Figure 1 - Annualised churn of regional incumbent(s) and of regional entrants, by type of account, March to August 2010

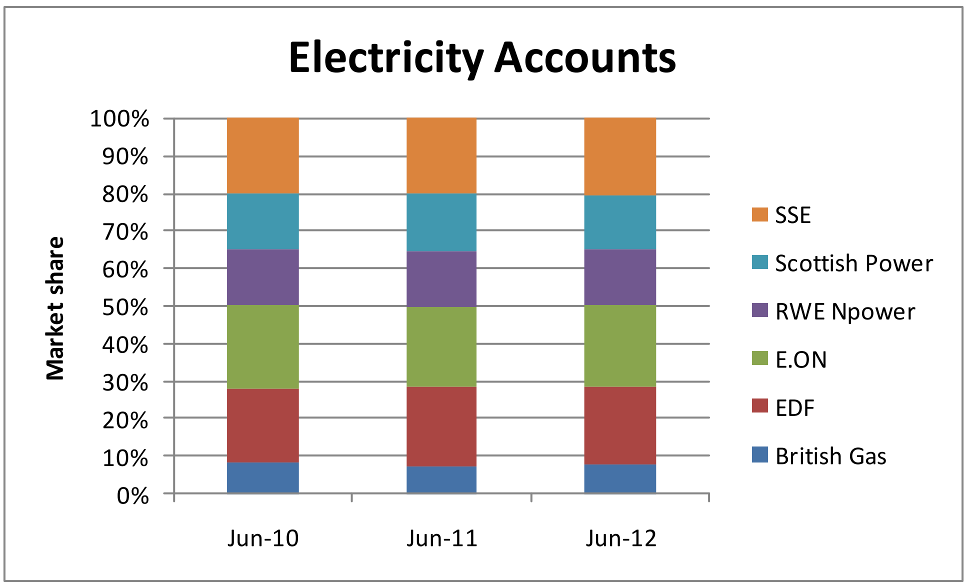


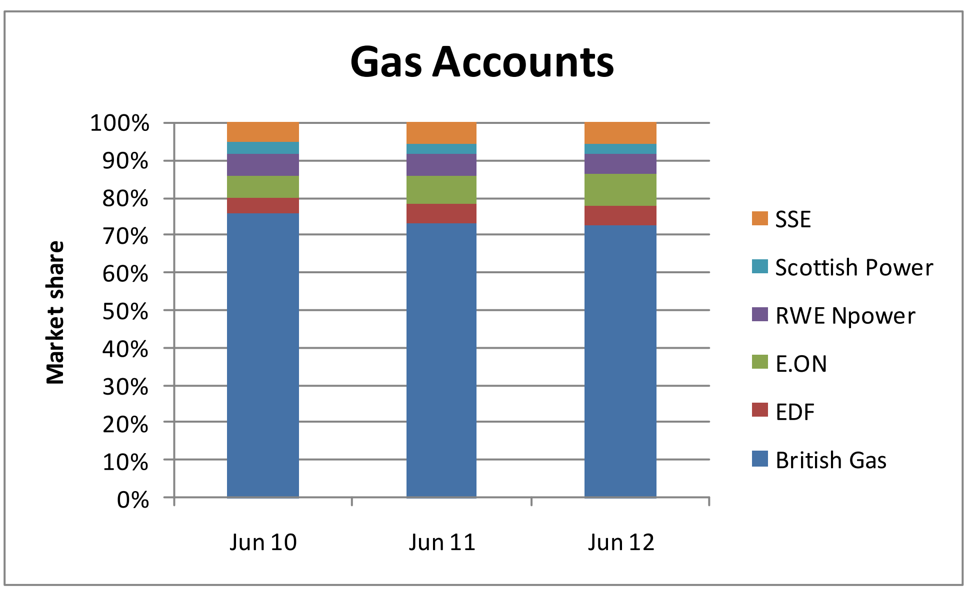
[61] Standard credit and pre-payment customers, the 15 to 34s, social groups D and E, those in rented accommodation, in rural areas and with non internet.
[62] Our 2012 customer engagement tracking survey shows a similar trend.
[63] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.

Stable market shares and liquidity

2.41. The opening of the energy retail market to competition gave significant market share to six large incumbents, which when combined account for more than 98% of the market. All of the incumbent suppliers have a legacy customer base created by transitioning from monopoly provision of energy to competitive provision. Whilst switching and churn statistics imply that market share can be won and lost, our analysis on the number of customer accounts shows that the net effect of this does not amount to any material change in suppliers' market share. In the period between June 2010 and June 2012 there was very little change in market share as shown below in figure 2.

Figure 2 – GB domestic market time series – electricity and gas accounts, June 2010 to June 2012

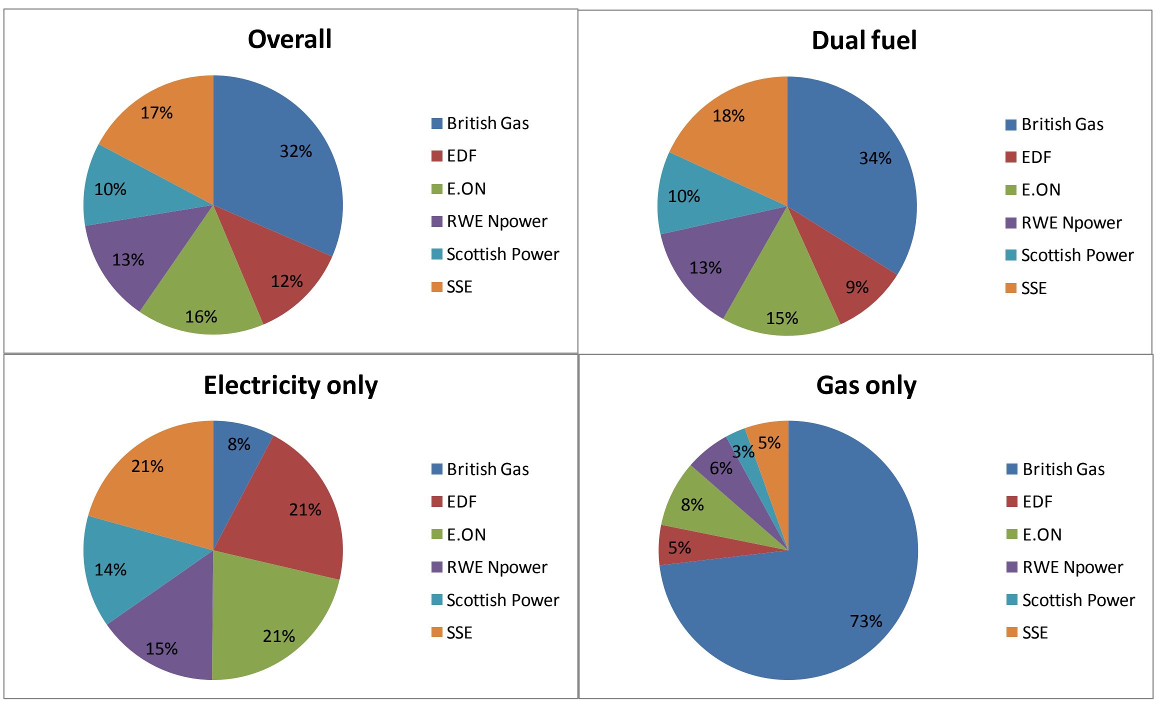




2.42. Breaking this picture down into more detail, figure 3 shows that British Gas retains a significant share of the domestic single fuel gas only market, accounting, as of June 2012 for 73% of customer accounts – contributing significantly to the market being 'highly concentrated' using OFT metrics[64]. British Gas also accounts for 34% of the dual fuel market, giving it significant market share in a sector that is fractionally below the 'highly concentrated' definition, and considered to be 'concentrated'. There is more diversity of market share in electricity across GB, although this still falls into the 'concentrated' definition used by the OFT. However, this significantly reflects the regional structure of the market before privatisation.

2.43. At a regional level, the predominance of the incumbent gas and electricity suppliers remains striking, with an average of more than 70% of all gas and electricity single fuel accounts supplied by either British Gas or the regional electricity incumbent.

Figure 3 – GB domestic market shares for different market sectors, June 2012



2.44. In addition to a broad picture of market concentration, all of the incumbent suppliers are vertically integrated (VI) across the supply chain, albeit to differing

[64] The Hirschmann-Herfindahl Index (HHI) is a measure of concentration ranging from 0 to 10,000, calculated as the sum of the square of company market shares. In its merger assessment guidelines, the OFT considers an HHI below 1,000 represents a market that is unconcentrated, between 1,000 and 2,000 as concentrated and above 2,000 as highly concentrated. The HHI for gas is 5,464, for dual fuel it is 2,072 and for electricity it is 1,814.

extents. Because of the stable market share and the reasonably close balance the suppliers maintain between wholesale and retail, they do not need to trade in the wholesale market as much as if they were significantly unbalanced, which serves to reduce market liquidity.

2.45. The wholesale market is a key driver of competition in the retail market. In order to compete effectively, suppliers need access to a range of wholesale market products to enable them to minimise their energy costs and offer competitive prices to consumers.

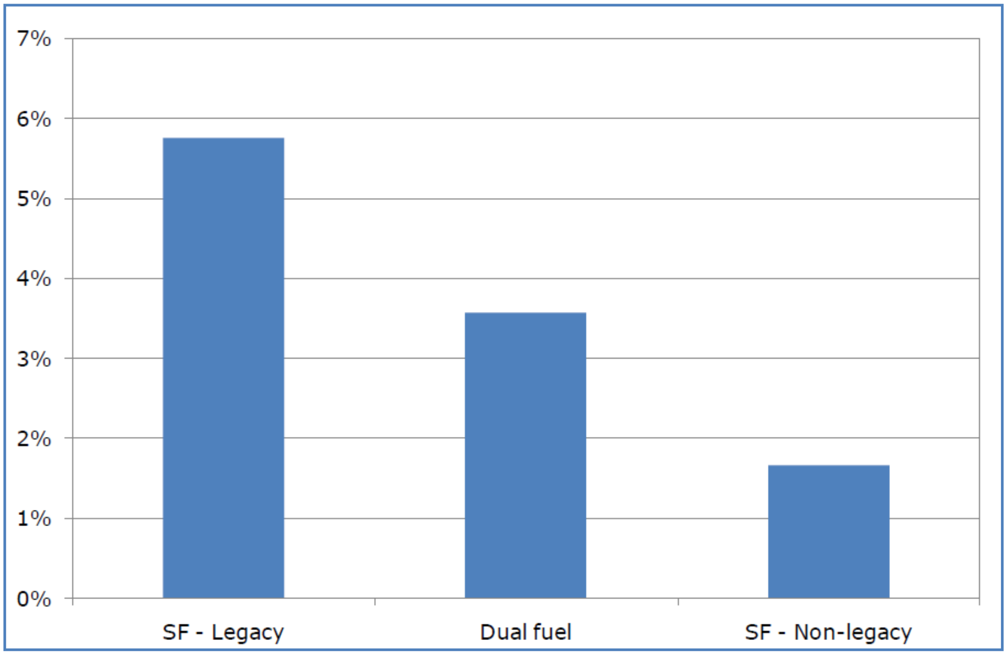
2.46. We are concerned that poor liquidity in the wholesale electricity market means that it is not currently providing the products that suppliers need, resulting in a barrier to entry and growth in the retail market. Poor liquidity is especially problematic for suppliers who are not vertically integrated – meaning they do not have an associated generation business that can ensure access to wholesale market products. Without these products, independent suppliers may not be able to offer the most competitive prices to consumers, making it difficult to enter and grow in the retail market. As a result, the incumbent suppliers are able to maintain their market share. Ofgem’s liquidity project aims to remove these barriers to ensure that the wholesale electricity market can support effective competition.

Market segmentation

2.47. As mentioned above, the incumbent suppliers have a significant inherited customer base, many of whom may be regarded as ‘sticky’ and less engaged in the market. The presence of sticky consumers in the domestic energy markets decreases the level of competition among suppliers. While it limits the scope for independent suppliers to attract new customers, it also allows the incumbent suppliers to segment their customer base. In this way they can make higher margins from sticky customers, or to pay little attention to customer service without fear of reprisal. This, combined with large stable market shares, confers a significant competitive advantage to the incumbents over other suppliers. This may result in consumer harm by insulating them from the pressure of competition from non-incumbent suppliers. Such an advantage is difficult for non-incumbents and small suppliers to compete with, meaning they are less able to match the prices offered by the incumbent suppliers to active consumers – the group of consumers most likely to switch.

2.48. Figure 4 below illustrates the difference in margin that may be earned from single fuel legacy customers (British Gas in the case of gas and the remainder of the incumbent suppliers in the case of electricity) versus dual fuel and single fuel non legacy customers (electricity in the case of British Gas and gas in the case of the rest of the incumbent suppliers). This in turn partly reflects the impact of selective online discounts, which reduce the margin earned by the supplier only for the active customers.

Figure 4 – Estimated margins on different products, 2010



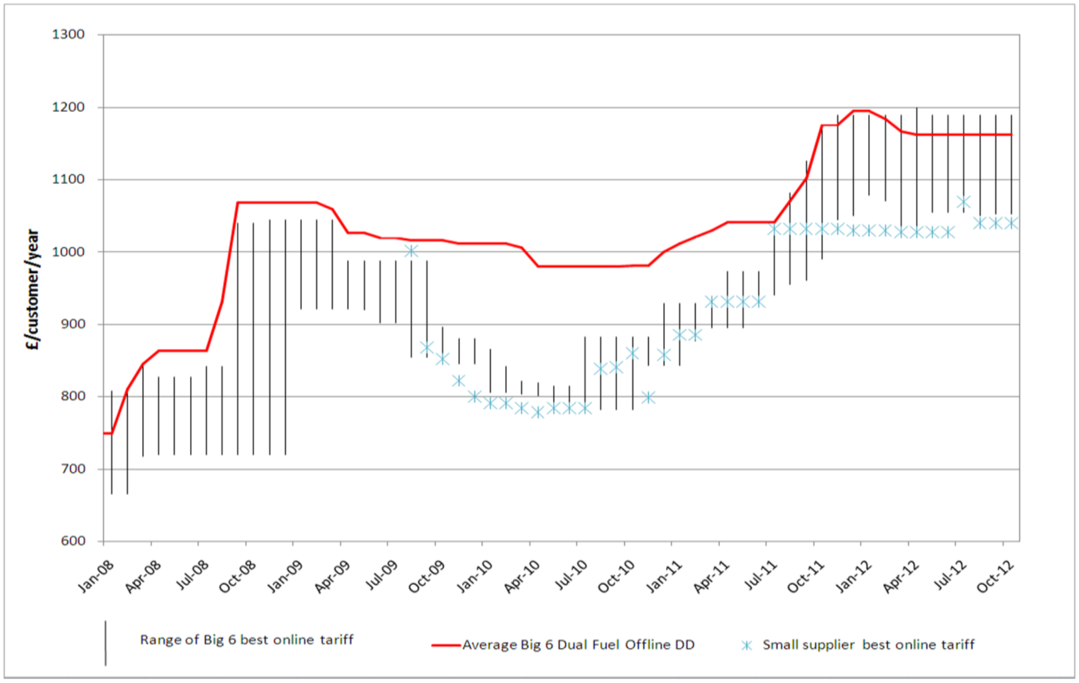
2.49. Whilst there may be reasons why this difference in profitability exists, we consider that one likely major explanation is the ability to leverage segmentation in the market with suppliers targeting the least price responsive with the less competitive offers in order to subsidise customer acquisition. The Probe findings showed that incumbent suppliers historically charged more to in-area consumers and less to out-of-area consumers[65]. We believe this is the case both from our evidence which shows there is a higher proportion of less engaged consumers on standard tariffs (which are typically amongst the worst value) and that stickiness gives suppliers a degree of market power. We also know from our 2012 tracking survey that the profile of those who say they have never switched is skewed towards those in less affluent socio-economic groups, including those who are state supported and rent their homes. The implication is that these customer types may be most likely to pay higher prices and be most profitable to suppliers.

2.50. A further area where segmentation is noticeable is in the market for online versus offline products. There is a significant number of introductory deals, bespoke products with tied in goods or services and a complex array of different discounts which, given their nature as being both complex and online, are likely to be targeted at the more engaged consumer. Over time the extent of the difference between the average dual fuel offline direct debit and the most competitive offers on the market has increased, before narrowing slightly more recently, as set out in figure 5 below. However, the range remains close to £150. We may therefore conclude that the

[65] Ofgem, Energy Supply Probe - Initial Findings Report, October 2008.

ability to leverage segmentation is a problem that continues, correlated with, albeit not necessarily explained by, the increase in the number of tariffs.

Figure 5 - Average dual fuel offline direct debit (DD) vs. best incumbent supplier and small supplier online deals



Outcomes for consumer

2.51. Insufficient competition means the market does not work as well as it could to serve consumer interests. In particular, we see:

- Similar business strategies which in particular mean that suppliers tend to put their prices up at similar times by similar amounts;
- Low priority being given to service and treatment of customers, and
- Little evidence of suppliers looking to reduce controllable costs.

2.52. Some of these market outcomes contribute to the barriers to consumer engagement. For example, many consumers tell us that one thing that puts them off looking for more competitive deals is the view that all suppliers are the same[66] and

[66] Insight Exchange, Consumer research and collaborative engagement on the proposed Standards of Conduct – Domestic Customers, October 2012.

that there is nothing to be gained from switching. Similarly, fear of poor treatment and distrust of the information provided by suppliers has dented the confidence of some consumers from engaging with the market.

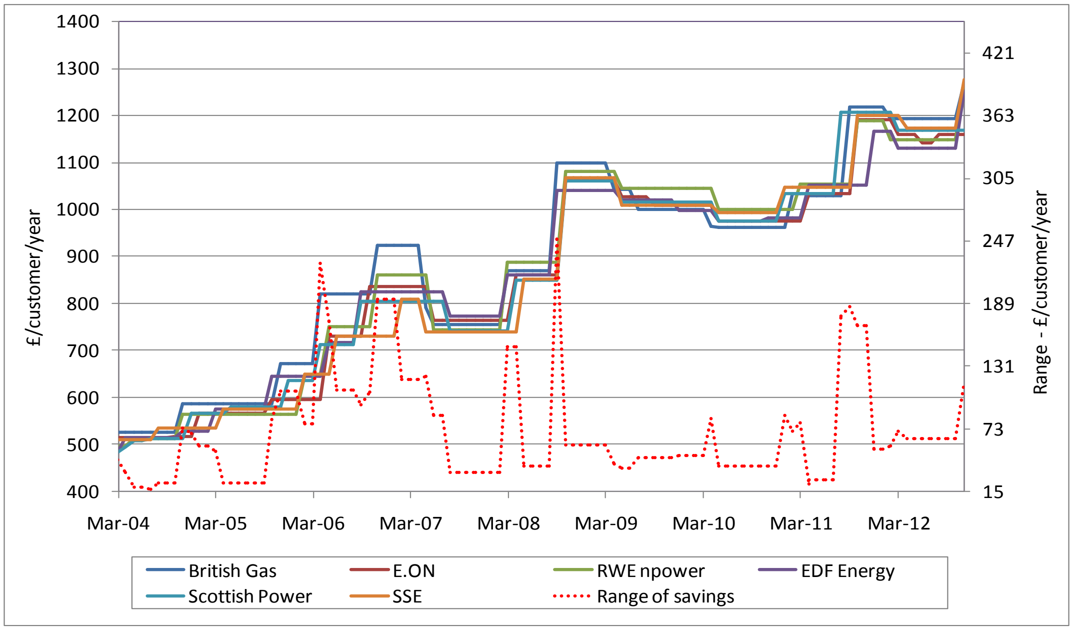
Similar business strategies

2.53. We have seen evidence of companies reducing the risk from competition through adopting similar pricing and hedging strategies, adding to consumers' perception that suppliers are 'all the same'. Many features of the energy retail markets could give rise to a higher risk of market outcomes that are highly responsive to other companies' actions. This is likely to lead to consumer harm by weakening the intensity of competition among suppliers and exacerbating consumers' feeling of helplessness cited in our research as prices often change at broadly the same time and by similar amounts.

2.54. Figure 6 below shows how closely suppliers continue to follow each other's prices. The red line on the diagram presents the 3-month rolling average of the range of prices. It shows that at the end of 2006, the price of an average, annual dual fuel bill offered by the incumbent supplier, varied by nearly £200 (using typical consumption figures). In the period to early 2009, the difference fell to less than £40 and remained there for the majority of 2009 and 2010. Following the price rise in March 2011 by the last incumbent supplier to raise prices in Winter 2010/11, the range between suppliers' prices fell to £22 in March 2011. The chart below shows data for March 2012, demonstrating the range of savings increased to £70. In November 2012 this figure will be around £115, accounting for recently announced price rises due to come into effect. However, the range in bills for those companies who have recently announced price increases will be £24[67].

[67] This excludes the recently announced price increase by ScottishPower as we do not have precise figures.

Figure 6 - Dual fuel, direct debit annual bills by supplier, March 2004 – October 2012



2.55. Price convergence to this degree is a sign that suppliers are reacting very strongly to decisions made by their competitors, rather than looking to compete directly with them to gain market share. The Probe examined in detail the basis for these price movements and the factors that suppliers take into account in their individual pricing decisions. Suppliers broadly wish to retain their existing customer numbers, in part because of the desire to retain a relatively balanced production and consumption portfolio. Consequently, pricing decisions by suppliers may be taken against the backdrop of independent decisions made by their rivals, with the first move on changing prices being responded to fairly rapidly by other suppliers. However, we should acknowledge that the above evidence pertains to dual fuel, direct debit products, which are more likely to be proportionately more represented by active consumers than the sticky.

2.56. We have also seen what appears to be loss minimisation strategies over the last few years, and know from suppliers' business plans collected as part of the Probe that they often wait for the regional incumbent to move first before planning their price moves so as to avoid negative publicity and to avoid being significantly out of kilter with the rest of the market.

2.57. We do not consider that such leader-follower behaviour is in consumers' interests and may reinforce consumers' view that suppliers are 'all the same', and the market consequently is not worth engaging in.

2.58. Given the desire for suppliers to remain at a comparable price level to regional incumbents and their direct rivals, we have concerns regarding suppliers' similar underlying cost structures which hinge on similar hedged positions and generation portfolios. These factors contribute to a lack of vigorous competition for more customers than their upstream assets can supply.

2.59. Taken together these factors contribute to there being a high risk of coordinated effects, which undermines effective competition and manifests itself as low pressure on companies to out-perform their rivals on price, quality of service, innovation or all these factors.

Low priority on meeting consumer needs

2.60. In a well functioning market, the threat of losing market share drives suppliers to consider what their customers want both in terms of products and services. We have seen little evidence that customers' actions are disciplining the activities of suppliers, and instead witness a number of misselling investigations, consumers complaining they do not trust their suppliers, concerns about confusing information being sent to them and little regard for the voluntary Standards of Conduct implemented during the Probe.

2.61. We acknowledge suppliers are now showing efforts to improve their behaviour towards their consumers and looking to rebuild trust, including through putting an end to doorstep selling. But this is being driven less by intense competition than by the attention that we and others are placing on these issues and the strong evidence that is emerging about consumers' lack of trust. It is worth repeating that the low attention suppliers have paid to the needs of consumers has resulted in behaviours which in themselves create barriers to consumer engagement.

Constraint on controllable costs

2.62. We have no evidence to suggest that suppliers have become more efficient over time or are seeking actively to minimise the procurement costs of wholesale energy, nor that they are under intense competitive pressure to pass any cost reductions onto consumers quickly.

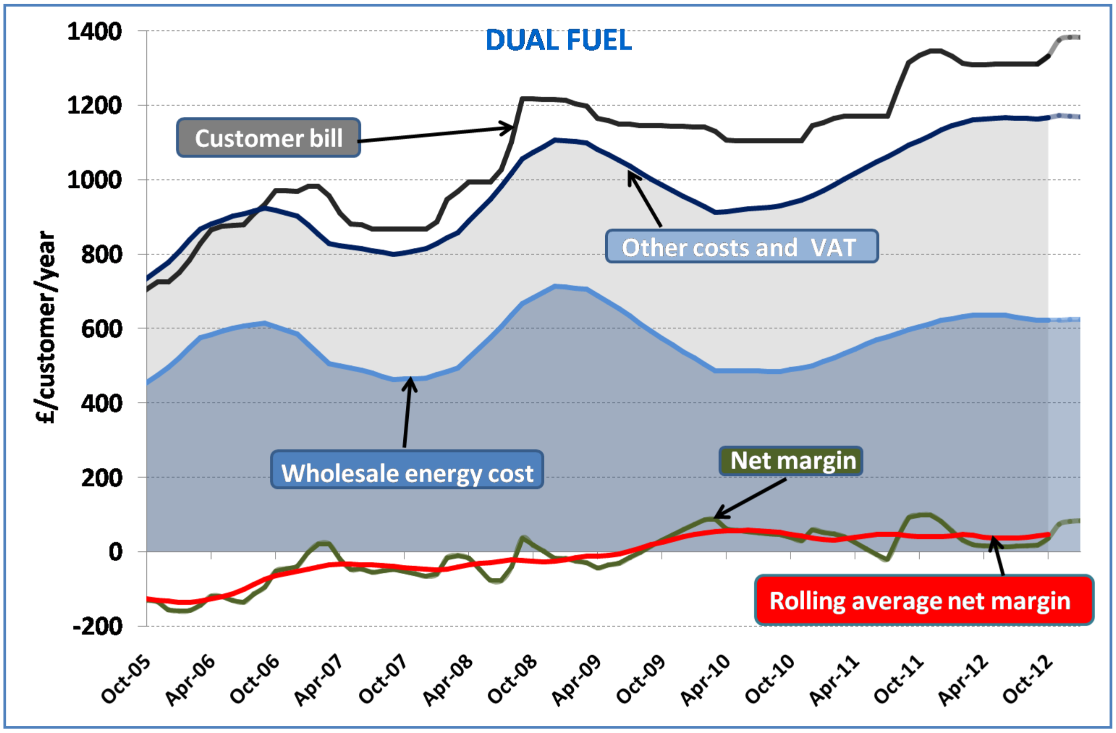
2.63. We have also observed a trend towards higher gas and dual fuel margins in recent years and changes in suppliers' retail price response to wholesale price movements (and potentially some evidence of asymmetry in response to changing prices).

2.64. Since the Probe, Ofgem has been monitoring suppliers' gas, electricity and dual fuel margins through the regular Supply Market Indicator (SMI) report[68]. In December 2010, following price increases by three of the incumbent suppliers, the report indicated our estimate of supply margins on a typical dual fuel domestic customer had risen to £90, just below the historic highs seen in early 2010. Since then, margins rose to record levels at the end of 2011 before falling back to around £35 at the end of October 2012. The figure below shows the current margin

[68] For more information see: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/smr/Pages/indicators.aspx

indicators and the trend over the last 7 years. Note that this trend of rising from a negative margin to an increasingly positive margin is more pronounced when looking at single fuel gas.

Figure 7 - Typical dual fuel customer bill, costs and total indicative net margin for the next 12 months

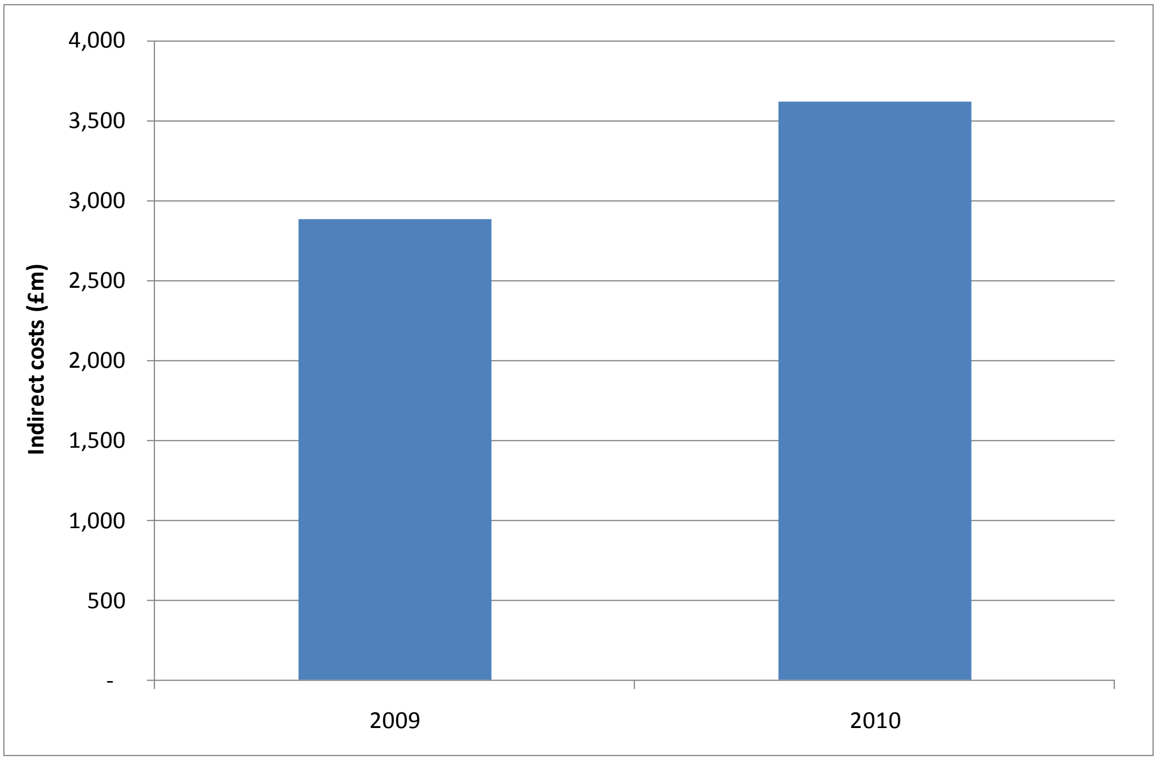


2.65. In addition, following measures introduced by Ofgem following the Energy Supply Probe, companies have been publishing separate accounts for their retail businesses as part of the Consolidated Segmental Statements[69]. These show aggregate retail margins in 2010 for domestic electricity were 0.3 per cent on average, and the equivalent figure for domestic gas was just below 6 per cent[70] - this compares with 2 per cent for domestic electricity and just below 0 per cent for domestic gas in 2009[71]. Although Ofgem has sought to ensure these accounts are presented, as far as possible, on a consistent basis, there is a limit to what can be achieved without recourse to operational or financial ring fencing of businesses. As Ofgem does not regulate end customer prices, we have not sought to establish whether or not the margins earned by supply businesses are reasonable.

[69] Please see the following link for further information: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Pages/rmr.aspx
[70] These figures use aggregate industry EBIT margins as set out in the Consolidated Segmental Statements: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/FIR_results_Final.pdf
[71] For more information see the following link: http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/RMR_Financial_Information_Report.pdf

2.66. In addition to the trend of higher indicative margins in recent years, there has been no evidence of a meaningful reduction in indirect costs[72], which have increased in recent years, potentially contrary to what one would expect in a competitive market. Figure 8 shows data from the Consolidated Segmental Statements demonstrating a significant increase in costs to the supply businesses as a whole on a year on year basis in the period of time for which we have data.

Figure 8 – total indirect costs for domestic GB energy supply in 2009 and 2010 (£m, nominal)[73]



2.67. Despite the above trend, we must expect that with a voluntary cessation of doorstep sales, suppliers' marketing costs will come down over time. In a competitive market this should in turn be passed on to consumers in the form of a reduction in prices.

[72] Indirect costs cover licensees' own internal operating costs including sales and marketing costs, bad debt, costs to serve, IT, staffing costs, billing and all meter costs.
[73] Defined as above.

3. Rationale for our package

Chapter Summary

This chapter sets out the reasons why we are proposing the package of RMR remedies in this document. It describes how we have incorporated feedback and findings since our December 2011 document in our updated proposals.

Question 1: Do you agree with our rationale for the proposed RMR package?

Question 2: What are your views on the proportionality of the proposed RMR package in the light of the evidence we have presented?

Question 3: Do you agree with our reasons for not proceeding with the alternative options set out below?

Introduction

3.1. In chapter 2 we set out the evidence that there are significant barriers to effective consumer engagement in the retail energy market. We also explained how this combines with and contributes to other features to weaken competition so that the market does not work as well as it could for consumers. The overall objective of our package of RMR proposals is to improve effective consumer engagement so there is stronger competitive pressure on supplier prices and other behaviour.

3.2. In this chapter we set out the overall rationale for the package of interventions we are proposing. We set out:

- A summary of the initiatives suppliers have taken in response to our December proposals;
- An overview of how our proposals have changed to address concerns raised in response to our December proposals;
- An overview of the benefits to consumers from this package;
- An assessment of how we expect consumers and suppliers to respond to the proposed package of RMR measures, and
- why we consider each of the measures in the package is needed to meet our objective of improving consumer engagement, and the alternatives we have considered.

3.3. More detail on the rationale for each intervention is set out in the associated chapter in Part B of this document. A detailed draft Impact Assessment of our proposals and how they compare with alternatives accompanies this document.

Supplier actions in response to our December proposals

3.4. In response to our December RMR proposals, a number of the incumbent suppliers have taken steps to improve their interactions with customers, simplify their tariff offerings and to rebuild trust. Some suppliers have introduced price comparison metrics and similar tools to make it easier for suppliers to compare tariffs. All incumbent suppliers have introduced new initiatives to engage consumers and all have taken steps to improve customer trust, including ceasing doorstep selling[74]. Some suppliers have redesigned bills to make them easier to understand and rationalised their tariffs and reduced the overall number.

3.5. Table 1 below sets out a summary of the key changes we have seen from suppliers. Alongside this document, we are publishing short documents produced by the 6 incumbent suppliers detailing the steps they have taken.

Table 1 – Summary of supplier initiatives in response to the RMR

Broad areas of concern	Steps taken by incumbent suppliers
Tariff complexity	• Four suppliers have reduced/simplified their tariff options. • Four suppliers have either eliminated or are phasing out two tier tariffs in favour of tariffs with a standing charge and a single unit rate. • Four suppliers have introduced a tariff price comparison tool, either through their website or on annual statements.
Informing and communicating with customers	• Four suppliers have included a more detailed breakdown of costs on their bills. • Four suppliers have changed their communication systems, with initiatives such as providing free phone or local rate contact numbers, offering alternate forms of communication (including a range of live chat/web based options) and training advisors in energy efficiency advice. • Four suppliers have begun to provide consumers with information on their cheapest tariff through price comparison tools or email communication – all six agreed to do this after the last review.

[74] To clarify, we refer to doorstep sales as meaning unsolicited sales activities at homes.

Broad areas of concern	Steps taken by incumbent suppliers
Improving trust	• Two suppliers have made all their tariffs open to all customers and available through all channels (telephone, internet, face to face). • Two suppliers have consolidated commitments into charters, whether this is to all customers or specific sets of customers – e.g. vulnerable customers. • Three suppliers have set up new mechanisms to understand consumer needs and/or gain consumer feedback.

3.6. We are encouraged by the supplier response to the concerns we have about the retail market, and we encourage suppliers to continue their work in this area ahead of the RMR arrangements coming into effect. However, we do not consider it appropriate for us to rely solely on these voluntary measures. Placing new, enforceable requirements on suppliers is vital to rebuild consumer confidence in engaging in the market, and this is clear from our consumer research. There is a role for consistency in approach to allow consumers to assess alternative offerings (for example in the application of the TCR and the introduction of Tariff Information Labels) and this will only be achieved through regulatory intervention. Further, more needs to be done, for example, to address the issues faced particularly by sticky and vulnerable consumers. We consider that the RMR package is vital to deliver enduring improvements across the market.

Key changes to our proposals since December

3.7. We have considered carefully the responses to our consultations, and have amended our policies to reflect issues raised and in the light of further consumer research and other analysis. The following sections describe the challenges that have been put to us by respondents to our March and December 2011 documents, and how we have responded to them in developing our updated proposals.

Tariff proposals

3.8. A number of consultation respondents doubted whether our December proposals would materially reduce the number of tariffs in the market as we were not planning to bring about restrictions in the fixed term market. We have moved away from our proposals to only limit standard tariffs, to a proposal that will cap the total amount of tariffs in the market, supported by a range of other rules aimed at preventing future tariff proliferation.

3.9. A number of respondents expressed concern about the effect our December proposals might have on innovation, particularly our proposals to limit companies to one standard tariff per payment type. Several small suppliers were concerned that a strict limit on the number of standard tariffs would inhibit their ability to compete with their rivals by providing niche products. In response, we have significantly lessened the restrictions enabling suppliers, including small suppliers, with freedom to innovate and compete, whilst making it simpler for consumers to assess the options for them in the market. We are consulting on whether we have got the balance right between simplifying choices and allowing room for innovation.

3.10. Several respondents noted that our proposal to ban discounts in the variable market would remove benefits (such as dual fuel discounts) that consumers value, which might have the effect of undermining the engagement we are looking to encourage. We have therefore reconsidered our policy in this area and have proposed to allow suppliers to offer dual fuel and payment method discounts to all tariffs, subject to a set of rules designed to simplify discount structures, without inhibiting innovation. Under our proposals, aside from dual fuel discounts, all other discounts would count towards the tariff cap. We believe this is a significant step towards addressing the complexity consumers face and have cited as a barrier to engagement.

3.11. Concern was expressed regarding our proposals to set the standing charge and/or regional adjuster to allow standard tariffs to be expressed in a single national unit rate. A number of respondents were concerned that our proposals would prevent suppliers from reflecting their fixed costs in the standing charge and would result in low or zero standing charge offers (which benefit low volume users) being removed from the market.

3.12. We are no longer proposing to set the standing charge to deliver an at a glance comparison of tariffs across the market, as we recognise and accept both the practical difficulties in implementing the policy as well as the risk of unintended consequences. Instead all consumers will be given personalised information on their estimated annual energy costs by their current supplier, using a prescribed methodology and as far as possible, suppliers will be required to use this methodology when selling to individual consumers. Finally, to address the particular challenges presented by the most sticky and vulnerable consumers, we propose to trial the Market Cheapest Deal scheme.

Standards of conduct

3.13. Respondents questioned whether it was appropriate for the SOCs to be legally binding. Over the summer we conducted further research on the SOCs and have been working closely with consumer groups to understand their expectations from suppliers in this area. This has revealed a lack of trust that suppliers would act on voluntary measures and that having the backstop of enforcement powers for failure to comply is favoured by consumers.

3.14. A number of respondents expressed concern that the nature of the SOCs as principles-based requirements means that there was greater risk of a difference of opinion between suppliers and Ofgem on the desired behaviours from suppliers and that this might increase the risk of enforcement action. Several respondents asked for greater clarity on the enforcement regime, and lobbied for either a two stage approach to enforcement and/or further guidance. We have considered our position on enforcement and have developed a bespoke approach, which we discuss in chapter 8 and which we consider addresses respondents' concerns. As part of this we are also planning to provide high level guidance in certain areas. We have also introduced a fairness objective into the drafting which we consider provides significant clarity on the context in which suppliers should seek to meet their obligations under the SOCs.

Supplier communications

3.15. Many suppliers did not support a prescribed and standardised set of customer communications, particularly for price increase notifications, as they considered it would impact on innovation and cost. Consumer research we carried out in April-May 2012[75] supports our earlier findings that personalised information in a standardised format is likely to[76] ensure communications effectively inform consumers of the impact of a price increase, and improve their understanding of how to manage it. We have, however, reduced the degree of prescription we are proposing for price increase notifications and have looked to minimise the space taken up by prescribed information on the front page of the bill.

3.16. A number of consultation respondents raised concerns about the cost of implementing the proposed improvements to supplier communications, particularly related to the cost of sending Annual Statements out separately to the bill. We received some indication of the cost from some suppliers but have not received further information since our consultation closed. So that we can take full account of the impacts of our policy in this area, we are keen for respondents to set out the details of the costs they would incur from these measures. We believe respondents will now be in a much better position to provide us with cost estimates as our proposals are fully developed. We will take our final decision having looked at the possible costs of our proposals in more detail.

3.17. A number of respondents suggested that rather than there being prescribed changes to the format and content of certain customer communications a wider review should be undertaken. We have established a working group with Energy UK, Consumer Focus, Which?, Citizens Advice and DECC to identify key objectives of consumer bills and other communications and to work through the detail of how to simplify the information presented to consumers. This work runs in parallel to our proposed changes via the RMR. We will consider the findings of this work ahead of making our final decision in this area of RMR policy.

Vulnerable consumers

3.18. Some respondents were concerned that our proposals (particularly our tariff proposals) might have a negative impact on vulnerable consumers. We have changed significantly our tariff proposals which are now based on limiting the number and complexity of tariffs rather than implementing a fixed standing charge.

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[75] SPA Future Thinking, Price Increase Notification Letters, Summary Box on Bills, Tariff Information Labels and Annual Statements, Report of consumer testing to support template development, forthcoming.
[76] Ipsos MORI, Consumer First Panel, Findings from Year 4, first workshop (published January 2012)

We have considered the potential for unintended consequences in our IA, and consider that the risk of vulnerable consumers being negatively affected is now lower. Furthermore we are looking at trialling the Market Cheapest Deal initiative with suppliers, specifically to make this market more accessible for vulnerable consumers. In parallel, further work on vulnerable consumers is being taken forward via Ofgem's Consumer Vulnerability Strategy.

Costs

3.19. A number of suppliers cited the risk with our RMR core tariff proposals in terms of one-off set up costs and associated ongoing costs, as well as other costs associated with the rest of the package. The costs estimated by suppliers differed from less than a million pounds to close to a hundred million pounds. Whilst we will provide our estimate of these costs in our final IA, some useful insights can be gained from recent supplier-led developments. Indeed our proposed tariff cap and associated rules for tariff features share elements of voluntary measures already introduced by some suppliers. We would therefore expect suppliers will be able to provide us with useful information on the costs they have experienced in rationalising their tariffs. We would be extremely interested to receive information on the costs of implementing and running our revised proposals from suppliers, and indeed other respondents, so that we can take this into consideration in our further policy development and, subsequently, final proposals.

Expected consumer benefits

3.20. We expect our proposals will have an overall positive effect in improving the ability of consumers to pick the best deal for them in the energy market and in widening the pool of consumers who are active in the market.

3.21. Our proposed measures for the Supplier Cheapest Deal, to require suppliers to include prompts to engage on all regular communications and to introduce the TCR as a common currency for use in all marketing materials are likely to impact positively in raising consumer awareness about the alternatives available in the energy market. We will also explore the Market Cheapest Deal initiative to address specific needs of vulnerable and disengaged consumers. Consumers would have better access to market information as a result of our proposals to facilitate the publication of best buy tables (using the TCR), introduce the Tariff Information Label, and to publish information on suppliers' comparative performance.

3.22. Consumers would face simpler choices when they are looking for alternative offers, as a consequence of our measures to reduce the number of tariffs and to introduce rules on the tariff and discount structures. The proposal to require suppliers to provide consumers with clearer information, including a personal projection of their annual energy costs on each bill, along with the Tariff Information Label and personalised information on the Supplier's Cheapest Deal will enable consumers to better assess the alternative offers available in the market.

3.23. Our proposals to introduce enforceable SOC and new rules on contract terms are likely to lead to consumers experiencing fairer treatment in all their interactions with suppliers. This, along with our tariff simplification proposals and the clear signposting to switching sites on key supplier communications, should mean that some currently disengaged consumers gain the confidence they need to look around for the best deal.

3.24. These proposals should mean that individual consumers are able to get a better deal in the market. More effective engagement should also have the effect of increasing competition so that the interests of consumers as a whole are better served by the market. Further, a number of our measures should reduce the scope for individual harm. For example, the rules on fixed term contracts will prevent consumers finding themselves on deals they did not sign up to, a range of our proposals should mean there is less scope for consumer harm arising from consumers unwittingly switching to tariffs which are more expensive for them and the Standards of Conduct should mean there is less individual harm arising from instances of poor supplier conduct.

Consumer and supplier response to our proposals

Consumer response

Improvements to consumer engagement

3.25. We are confident that the proposals in this document will make a significant improvement in effective consumer engagement, as defined in chapter 1, for a number of reasons.

3.26. Firstly, we have listened carefully to what consumers say they need in order to engage more effectively in this market (see the research cited in chapter 2) and have designed our proposals to meet these needs.

3.27. Consumers have told us they want fewer tariffs and less complex offerings, in our March 2011[77] and March 2012 Consumer First Panel[78] findings, Vulnerable Consumer Research (2011)[79] and our qualitative Tariff Comparability research in October 2011[80]. However, it is also clear that consumers value elements of choice (for example the ability to receive a discount for dual fuel contracts[81]) and our proposals are designed to strike a balance between simplicity and preserving what consumers currently value. In our 2012 communications testing research[82]and in

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[77] Opinion Leader, Ofgem Consumer First Panel Year 3, March 2011.
[78] Ipsos MORI, Consumer engagement with the energy market, information needs and perceptions of Ofgem, Findings from the Ofgem Consumer First Panel Year 4: second workshops (held in March 2012), October 2012.
[79] FDS International, Vulnerable Customer Research, March 2011.
[80] Creative Research, Tariff Comparability Models - Consumer qualitative research findings, October 2011.
[81] Ipsos MORI, Consumer reactions to varying tariff comparability models, Quantitative Research conducted for Ofgem, October 2011
[82] SPA Future Thinking, Options for cheapest tariff messaging on customer communications; Report of qualitative research, forthcoming, and SPA Future Thinking, Price Increase Notification Letters, Summary Box on Bills, Tariff Information Labels and Annual Statements, Report of consumer testing to support

several waves of Consumer First Panel events, consumers have also told us they want information provided to them to be clearer, more user friendly, free of jargon, and to adopt a degree of standardisation of language, format and content. They say they would also value clear messaging on the details of their tariff, their consumption and what other deals are available in the market. These preferences came through consistently in our March 2011, November-December 2011 and March 2012 Consumer First Panels.

3.28. Secondly, we have used expert advice in the design of our proposals so that they are most likely to have the desired effect. We sought input from expert advisers on linguistics, semiotics and information design on the current information that consumers receive, including what makes them open, read and retain documents, and have proposed improvements based on that advice.

3.29. Thirdly, as far as possible, we have looked to test our draft proposals with consumers and have reflected feedback from this research. We have tested our proposed improvements to regular customer communications through our work with SPA Future Thinking earlier this year and have included the findings in our proposals. Through Consumer First Panels, our work with Ipsos MORI on price comparison guides and tariff structures and our September 2012 research with SPA Future Thinking we have developed and tested the format of the TCR. We have amended our proposals to create a distinctly different purpose for the TCR and the personalised projection, acting on consumers' desire to have personalised information on their tariff options as well as a general prompt. In our work with SPA Future Thinking we also tested messaging on the Supplier's Cheapest Deal and took this into account as we developed our proposals.

3.30. We have tested our Standards of Conduct proposals through consumer research and collaborative sessions in our work with Insight Exchange in September 2012, and factored the key findings into our proposals, including our overarching fairness objective.

3.31. Finally, we have carefully considered the specific needs of the most sticky customers, those who are permanently disengaged.

Further work to assess the impact on consumer engagement

3.32. While we have tested our proposals with consumers, we have not yet been able to assess how powerful our new information, TCR, and Supplier Cheapest Deal proposals are in providing a prompt to consumers to engage. For this reason, ahead of our final decision on the RMR we intend to conduct field trials with large samples of consumers to understand how different groups respond to the information in the Annual Statement, and to understand any unintended consequences.

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template development, forthcoming.

3.33. We are interested to understand from this work the extent to which the Supplier Cheapest Deal initiative impacts on inter- and intra-supplier switching. We will also be interested to find out what impact this information has on active versus less engaged consumers. Information from this trial could be helpful in making the final decision on whether to go ahead with the trial of initiatives such as the Market Cheapest Deal scheme which are targeted at helping the stickiest customers to engage. Whilst the findings from this research will inform our final proposals, we need to consider the extent to which the results of the trial might underestimate the effectiveness of our full package of RMR proposals because of the short term nature of the trials, and the absence of other important features of our proposals (such as simpler tariffs and Standards of Conduct).

3.34. We are also considering whether we can test the impact of some of our other proposals using economic experiments in carefully designed and controlled laboratory conditions.

3.35. Finally, we will also have to trial the Market Cheapest Deal proposal before we can consider whether it is appropriate to introduce it (and how).

Mitigating adverse effects

3.36. We have considered what negative effects our proposals might have on consumer engagement or on consumers generally, and have thought about how we can mitigate this risk. The key risks we have considered are set out below. Further detail is contained in our draft Impact Assessment.

3.37. Providing consumers with information about a cheaper tariff that might not be available to them could be frustrating and reduce engagement. For example, the supplier’s cheapest tariff may be available only through a payment method that they do not have access to or may only be available online. This frustration could lead the consumer to further disengage from the energy market as they are not able to benefit from the savings that have been brought to their attention. We are addressing this issue in our Supplier Cheapest Deal and Market Cheapest Deal proposals by requiring information to be provided on the cheapest deals of the same payment type and of any payment type.

3.38. There is also a risk that this information simply encourages consumers to switch to another tariff with their current supplier, and not look further for better deals. This would limit the effectiveness of our proposals in improving competition although it may lead to fairer outcomes for individual consumers. We think that this risk is greatest with the vulnerable and most sticky customers who tend to be more risk averse. Our proposal to explore giving these customers information on the Market Cheapest Deal could address this risk, as could providing a range of other prompts to remind people that the best offers might be available from other suppliers.

3.39. We will use the field trial we mentioned above, from which we expect to have findings in early 2013, to understand the materiality of these risks and whether there are further ways of tailoring our proposals to make them more effective.

3.40. The combination of the TCR, the simplified tariffs and information provided on bills and annual statements may also result in consumers focusing on price, rather than non-price features of suppliers' offerings. However, our Tariff Information Label and the information we intend to publish on supplier performance on, for example, handling customer complaints is intended to mitigate this risk. Further, we are not proposing material restrictions to how suppliers promote the non-price benefits of their tariffs.

Supplier response

3.41. Our proposals should place additional competitive pressure in the market and our intention is that suppliers respond by considering how they can retain and attract engaged consumers through efficiencies and/or the quality of their service or products. We think that if more consumers are engaged and those who are engaged are more able to choose the best deal for them, this should allow suppliers who offer good price and service to grow market share. This should mean it is easier for new entrants who want to compete in this way to acquire customers, and this may be effective in attracting new entrants to the market. We also aim to reduce the ability of incumbent suppliers to respond to competition for a small proportion of active consumers simply by shifting costs onto a sticky customer base. We hope to achieve this through significantly widening the pool of more engaged customers and reducing the scope for market segmentation, for example through limiting tariff numbers and increasing consumer awareness of competitive offers.

3.42. Our objective is also that with the increase in customer churn and changes to suppliers' market share, the vertically integrated suppliers need to look more to the wholesale market to meet their upstream needs. This should improve wholesale liquidity and the scope for independent suppliers to enter and grow market share.

3.43. In designing these proposals we have thought carefully about the commercial strategies suppliers might take in response to our proposals and which might undermine the effectiveness of our policies. Full detail of our work in this area is set out in our draft Impact Assessment. An indication of the things we have considered and how we have looked to mitigate these risks are set out below.

3.44. We have recognised the scope for suppliers to reduce the effectiveness of the TCR in helping consumers access market information and have designed rules specifically to address risks in this area. For example, without rules, suppliers would have discretion over what costs and discounts they did and did not include to make their product look cheaper than others in the market, or might seek to make the TCR information difficult for consumers and those looking to publish best buy tables to find.

3.45. We also note the risk that if all that is published is the TCR based on medium consumption levels, there might be an incentive for suppliers to structure their tariffs to be low cost for medium user tariffs, but potentially high cost for customers at consumption levels slightly lower or higher than this level. Our proposal that TCRs are published for high, medium and low consumption categories reduces this risk.

3.46. There are a number of ways in which supplier action might undermine the policy intent of our proposals to limit tariff numbers. For example, they could look to make this a confusing market for consumers by withdrawing and adding new tariffs within the overall cap on a frequent basis. Partially for this reason, our rules on tariff numbers will require suppliers who withdraw an evergreen tariff from the market to transfer customers on that tariff onto their cheapest live tariff, and, if this entails an adverse change in prices or other terms, that they should issue a Price Increase Notification to affected customers.

3.47. In the same vein, suppliers could look to put complicated bundles or add on non-price features into the market to add confusion despite the limit on tariff numbers. For this reason we have proposed rules that any bundled product (for example boiler cover) or non-price options (for example loyalty points) must be available on all of their live tariffs. Any bundle not offered on all tariffs will represent a separate tariff within the cap.

3.48. There is a risk that with greater transparency and comparability of tariffs, suppliers respond by offering similar products and prices, leading to a reduction in choice and supplier differentiation across the market. We think that if we have been successful in improving consumer engagement, there should be a strong incentive for one or more supplier(s) to break away from this strategy in order to capture market share. While the market may lend itself towards coordinated effects, (see chapter 2) we think that independent suppliers (current or new) would have a strong incentive to disrupt this strategy.

3.49. Similarly, there is a risk that suppliers' response to our reforms is to put up prices for active (such as online) consumers, to avoid the loss of revenues which might come about if a high proportion of their customers switch to these deals on the back of information on the Supplier Cheapest Deal and other measures. While this may be a short term result of our reforms, we would not expect it to be long lived, absent collusion amongst suppliers. We would expect that if there were any gains to suppliers' from this approach they would be temporary given that our reforms should make it easier for active customers to shop around for better deals.

Proportionality of the package

3.50. As well as doing all we can to ensure our measures are designed to be effective in tackling the barriers to engagement we have identified, and specifically addressing the concerns that stakeholders have raised, we have been mindful of the need to ensure that the proposals are proportionate. This has involved considering whether:

- Less alternative, less intrusive measures would be effective, and

- All measures in the package are necessary or whether the package could be effective absent one or more of these proposed interventions.

Alternatives considered

3.51. As part of our process of coming to our updated proposals, we have considered and assessed whether there are alternative proposals that achieve the objectives of the RMR. Full detail on the alternative measures we have considered is included in our draft Impact Assessment published alongside this document. Key points include:

- We have already considered and rejected an alternative to the proposals on tariff simplification in this document, namely the December proposals discussed above. For the reasons already discussed, we consider that our new proposals are more proportionate and have less unintended consequences than our previous set.

- We have considered an alternative to the cap on tariff numbers which would instead place a 'principles based rule' on suppliers to prevent tariff proliferation. We have rejected this alternative because:

    - Regulatory risk – clear rules are easier for suppliers to act upon and design systems and processes around, as well as providing greater certainty to consumers that the complexity of the tariff offerings they face will reduce.

    - Uncertainty around whether it would be effective – previous experience in relation to the voluntary Standards of Conduct was not encouraging.

- We have considered a range of detailed alternatives to the rules around the calculation of TCRs (including whether they should be regional or national), in each case weighing up the relative balance of additional accuracy versus simplicity.

- We have tried a voluntary approach to SOC – we do not consider that the voluntary SOCs were acted upon by suppliers, and in that timeframe trust in energy companies has remained an issue[83]. It is clear that an enforceable approach is vital to rebuilding consumers' trust.

- Relying on a voluntary approach to Supplier Cheapest Deal – we see some voluntary measures in the market at present to give consumers information about their supplier's alternative tariff offerings. However, our proposals ensure consumers get regular and personalised

[83] Only about one-third of consumers say they trust energy suppliers to be open and transparent with their customers (just 6% of consumers say they completely trust them). This compares to about two in five (39%) who distrust suppliers, and 26% who are neutral. Ipsos MORI, Customer Engagement Tracking Survey, October 2012.

information about the cost savings available in a prescribed format which has been tested with consumers.

- Following the Probe, we tried an approach to improving the information given by suppliers to consumers that was flexible and non-prescriptive – this has not worked. It is clear from our consumer research customers want standardised, simpler, more user friendly information that contains the relevant information for them.

- We have considered alternative approaches to our narrow and wide messaging on Supplier Cheapest Deal but based on our consumer research[84] think that it is important for consumers to receive both tailored information on tariffs similar to their own as well as information on other options should consumers be willing to change their preferences. For example, in some circumstances prepayment consumers may want to move onto standard credit and vice versa, and should be able to find out easily whether it is in their interests to do so.

The extent of the package

3.52. We have given consideration to the scope of the package and whether we could remove any elements without there being a significant reduction in the effectiveness of the package. We set out below the reasons why we consider all of the RMR proposals are justified interventions and will work together and reinforce each other in meeting our objectives.

3.53. We have considered whether we need both a cap on tariff numbers and rules on tariff structure/discounts. We think that without some constraint on tariff numbers it will be difficult to rebuild trust and confidence, and for consumers to be able to feel confident of choosing the right tariff for them. Likewise we believe it is important to reduce consumers' confusion when comparing offerings by proposing that all tariffs have the same standing charge and unit rate structure. This objective will not be achieved through a cap on tariff numbers alone. Without both of these policies (limits on tariff numbers and rules on tariff structures and discounts) the effectiveness of other policies aimed at helping consumers access and assess market options, such as the TCR, the TIL and the personal projection would be less effective at engaging consumers.

3.54. We have considered relying on the Annual Statement and not putting any prompts, or other such information, on the bill, but this means that consumer information would be out of date quickly given its annual cycle, and consumers would be prompted to engage only infrequently. It is also clear that because the bill is the key communication that consumers read because it sets out what they owe, messages placed on it may be more likely to engage them. Our research shows that

[84] SPA Future Thinking, Options for cheapest tariff messaging on customer communications; Report of qualitative research, forthcoming.

many consumers would welcome information on how they can save money on a regular basis.

3.55. We cannot rely just on the cap on tariff numbers to rebuild trust. It is clear that consumers' concerns go beyond that to all types of engagement they have with their suppliers. Some consumers and particularly vulnerable consumers, as we found from our 2011 vulnerable consumer focus groups, are put off engaging in the market for fear of a bad experience. This is addressed by the binding Standards of Conduct. Similarly, our October 2012 research on what prompts consumers to open, read and retain information shows that consumers may question the motives of suppliers if they tell them they can save money. It is therefore important for the efficacy of our proposals to improve information that suppliers rebuild trust with their consumers via the Standards of Conduct.

3.56. Both the TCR and personal projection information are needed because consumers engage in different ways. Some consumers will be prompted by a best buy type table or by TCRs in the media or on websites, serving as a nudge for them to explore options in the market. Others will use the personal projection and gain market information by going straight to suppliers' or switching sites.

3.57. Consumers have told us that they would like more bespoke, personalised information on their tariff choices[85]. The only way at the moment of giving personalised information on savings is via the Supplier Cheapest Deal proposal. Without this information there will be a key prompt and key piece of missing information, which we believe will serve as an effective tool to increase consumers' engagement.

3.58. Were we not to have our proposals on fixed term tariff rules, consumers would continue to be reluctant to participate in the fixed term market for fear of finding themselves on a poor value deal at the end of the contract, or to have their terms and conditions changed without needing their consent. Both these factors may contribute to the lack of trust in the market and contribute to a fear of engaging.

3.59. Finally, and as discussed elsewhere, we think the effectiveness of our package could be constrained if we do not specifically address the engagement of the most sticky and vulnerable consumers. This is the purpose of our proposal to trial a Market Cheapest Deal scheme. We are concerned that new Standards of Conduct and the reduction in the number of tariffs may not be sufficient to build the confidence of these consumers, or that it could take many years before these measures and improved information have an effect on this customer group. As we have dropped our 'at a glance' proposals, and despite tariff simplification and other measures in our package, evidence and behavioural science suggests these consumers will need further prompts to engage. As we describe in chapter 2, vulnerable consumers are least aware of the options the market presents to them, they most fear and bear the greatest consequence of making a wrong switching

[85] SPA Future Thinking, Options for cheapest tariff messaging on customer communications; Report of qualitative research, forthcoming.

decision and they have made it clear they would need to understand the cost savings they could make if they are to engage.

3.60. The Market Cheapest Deal scheme is intended to address this issue. Without it or an alternative that achieves a similar aim, the RMR package will not be complete.

4. Tariff simplification

Chapter Summary

Consumers tell us they find energy tariffs too complex. This chapter sets out our proposals for making energy tariffs simpler, clearer and fairer.

Question 1: Are our rules to reduce the number of tariffs appropriate? Have we set the cap on core tariffs at the right level? Should a different cap be set for time of use tariffs? What derogations from our tariff cap would be appropriate?

Question 2: What surcharges should suppliers be able to offer without this counting as an additional core tariff, and why? How could these be defined in a licence?

Question 3: Are our rules to simplify tariff structures and discounts appropriate? Should they only apply to open tariffs or be extended to cover dead tariffs too?

Question 4: What categories of dead tariffs should be derogated from our proposals, if any? Are any other measures required to avoid any consumer harm?

Question 5: What would be the implementation issues and costs of our proposals?

Question 6: Is our proposed timeframe for implementation appropriate?

Introduction

4.1. In this chapter we describe the first of our initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so stronger competition places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices and to rebuild trust and confidence in those who are not engaged and encourage them to participate.

4.2. This chapter focuses on measures to reduce the number of tariffs and to make it simpler for consumers to understand suppliers' tariffs and to choose between them.

Our proposals

4.3. Our proposals have broadly three strands. Our measures aim to reduce the number of open tariffs, simplify the structure of open tariffs and eliminate expensive dead tariffs. These proposals, and what they imply for tariffs, are set out below.

Reducing the number of open tariffs – introducing a cap on 'core tariffs'

4.4. Unfettered tariff proliferation allows suppliers to segment the market and complicate consumers' tariff options. This can put people off engaging in the market in the first place or make it difficult for them to choose the best deal. Our intention is to reduce the number of options any individual consumer would face, and make it easier to assess different tariff offers by a) setting a cap on open 'core tariffs' and b) setting rules on tariff structures, discounts and bundles.

4.5. In the broadest sense, a tariff can be defined as a set of terms and conditions of the contract between the supplier and their customers. It follows that where there is any difference between the terms and conditions of two contracts (for example, the level of charges, and the services or option of services offered) they would be considered different tariffs.

4.6. To enable the implementation of our proposed cap we are introducing the concept of a 'core tariff'. Under our definition, a 'core tariff' refers to all of the terms and conditions of a contract with the following exceptions i) dual fuel discounts ii) appropriate surcharges[86] iii) adjustments to charges reflecting payment method, and iv) optional bundles (i.e. 'opt in' and 'opt out' bundles). We also propose that each core tariff would have a unique name. Apart from these exceptions, any difference between the terms and conditions of a contract would count as an additional core tariff.

4.7. For example, a tariff offered only to customers signing up online and that had a lower standing charge and / or unit rate compared to another tariff (not requiring an online sign up) would count as a separate core tariff.

4.8. We propose to set our cap so that suppliers can offer no more than four core gas and four core electricity tariffs to any individual customer. For this reason, we propose that suppliers can set up to four core tariffs per fuel for customers with non-time of use (ToU) meters (standard credit meters and pre-payment meters) and four core tariffs per fuel for each type of ToU meter (including E7, E10, DTS and smart meters) or smart meter mode for any particular location at any one time. For the avoidance of doubt, our limit of four core tariffs does not just apply to evergreen tariffs, and spans all types of tariffs a supplier might offer including evergreen and open fixed term[87] tariffs, deemed contract rates and suppliers' white label tariffs[88].

4.9. One additional core tariff would be permitted to a supplier if they needed it to participate in a collective switching scheme. We will ensure our rules on open and dead tariffs do not prevent this core tariff from being an evergreen tariff.

[86] For example, late payment charges, replacement bill charges, meter reconnection charges etc.
[87] For the avoidance of doubt, a supplier will not be able to extend the duration of an existing fixed term offer and suppliers may only offer customers coming to an end of a fixed term contract a tariff from their open core tariffs.
[88] A supplier may offer a tariff through a white label providers and this will not count as an additional tariff so long as all the terms and conditions (including tariff name) remain the same.

4.10. We will consider whether our limit should exclude preserved tariffs and legacy discounted tariffs[89] as well as any tariffs suppliers are obliged to offer for other reasons. We will consider whether it is appropriate to allow derogations for innovative ToU tariffs to facilitate the benefits of smart meters or for legacy ToU meters such as DTS meters or other tariffs where there is a strong case to do so.

4.11. In terms of rules for open tariffs, we propose that suppliers would need to offer at least one evergreen non-ToU tariff for each fuel. To facilitate appropriate rollover arrangements, we propose that where a supplier chooses to offer a fixed term tariff for a particular ToU meter they must also offer at least one evergreen tariff[90] for that meter type.

4.12. We propose that all evergreen tariffs (i.e. contracts that have no end date) will continue to be prohibited from being subject to termination fees and propose that they will have a maximum notice period of 28 days for termination (which may be given at anytime). To ensure that suppliers cannot avoid our rules on termination fees we propose to prohibit loyalty discounts from the evergreen market[91].

4.13. We also require that any tariff open to a new customer must be open to a supplier's existing customers and would be captured by the supplier's cheapest deal information requirements set out in chapter 5.

4.14. Regional variations in tariffs do not add to the complexity faced by any one consumer. A consequence of our rules on core tariffs is that regional variations are still possible[92]; for example, regional brand names, regional differences in charges, bespoke contracts for exceptionally high energy consumers, etc[93]. However, we intend to monitor the extent to which suppliers present different tariffs to different regions of GB and the differentials between them to ensure practice in this area does not undermine our overall RMR objective.

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[89] Under the Warm Home Discount suppliers are allowed to continue offering discounted tariffs as part of their overall legacy spending limit. This spending limit is decreasing each year until it ends in 2014. The main focus of the government's Warm Home Discount programme is to provide rebates to certain consumers on their bills. These rebates are not affected by our RMR proposals.

[90] As set out in the chapter on fixed term offers we will require customers coming to the end of a time of use fixed term tariff to default to the cheapest evergreen tariff of the same meter type (or in the case of smart meters the meter mode). Suppliers retain the right not to offer a tariff for a particular meter types or meter modes.

[91] To achieve this effect we envisage amending the existing definition of termination fees in licence conditions to cover something of value that would not be available to a domestic customer on the basis that they have terminated the contract before a particular period of time.

[92] The effect of our proposals would mean that regional variations are permitted provided the total number core tariffs (and therefore choices) available to customers in the relevant regions did not exceed the tariff cap. By way of example, if a supplier decided to offer a customer in a particular location with a bespoke core tariff, the supplier may have to ensure that some or all of the core tariffs available nationally were not available to that customer (or alternatively operate on the basis that the total number of national core tariffs is reduced by one).

[93] Such as non-commercial collective purchase.

Simplifying open tariffs

4.15. In order to reduce the scope for customer confusion and increase tariff comparability we propose that all tariffs must be of a standing charge and unit rate structure. For non-ToU tariffs there should be a single unit rate (multi rate tariffs are not permitted) that does not vary with the consumer's level of consumption. For ToU tariffs we propose that the unit rate could vary by the time of day or on different days of the week etc. but not by a consumer's level of consumption.

4.16. To help consumers compare tariffs we propose that each of a supplier's core tariffs per fuel must contain the same:

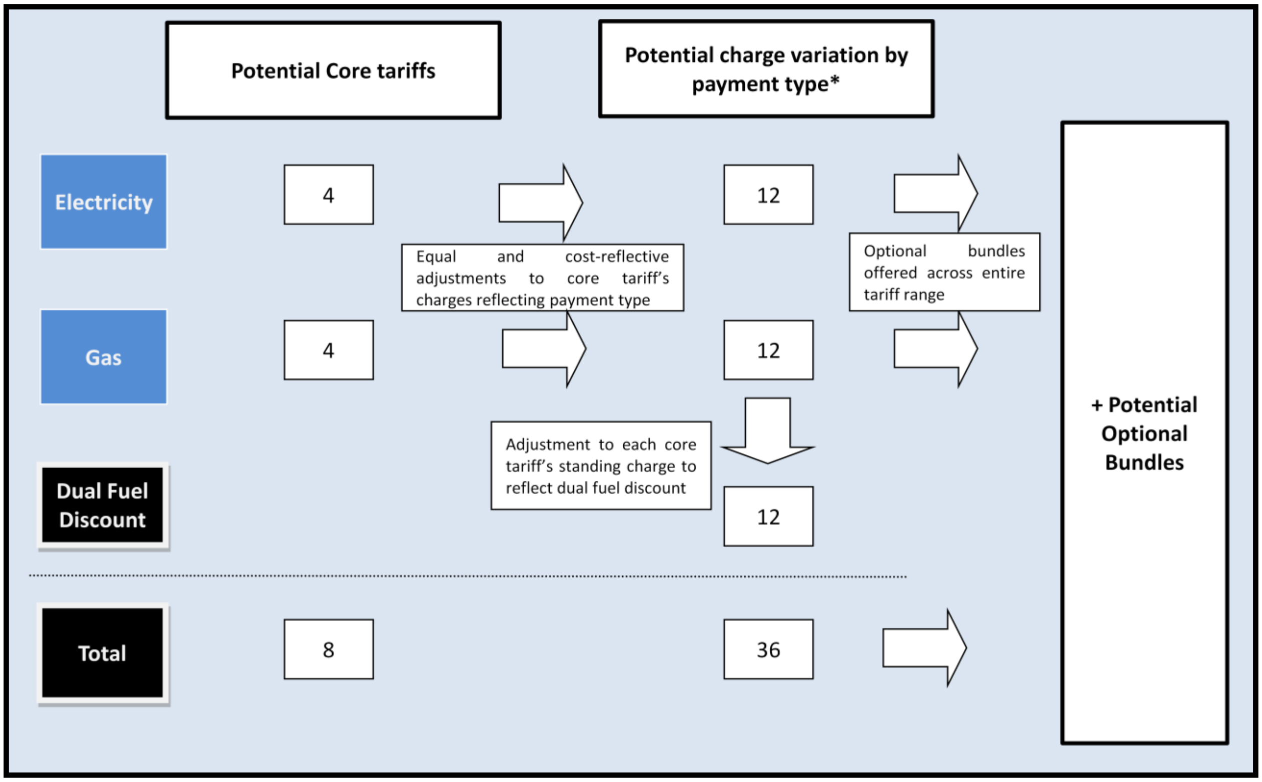
- discounts for taking dual fuel,
- surcharges (for example for repairing a meter or changing the location of a meter),
- adjustments to charges to account for different payment methods, and/or
- optional bundles.

4.17. We would also require that the method of calculating the charges for bundles and level of dual fuel discounts and surcharges must be the same across all of a supplier's tariffs and be the same across all regions.

4.18. We propose that adjustments to the standing charge or unit rate may be made to reflect differences in the cost of providing different payment methods. They must be the same across all of a supplier's tariffs and be the same across all regions. These adjustments cannot be presented as a percentage of the total bill, unit rate or standing charge. This will still allow, for example, lower charges to be provided to customers who pay by direct debit relative to standard credit[94]. However, the differentials between these payments must be the same across all of the supplier's core tariffs for gas or electricity.

[94] This will still allow a supplier to not offer some core tariffs to some customers. For example, a supplier may adjust the charges of its standard tariff depending on whether a customer pays by standard credit or prepayment, though this does not mean that that all of a supplier's tariffs must be made available to prepayment customers.

Figure 1 - Schematic of our tariff proposals (non-ToU tariffs, non-collective purchase[95])



**Assumes only three payment method variations*

Banning expensive dead tariffs

4.19. So called 'dead tariffs' (those evergreen tariffs that are no longer available to new customers) allow suppliers to segment the market, in some cases offer poor value for money and contribute to customer confusion since consumers would need to identify their own tariff for the purposes of comparison. Dead tariffs are particularly problematic if they do not have a contractual end date (evergreen) as consumers can find themselves on the tariff for a long period of time with no obvious prompt to check if they are on a good deal or not.

4.20. Whilst we would welcome comments on any particular legal constraints that apply to preserved tariffs, we propose that, where it would save them money, consumers on dead tariffs should be transferred to the supplier's[96] cheapest[97]

[95] We propose an additional core tariff for collective switches for both gas and electricity. If suppliers made use of this it could potentially increase the total core tariffs to 10 and core tariffs' variations in charges, after assumed adjustments by payment types, to 45.
[96] For the avoidance of doubt a supplier's tariffs include those tariffs of any related 'white label' provider and vice versa.
[97] Accounting for appropriate discounts.

evergreen tariff given their payment method, meter type and whether their access is offline[98]. We propose further that suppliers are required to provide an annual check of whether consumers on dead tariffs would be better off being transferred to their cheapest equivalent open evergreen tariff.

4.21. We also propose that suppliers be prohibited from introducing any new dead evergreen tariffs. In other words, if a supplier decides to withdraw an open tariff (within its limit of 4 core tariffs), consumers on that tariff will need to be transferred onto another open tariff.

Our reasoning

4.22. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate. We draw on our own evidence and analysis and evidence drawn from submissions and stakeholder engagement.

4.23. First, we define the problem. We describe the environment that should prevail for consumers, explain how the current environment falls short of that standard, and explain why these deficiencies are material. We then explain why our updated proposal is an appropriate and proportionate means of addressing the problem identified. We explain why regulatory action is a relevant consideration, and why we consider our proposal to be the most appropriate form of regulatory action in the circumstances, having regard to alternative courses of action.

The problem

4.24. Many consumers find it difficult to make sense of their options in the energy market. Whilst generally consumers value choice, many perceive there are too many tariffs and that they can be complex and off-putting.

4.25. Using our original approach to estimate the number of tariffs reveals that there are still approximately 400 open tariffs[99]. Since then we have sought information from suppliers and we have been able to more fully account for the array of payment methods, meter types and discounts suppliers offer. Using this more comprehensive data and a wider definition puts the number of open tariffs at around 900[100].

4.26. Tariff structures can have a number of components and discounts can be applied in different and complex ways. For example, over a third of the open non-

[98] An offline customer would need to be transferred to an offline tariff. An online customer would be transferred to the cheaper of an offline and online deal.
[99] Source: Ofgem analysis of data from TheEnergyShop.com, as at 16 October 2012.
[100] Source: Ofgem analysis of supplier tariff permutations as at 28 August 2012 using information available from our information request to suppliers. Across both large and small suppliers (including White Labels), meter types, and payment types. Numbers are based on London region.

ToU tariffs offered in the market have unit rates that that vary by the level of consumption (i.e. multi-rate tariffs).

4.27. Behavioural economics shows us that many consumers will switch off from making decisions if they believe their options are too many or too complex[101]. Unless consumers understand their options, and are able to assess the respective benefits relatively easily, they will be less likely to engage and less able to make an informed choice on which option to switch to.

4.28. The result is that consumer trust and engagement is less than it would otherwise be.

4.29. Large numbers of tariffs also allow suppliers to segment the market. Not only does this mean that some consumers pay significantly more than others, but it also further weakens competitive pressures by advantaging the previous incumbent supplier (since they have a significant number of sticky customers) over smaller suppliers and new entrants. The result is that the previous incumbent suppliers' cost increases can more easily be passed through to consumers and therefore these suppliers have less of an incentive to reduce their controllable costs.

Addressing the problem

4.30. Suppliers had the opportunity to tackle tariff complexity on a voluntary basis through the 2008 Energy Supply Probe[102]. Yet the problem has not abated and tariff numbers increased in the years following the Probe. Since our December 2011 consultation document some suppliers have made progress to help reduce confusion around tariffs and reduce the number of tariffs available. We consider that we need to take formal measures to lock in and build on these developments and ensure that actions are taken in a way that addresses consumer needs.

4.31. As discussed earlier, reducing the number of complex tariff offers in the market and allowing consumers to choose from a simplified set of tariffs will help consumers to assess their options. It should also help address some of the lack of trust and confidence as well as the perception that that the market is too complex which prevents some consumers from engaging.

4.32. We are proposing to reduce the complexity consumers experience by setting a cap on the number of core tariffs a supplier can offer and by setting rules to make tariffs easier to understand. Our proposals cover both the evergreen and fixed term market.

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[101] Source: Ofgem, March 2011. What can behavioural economics say about GB energy consumers? http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/Behavioural_Economics_GBenergy.pdf
[102] Through a Standards of Conduct that included 'an expectation that suppliers take all reasonable steps to not offer products that are unnecessarily complex and confusing.'

4.33. We recognise that consumers benefit from choice and innovation. Consequently, we are proposing to strike a balance between choice and complexity by setting our proposed cap to four core tariffs – a number similar to some of the voluntary measures that suppliers have adopted. To ensure that consumers can still benefit from the discounts and bundles they value, our proposals explicitly allow for these though ensure they are applied in a way that is simple and understandable. Our proposals still allow sufficient freedom for suppliers to offer the tariffs, bundles and discounts that consumers value, as well as allowing scope for innovation in ToU tariffs.

4.34. Whilst our proposals do not permit 'at a glance' tariff comparisons across the evergreen market, we believe the proposals outlined in this chapter improve on our December proposals. We consider that our updated proposals address important concerns raised by stakeholders (which are discussed elsewhere) while still achieving the core policy objectives of our previous consultation.

4.35. Our proposals on dead tariffs target another source of customer confusion and market segmentation and are intended, where possible, to eliminate dead tariffs where they are not in consumers' interests.

4.36. In coming to our proposals we have considered a range of options, such as introducing our simplification rules without the cap on the number of open core tariffs or a cap on the number of open core tariffs without simplifying tariff structures. The pros and cons of these options are set out in our Impact Assessment. Overall we think our proposal best achieves the simplification needed in the market.

Implementation

Implementation processes

4.37. We recognise that our proposals will need to be refined, for example through ensuring an appropriate range of surcharges is defined, that appropriate derogations are established and that our implementation timetable is appropriate. We welcome feedback on these, and other, areas.

4.38. Suppliers will need to undertake a range of actions to implement our proposals. For example they may have to amend the terms and conditions of dead tariffs and undertake a carefully managed process to transfer customers on tariffs which might be withdrawn to comply with the cap on tariff numbers onto new terms and conditions. We seek views on the tasks and the costs associated with implementing these proposals.

Timetable

4.39. We propose that suppliers are required to comply with the new tariff simplification rules set out in this chapter within two months of the acceptance of the RMR licence conditions.

4.40. In terms of the migration of customers currently on expensive dead tariffs to open tariffs we expect suppliers to assess which customers should be moved to the appropriate open tariff and to complete this migration within six months after the implementation date of the package of RMR proposals. We would expect suppliers to repeat this exercise annually to ensure that remaining dead tariffs remain good value for their customers.

5. Clearer and simpler information

Chapter Summary

This chapter sets out our updated proposals for the five key communications that consumers receive from their energy suppliers and our commitment to improve the transparency of information on supplier performance. We are proposing rules on the content, and in some cases both the prescribed format and the language of the content, of these key communications in order to ensure consumers get the information they require to engage effectively in the market and to make them simpler and clearer, and more consistent. We are proposing these steps because information has a material impact on consumers' inclination to engage in the market, and is critical to their ability to make appropriate choices.

Question 1: What are your comments on the degree of prescription proposed, and on the design of the documents and messaging?

Question 2: What are your views on the appropriateness of content requirements for each of the communication channels?

Question 3: Should Ofgem explore further ways in which suppliers might increase the effectiveness of online/paperless communications?

Question 4: Should Ofgem consider making further recommendations, or issuing best practice for enhancing the impact of Annual Statements by looking at messaging and co-branding of envelopes?

Question 5: Do you agree with the view additional contractual information can be included on an additional page on the Annual Statement?

Question 6: What are your views on the classification of duel fuel for the purposes of the template designs?

Question 7: What are your views regarding including energy efficiency advice in Annual Statements?

5.1. In this chapter we describe the second of seven initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so the threat of switching places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices. It also requires measures to rebuild trust and confidence among those that are not engaged and encourage them to participate.

5.2. This chapter focuses on the routine communications from an energy supplier to their customer. The particular communications we focus on are (a) the Bill, (b) the

Annual Statement, (c) the Price Increase Notice (PIN), (d) the Tariff Information Label, and (e) the End of Fixed Term notice. We also discuss our commitment to improve the flow of customer service information to consumers and our plans to increase the standardisation of language across communications.

5.3. Our overall objectives are to make these communications simpler and clearer and to ensure that:

- key communications contain effective prompts to engage;
- all information needed for consumers to make informed choices is provided to them; and
- all information and/or messaging is presented in a clear and accessible manner.

Our proposals

5.4. The eight component parts of our updated proposals for improvements to information provided to domestic consumers on key communications are set out below. Templates showing the prescribed element of each of our proposals are set out in appendix 4. In addition, supplier design implementation guidelines for each of the templates will be published alongside this consultation[103]. Before we finalise these templates we will consider them in the light of consultation responses and engagement with stakeholders.

5.5. These proposals apply both to consumers who receive communications in paper format and to those who manage their account online or receive paperless bills. Our document retention research[104] highlights that in comparison to paper documents, online documents are opened and read by a smaller proportion of consumers who receive them. We welcome stakeholders' views about ways in which the effectiveness of electronic communications can be improved.

Tariff Information Label

5.6. We propose to prescribe the format and the content of a standard Label to describe the key features of each tariff. A version of the Label would appear on annual statements. Suppliers would be required to publish the Label on their website in a position that can be easily accessed by the consumer. Suppliers would also be required to provide Labels to consumers on request and should take all reasonable steps to ensure that intermediaries provide Tariff Information Labels to consumers.

[103] Boag McCann (2012) 'Ofgem Information Improvements: Implementation Guidelines', October 2012
[104] Ipsos MORI (2012), 'Prompting engagement with and retention of written customer communications, Final report prepared for Ofgem', October 2012

Our current position, set out in draft domestic licence conditions[105] is that the label is to include the following information[106]:

- the key contractual terms applicable[107] to the tariff, including standing charges and unit rates[108];
- the tariff comparison rate (TCR) for each of the three consumption categories[109]. When it features on the Annual Statement, the TCR will be provided for the consumer's consumption category; and
- when it features on the Annual Statement, a personal projection of the consumer's annual spend on their current tariff.

5.7. Our proposal is that the Tariff Information Label will not be permitted to include any information other than that specified in the Licence condition.

Summary Box on Bills[110]

5.8. We propose to mandate the format and the content of the summary box for inclusion on every bill sent to domestic consumers so that it is distinctive and engaging. The summary box, split over the first and second pages of the bill, is intended to prompt engagement, and to provide the minimum information necessary for consumers to do so. Our current position, set out in the draft domestic licence conditions, is that the standard form is to include the following information[111]:

On page one: A box with a coloured border positioned on the right-hand side of the page, titled 'Paying more than you need to?', and containing the following:

- a personal projection of the consumer's annual spend on their current tariff;
- the cheapest tariff(s) available from their supplier along with associated messaging (see chapter 6); and

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[105] Draft domestic licence conditions.
[106] Please note that this is not a comprehensive list of the information or formatting – see draft domestic licence conditions for information requirements.
[107] However, we are also proposing to amend existing licence conditions to help clarify what terms constitute principal terms and ensure that such information is actually provided to consumers in plain and intelligible language before they enter into an energy supply contract. For full details see the proposed modifications to standard conditions 1 and 23 in the draft domestic licence conditions.
[108] We note that some consumers find standing charges and unit rates confusing. However, we consider that it is important for consumers to be informed of the key terms and conditions of a tariff when comparing options. The standing charge and unit rate are important features of a tariff.
[109] Based on the electricity/gas usage in the last 12 months consumers are classified as low, medium or large users.
[110] For the avoidance of doubt, any reference to 'bills' also includes statements of account (i.e. the communications commonly used for direct debit and pre-payment meter customers).
[111] Please note that this is not a comprehensive list of the information or formatting requirements. See the draft domestic licence conditions for full details.

- signposting to independent switching advice.

On page two: A box with a coloured border situated on the right-hand side of the page, titled 'About your tariff', and containing the following:

- personal consumption information and details of the consumer's current tariff[112]; and

- the TCR for the consumer's consumption band for their current tariff.

5.9. Our proposal is that the Summary Box will not be permitted to include any information other than that specified in the standardised form.

Annual Statement

5.10. We propose to prescribe the content and format of a new style Annual Statement to be sent to domestic consumers. We propose this is titled 'Your annual gas/electricity summary' and intend this to be a distinctive two-page document with bold headings, sent as an individual communication (i.e. not in conjunction with a bill or any other communication). We intend to prescribe the majority of the content and format of the document, with suppliers able to use company branding to head up the document, and to use their own colour schemes.

5.11. The Annual Statement has a clear purpose. It is intended to prompt quality engagement in the market by providing key information about energy use and its cost for a particular consumer. This can incentivise and equip consumers to engage in the market, making them comfortable and confident in assessing their options.

5.12. We intend this document to be kept for reference much like a P60 or an insurance certificate. Our document retention research[113] has suggested additional ways to enhance the impact of these statements by looking at the design and branding of the envelope. We welcome views about whether Ofgem should consider making further recommendations, or issuing best practice for enhancing the impact of Annual Statements by looking at messaging and co-branding of envelopes.

5.13. Our current position, as set out in the draft domestic licence conditions, is that the Annual Statement should include the following information[114]:

- a summary of the consumer's energy usage over the previous year;

- a personal projection of the consumer's annual spend on their current tariff;

[112] Two boxes, one for each fuel for dual fuel.
[113] Ipsos MORI (2012), 'Prompting engagement with and retention of written customer communications, Final report prepared for Ofgem', October 2012
[114] Please note that this is not a comprehensive list of the information or formatting requirements. For full details see the draft domestic licence conditions.

- information and messaging on the supplier's cheapest deal (see chapter 6);
- prompts to switch and signposting to impartial switching advice;
- a version of the Tariff Information Label for the consumer's current tariff, featuring the key contractual terms applicable to the consumer; and
- a glossary of terms used within the Annual Statement.

5.14. As with all of the communication channels, it is important the purpose of the communication remains clear. Therefore we are proposing only the information included in the draft Standard Licence Condition 31A[115] can be included in the Annual Statement.

5.15. However, we recognise all key contractual terms may not be able to be contained within page two of our Annual Statement, therefore our proposal is that any additional contractual terms should be included on a separate page to be sent alongside the standardised communication. We welcome views regarding a 'third page' for accommodating these terms, and whether this should be broadened to include any other relevant information related to the Annual Statement. For instance, whether energy efficiency information should also be included.

Price Increase Notice (PIN)

5.16. We propose to prescribe the format of certain elements of the information included on the notice provided to domestic consumers when their supplier is increasing its prices. The price increase notification as a communication is intended to inform consumers of what about their tariff has changed, how it will impact each consumer personally, and the steps they can take to manage the situation. Therefore, our current position, as set out in the draft domestic licence conditions, is that the following information must be included in two tables of a specified format on page one of the notice:

- a comparison of previous unit rates and standing charge, compared to the new rates;
- a personal projection of the consumer's annual spend on their current tariff at the old rates and new rates; and
- a comparison of the personal projections at the old and new rates.

[115] For full details see the draft domestic licence conditions.

5.17. To ensure consumers have the information required to make informed decisions, and the purpose of the PIN remains clear, we also propose to prescribe the content of the notice. This will include[116];

- a clear title to highlight that the letter is informing the customer of an increase in charges;
- personalised tariff details, including tariff name and payment type;
- information on the key reasons for the increase in charges;
- where applicable, an explanation of when a termination fee cannot be charged;
- reminders to switch and signposting to impartial switching advice;
- the circumstances where a consumer's outstanding charges (debt) could prevent that consumer from switching supplier;
- information on the new TCR for that customer's current tariff;
- clarification that should a consumer wish to switch tariff or supplier, so as not to be affected by the price increase, they can do so; and
- information on the supplier's cheapest deal (see chapter 6) and associated messaging.

5.18. Suppliers will be prohibited from including any additional information in[117], or along with, the Price Increase Notice.

End of Fixed Term Notice

5.19. We propose to prescribe content requirements only for the notices that are sent from a supplier to a consumer when the consumer's fixed term tariff is coming to an end. Our current position, as set out in the draft domestic licence conditions, is that the content of the notice will be prescribed, this will include[118]:

- personal consumption information and details of the consumer's current tariff;
- the date the fixed term period is due to end;

[116] A full list of the content requirements can be found in the draft proposed amendments to Standard Licence Condition 23 set out in the draft domestic licence conditions.
[117] Excluding basic information such as details about the customer, the supplier and in the case of dual fuel accounts, combined information for gas and electricity.
[118] Please note that this is not a comprehensive list of the information requirements. For full details of our proposals for the End of Fixed Term Notice please see the draft domestic licence conditions,

- a personal projection of the consumer's annual spend on the tariff they would roll onto should they take no further action;
- information about the supplier's cheapest tariff and associated messaging; and
- the personal savings achievable by switching from the consumer's 'default' tariff to the cheapest tariff available from their supplier.

5.20. Where a supplier wishes to offer a consumer a further fixed term period, additional content requirements will apply, including informing of the purpose of the communication and that the consumer is under no obligation to agree to a further fixed term period[119].

5.21. To ensure the purpose of these communications remain clear to the consumer, no additional information can be provided with, or contained within these notices, other than the information set out in the draft Standard Licence Condition 22C[120].

5.22. We are not minded to prescribe the format of these notices at this point, but we may look to do so in the future if we are not satisfied with the way in which these measures are adopted.

Mutual Variations

5.23. As noted in chapter 9 we will now also be requiring suppliers notify consumers about proposed mutual variations, as well as provide written confirmation of any agreement made thereafter. In addition to informing the consumer that they are under no obligation to agree to a mutual variation, we propose that these communications will also be subject to some content requirements, details of which can be found in the draft domestic licence conditions.

Supplier Customer Service Performance

5.24. To assist with the provision of impartial information to consumers, we propose to publish regular updates on suppliers' customer service performance, for example in handling complaints, or supplier satisfaction survey results. This would assist consumers in making better-informed switching decisions and may potentially incentivise improvements in supplier performance.

5.25. Taking on this function would be consistent with other regulated sectors such as communications[121] and finance[122], where comparable functions are performed by

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[119] Please note that this is not a comprehensive list of the information or formatting requirements. For full details of our proposals please see the draft domestic licence conditions.
[120] Please see the draft domestic licence conditions.
[121] Ofcom publish aggregate complaints data in their annual report: Please see a link to their 2011 report 'The Consumer Experience: http://stakeholders.ofcom.org.uk/binaries/research/consumer-experience/tce-11/research_report_of511a.pdf

the sector regulator. This will also replace the company performance information currently published by Consumer Focus[123] when this body is disbanded in 2013.

Standard language

5.26. We propose to explore the opportunities to standardise elements of the language used across communications in order to aid consumer familiarity with, and understanding of, the key terms they are presented with on a regular basis.

5.27. While we have started to conduct some research into this area, we recognise that there are complex issues to work through in this regard. We intend to discuss this topic in detail with stakeholders over the coming months.

Our reasoning

5.28. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate. We draw on our own evidence and analysis and that provided in submissions and obtained through stakeholder engagement.

5.29. First, we define the problem by describing the environment that should prevail for consumers and explaining how the current environment falls short of that standard to a material degree. Second, we explain why our updated proposal is an appropriate and proportionate means of addressing the problem identified by explaining why regulatory action is a relevant consideration. Finally, we explain why we consider our proposal to be the most appropriate form of regulatory action in the circumstances, having regard to alternative courses of action.

The problem

5.30. For the energy market to function effectively, consumers need to receive prompts to engage in the market and the information they need if they want to look around for alternative tariffs.

5.31. If consumers are to make well informed choices they need to be given accurate estimates of the cost they are likely to incur on their current tariff and the consumption assumptions which underpin this forecast. This can enable consumers to compare the expected cost of their current tariff with others in the market on a like for like basis. Consumers also need to be able to compare the key non-price terms and conditions of their current tariff and any other tariff they might consider

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[122] FSA publish aggregate and firm-level complaints data bi-annually. Please see a link to this data on their website: http://www.fsa.gov.uk/library/other_publications/commentary

[123] Consumer Focus publish supplier performance information in the form of a league table based upon contacts and complaints regarding the Big Six on their website: http://energyapps.consumerfocus.org.uk/performance/

switching to. All of this information needs to be set out in a way that is clear and easy to understand if it is to be effective.

5.32. While suppliers have made some improvements to their consumer communications as a result of the Energy Supply Probe reforms in 2008[124], we have continued to observe instances where key information is too complex[125], unclear and in some cases incomplete. These features limit a consumer's ability to understand their options, and to make well-informed decisions. They also prevent the consumer from receiving clear prompts to engage with the market.

5.33. Despite writing to domestic energy suppliers outlining our expectations regarding compliance with licence conditions relating to bills, annual statements and PINs and issuing guidance on some of the requirements relating to PINs[126] more needs to be done to ensure that consumers realise the full benefits of improved information[127].

5.34. It is also notable that a large proportion of consumers remain disengaged from the energy market[128]. Consumers that attempt to switch often find it difficult to compare options and to make well-informed decisions. Even when consumers have switched, many are not confident that they have made the right decision.

Addressing the problem

5.35. In order to encourage more consumers to engage with the energy market it is crucial that they are regularly provided with clear prompts to take action with the information they receive, when the time is right for them. In particular, ensuring they are aware of better tariffs for them, or providing them with engaging personalised information which is distinctive and noticeable. If they decide to act it is important consumers have the information they need to engage in a comprehensive, clear, simple, consistent and easy to understand way.

5.36. We have designed the information improvements to work together to meet our objectives of providing:

- prompts to switch;

[124] Energy Supply Probe – Initial Findings, October 2008
[125] Lawes Consulting, 'Energy bills, Annual Statements and price rise notifications: advice on the use of language', November 2011
[126] Guidance on notification of price increases – Standard Licence Condition 23, 16 August 2011
[127] We have opted not to take enforcement action at this time, but have written to suppliers to remind them that they alone are responsible for ensuring compliance with the licence conditions, and to prompt certain individual suppliers to review their bills and annual statements and make amendments where appropriate. Additionally, we are currently in the process of developing guidance on the licence requirements relating to bills and annual statements.
[128] In the March 2011 RMR Finding and Initial Proposals document we estimated that around 40-60 per cent of customers in the energy sector are currently sticky (although we recognise they may have switched in the past) and that vulnerable customers are likely to be disproportionately represented in this group.

- information to make informed choices; and
- information and messaging that is clear and accessible.

5.37. Some information is carried on several communications and is therefore conveyed to consumers a number of times, albeit with differing levels of detail. We consider that this is justified and proportionate as it is necessary to ensure that the key information is available to consumers when they need it. For example, the supplier's cheapest alternative tariff will change throughout the year for many consumers and we consider that it is important that customers are informed of this regularly on their bills as well as on their Annual Statement and other communications.

5.38. We want to encourage customers to keep their Annual Statement and use it as a reference point if they are approached by sales agents or want to shop around. However, we note that in some circumstances and for some consumers the bill will continue to play a vital role as the piece of information which is at hand when they are considering a switch. It is therefore essential that key information and prompts are carried on this communication.

5.39. In designing these proposals we have taken on board considerations raised by stakeholders and by consumers through our research. In particular, we have kept prescription of format to a minimum and only where we think it is needed to meet our objectives. We have recognised the pressure for space on the bill and have looked to minimise the amount of information that is to be included in the summary box. We have also sought to keep the amount of information on the first page to a minimum. We have developed our templates through an iterative process of consumer testing to ensure that we could combine good design practice with an in-depth understanding of how consumers are likely to engage with the information and messaging contained within these key documents.

5.40. An overview of how we envisage the information improvements would tackle the problems identified in the retail energy market is in the table below. A detailed discussion of how our proposals meet each of the aims identified in the table follows.

Table 1 - Summary of proposals for improving information to consumers

Aim	Reasoning	Proposal	Information Channel for each proposal
Prompt engagement	We have found a large proportion of consumers are still disengaged from the energy market. In order to encourage the majority of consumers to engage in the energy market, it is important they are provided with clear triggers and prompts to act on information they receive.	• Cheapest tariff within supplier messaging • Signposting to consider switching tariff/supplier and information on where consumers can find independent advice on changing supplier	Annual statement, Bills, Price Increase Notices (PINs) and end of fixed term notices Annual statement, Bills, PINs and end of fixed term notices
Inform consumers	Our evidence suggests many consumers who try to switch find it difficult to make a well-informed choice. Our consumer research indicates even when consumers have switched they are not confident they have made the right decision. We need to ensure that consumers can confidently navigate the market and have the correct information they need to make an informed choice.	• Personal information on consumption and personal projections of annual cost of current tariff • Provide easy access to key information about a consumer's current tariff • Details of key T&Cs of current deal in a form comparable with information about other deals in the market • Personalised information about the effect of price increases using consumers' current consumption • Clear information about the personal impact of a new contract	Bill, Annual Statement, PIN Annual Statement, PIN and Tariff Information Label (TIL) Tariff Information Label (TIL) provided on Annual Statement, marketing materials and pre-contractual information PIN End of fixed term notices
Increase understanding	Information provided to consumers is incomplete, complex and unclear. This limits consumers' ability to understand the key messages and data they are being provided with.	• Standardise language/terminology • Standardise formats and content	Annual Statement, Bill, PIN Annual statement, Bills and PINs

Prompts to engage

5.41. Our analysis suggests that 40-60 per cent of consumers are either disengaged or permanently disengaged from the energy market[129]. These customers

[129] Ofgem (March 2011), 'The Retail Market Review', page 30.

report that they have never switched supplier and so can be considered to be sticky customers. In addition, the majority of consumers are on standard tariffs[130] with limited decision or trigger points for engagement. To address this we want customers to be given information about suppliers' cheapest tariff on Bills, Annual Statements, PINs, End of Fixed Term notices and potentially other communications.

5.42. We also propose to include prompts to consider switching tariff or supplier in prominent positions on key communications. This will sit alongside our existing requirements for these communication channels to also provide consumers with information on where they can receive independent advice on switching supplier or tariff. This will ensure consumers are aware of the independent channels available to support them in assessing their options.

Information to consumers

5.43. Consumers have clear information needs that need to be met if they are to navigate the market confidently and make an informed tariff choice. Consumers have also expressed a strong preference for personalised communications which use information which is directly relevant to them[131]. Our proposals are designed to ensure consumers are provided with personalised information (e.g. personalised annual projections of price increases, cheapest tariff messages). We propose that the content of key communications is prescribed to ensure consumers receive all the information they require and that the information is relevant to them.

Tariff Information Label

5.44. At present, our review of tariff information suggests it is often not presented in a consumer-friendly format and it is not always easy to compare the terms and conditions of different tariffs. Comparing tariffs offered by different suppliers can be particularly challenging, may lead consumers to switch to tariffs based on incomplete information and may result in poor choices.

5.45. The Tariff Information Label will make it easier for consumers to compare price and non-price features of tariffs. This should lead consumers to make better-informed switching decisions. The format and content of the Label are prescribed to ensure consistency.

Key tariff information

5.46. A lack of information about a consumer's current tariff is clearly a potential barrier to engaging with the market[132]. To help consumers overcome this barrier, we

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[130] 75 per cent of consumers are on standard tariffs (DECC Quarterly Energy Trends March 2010, p 48, 49).
[131] SPA Future Thinking (2012), 'Energy bills, annual statements, price increase notification letters and tariff information labels: proposals for consumer testing', forthcoming.
[132] Ipsos MORI, Ofgem Consumer First Panel Year 4, Findings from second workshops (held in March 2012), October 2012.

propose that this information is provided on key communications. The required information includes: the exact tariff name; payment method; the amount of energy used; standing charge/unit rates; exit fees where applicable; personalised projected cost and TCR.

5.47. While we consider some key information is required on a range of communications, we recognise each of these information channels has a distinct purpose. Consumers need to clearly understand the point of the communication to remain engaged with its content[133]. For this reason, we consider some information is only appropriate on specific channels (e.g. the summary on a bill contains the minimum information required to engage with the market, whereas the primary purpose annual statement is to improve the quality of engagement in the market, and provides information that is needed for consumers to be confident and comfortable navigating the energy market).

Increase understanding

5.48. We want consumers to be confident they can navigate through the market, and comfortable that they understand the options available to them. To do this we are aiming to improve the quality and accessibility of information by making communications simpler and more consistent for consumers. This will be achieved by ensuring information is more user friendly through: standardising formats, content and language; ensuring that key communications have a clear purpose; and ensuring that each communication is distinct.

Implementation

5.49. Following consideration of responses to this consultation and dependent on their views, we envisage proceeding with a consultation on final proposals (including statutory consultation on licence modifications) in spring 2013. On this basis, certain licence modifications may come into effect in summer 2013. Given these timeframes our requirements for;

- Price Increase Notices and End of Fixed Term notices we expect to come into effect two months after the implementation date of certain other licence conditions in the summer of 2013, and;
- Bills, Annual Statements and Tariff Information Label we anticipate these will come into effect by the end of 2013 (approximately 4 months after the implementation of the requirements relating to Price Increase Notices and End of Fixed Term notices).

5.50. We expect that these proposals may require significant changes to back office systems and we need to take this into consideration in the date we set for

[133] SPA Future Thinking (2012), 'Energy bills, annual statements, price increase notification letters and tariff information labels: proposals for consumer testing', forthcoming.

implementation of these new information provisions. We would welcome stakeholders' input on this point as well as their estimates of the cost of implementing these proposals.

6. Supplier cheapest deal

Chapter Summary

This chapter sets out our proposal to require each supplier to provide their customers with personalised information about the supplier's cheapest tariff. We propose definitions that suppliers will be required to use to identify the cheapest tariff for each of their customers. We propose suppliers are required to provide clear information about the annual savings available from taking up the cheapest tariff. We propose that this information is provided in a prescribed format, and included in key documents including the 'Summary Box' on Bills, Annual Statements, Price Increase Notification Letters and End of Fixed Term Notices.

Question 1: Do you agree with our view that the cheapest tariff message should include both supplier's cheapest tariff for their payment method, consumption and meter type, and the cheapest overall tariff from their supplier irrespective of their current circumstances, personalised by consumption?

Question 2: Do you agree with the approach to tariff eligibility criteria proposed for supplier's cheapest tariff?

Question 3: We seek views from stakeholders on whether consumers with smart meters and any relevant time-of-use tariffs that the supplier is offering require separate consideration in relation to this policy proposal.

Question 4: Do you have any suggestions regarding additional rules which they consider relevant for the construction of the cheapest tariff messaging?

6.1. In this chapter we describe the third of our initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so that stronger competition places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices and to rebuild trust and confidence in those who are not engaged and encourage them to participate.

6.2. This chapter focuses on measures to require each supplier to provide their customers with personalised information about the cheapest tariff they are offering and the amount of savings available to them if they were on that tariff. This measure is aimed primarily at showing currently disengaged consumers the savings that can be made from participating in the market, rebuilding their trust and prompting them to engage through this added transparency. We see the provision of this information as also limiting the ability of the incumbent suppliers to respond to competition from other suppliers simply by shifting costs onto their legacy customer base. We expect full implementation of this proposal four months from the acceptance of the RMR licence conditions.

Our proposals

Cheapest tariff by current supplier

6.3. Our proposal is that suppliers will be required to provide each of their customers with personalised information about the cheapest tariff that they offer and the amount of savings available to them if they switch to that tariff.

6.4. We propose that there are two sets of cheapest tariff message given to consumers: (1) 'narrow' - defined as the cheapest tariff offered by that supplier for the consumer's current payment method, consumption level and meter type, and (2) 'wide' – defined as the cheapest tariff of all their available tariffs available irrespective of payment method, meter type or other preferences, but based on the consumer's own consumption.

6.5. In order to provide this information, suppliers will be required to do the following:

- follow the tariff comparison rate (TCR) rules on the treatment of discounts and bundles so that all tariffs are compared on a like for like basis (see chapter 7 for details);
- calculate a personal projection for all eligible tariffs a supplier offers;
- identify:

    1. the cheapest tariff offered by that supplier within each consumer's current payment method, consumption level and meter type, and
    2. the cheapest overall tariff offered by that supplier irrespective of a consumer's payment method, meter type or other preferences, but based on each consumer's own consumption, and

- provide this information in key communications, i.e. Summary Box on Bills[134], Annual Statements, Price Increase Notifications and End of Fixed Term Notices, following prescribed formats and standardised language in some cases to ensure it is clear and accessible (see chapter 5 for details).

6.6. We believe that the aim of a voluntary agreement between the Government and energy suppliers, that included providing consumers with information about the best deal for them (Clegg agreement[135]) complements our RMR objectives of

[134] For the avoidance of doubt, any reference to 'Bills' also includes Statements of Account (i.e. the communications commonly used for direct debit and pre-payment meter customers).
[135] Announced by the Deputy Prime Minister, Nick Clegg on 1 April 2012: http://www.decc.gov.uk/en/content/cms/news/dpm_bestdeal/dpm_bestdeal.aspx

improving customer trust and facilitating consumer engagement. However, our view is that a more stringent and consistent approach and an enforceable framework is required.

6.7. We are proposing to go beyond the voluntary commitment by requiring that the information is personalised for each consumer using their consumption data. We note that under the Clegg agreement suppliers have committed to pass on usage data when a consumer changes supplier, therefore in most cases the supplier should hold a customer's consumption data. However, there will be cases where less than 12 months of consumer's consumption data is available (for example, where a consumer has moved property recently). In this situation we propose that generic advice is given, in line with SLC 31A.

6.8. On Bills and Annual Statements, we are also proposing to prescribe the message to be provided alongside the information on the supplier's cheapest tariff. At this stage we have developed core messaging on the 'cheapest tariff'. We intend to continue to develop further alternative presentation types for the messaging (e.g. tabular, alternative phrasing) for final proposals. An example of the core messaging is presented in the example below:

> *"Based on your current payment method, consumption and meter type, our cheapest tariff for you now is our tariff 'Clear and Simple', with a personal projection of £450.00 per year. If you switch to it, you could save £50.00 per year.*
>
> *Our cheapest overall tariff for you now is 'Online Saver', with a personal projection of £425.00. If you switch to it you could save £75.00 per year but you will have also to switch to pay by Direct Debit and manage your account online.*
>
> *Please note that changing tariffs may involve changing to materially different terms and conditions. Call us or visit our website for details."*

6.9. We are proposing that this messaging is included in the Summary Box on the Bill and on the Annual Statement. Information about the supplier's cheapest tariffs would also be provided on Price Increase Notifications and End of Fixed Term Notices. We propose that the core messaging may be adjusted to accommodate the rules on tariff eligibility criteria set out below and, where we are not prescribing the exact phraseology, we would require this to be clear and accessible. Consumers on fixed term tariffs would also be given information about the supplier's cheapest tariffs in the end of fixed contract notice.

6.10. In developing our proposals we shifted emphasis from provision of 'best deal' and 'best tariff' information as per the Clegg agreement, to 'cheapest tariff' which provides more of an objective outcome that is clearer and simpler to implement.

Eligibility criteria

6.11. It is important that tariffs offered to consumers are genuinely available at the time they are offered, and for a reasonable time afterwards so as not to erode consumer trust. Suppliers may have tariffs that have very competitive prices but are not available to more than a few consumers. Such tariffs may offer significant savings but the majority of consumers may not be able to access that tariff. A similar issue could arise if suppliers set a 'subscriber limit' for a particular tariff and do not remove the tariff from messaging once the limit has been reached. Also, a tariff may be open to new subscribers only for a very limited period.

6.12. To mitigate these potential problems, we propose setting some criteria for the inclusion of a tariff in the supplier's cheapest tariff messaging. For example, criteria could include a requirement that tariffs are open to an unlimited number of consumers for at least four weeks from the time the communication goes out to consumers, with no restrictions on location or qualification. The key principle would be that niche, limited application or limited availability tariffs could not be included. **We welcome stakeholder views on these criteria.**

Rules for construction of the cheapest tariff messaging

6.13. Alongside the core proposals we propose that the cheapest tariff messaging follow a set rules for specific circumstances:

- **Prepayment meters (PPM)** – options for consumers on PPMs are limited as suppliers often only offer one PPM tariff[136]. Further, PPM consumers receive an Annual Statement and Statement of Account, but do not receive a Bill. We propose that suppliers provide messaging to remind their PPM consumers of their right to switch supplier even if in debt up to £500 according to the debt assignment protocol (e.g. 'Did you know you can switch supplier to another PPM tariff even if you are in debt up to £500?'). In the case of PPM consumers, we propose that the wide definition of the cheapest tariff will respect their meter type. This means suppliers will not be required to inform PPM consumers of the cheapest overall tariff if this involves them having to change meter type. This is to avoid consumers feeling frustrated about cheaper tariffs which they cannot take advantage of because of their meter type.

- **Consumers with E7 meters** – where E7 meters can run in standard mode consumers should be offered standard meter tariffs in the narrow definition where they are cheaper than E7 tariffs.

- **Differences in terms and conditions** – we are proposing that all relevant communications should, as a minimum, include appropriate messaging to make consumers aware that changing tariff may involve material changes to terms and conditions (such as termination fees and

[136] Currently only two suppliers of the incumbent suppliers offer more than one PPM tariff.

other important differences). However, we would welcome views from stakeholders on whether more detailed information should be included in the relevant communications to provide a more comprehensive explanation.

- **White label** – any tariffs of a related 'white label' provider should be included in the assessment of supplier's cheapest tariff and should be offered to consumers with explanatory text if these are the cheapest available for them and vice versa (i.e. consumers currently on white label tariffs should be provided with the information on the supplier's cheapest tariff - this proposal is just about the price and not other non-monetary benefits).

- **Consumers on fixed term contracts** – suppliers will be required to inform their customers on fixed term contracts if there is a cheaper tariff for that customer using the narrow and wide definitions, even if this means switching from a fixed term to an evergreen contract. Suppliers will be required to take into account any exit fees in making this assessment and the message should also include information on the exit fee. Suppliers will be required to highlight key changes to terms and conditions. For example, if the consumer would be switching from a fixed price tariff to a variable price tariff, the supplier will be required to inform the customer that their new price may increase after the switch.

- **Consumers on evergreen tariffs** - under the narrow definition we propose that suppliers inform their customers on evergreen tariffs of any fixed term tariff which would be cheaper.

- **Consumers on green tariffs -** under the narrow and wide definition we propose that suppliers inform their customers currently on green tariffs of any cheaper non-green tariff.

- **Consumers already on the cheapest tariff** - for either narrow, wide or both definitions - we propose to require suppliers to give a clear message to consumers that they will be informed through their Bills and Annual Statements when/if a cheaper tariff becomes available to them (e.g. 'You are currently on our cheapest tariff. Note however, that this may change, and we will inform you through our regular communications when a cheaper tariff becomes available to you.')

- **Consumers who are with a supplier who has only one tariff** - for either narrow, wide or both definitions - we propose to require suppliers to give a clear message to consumers that they will be informed through their Bills and Annual Statements when/if the supplier introduces a new tariff which is cheaper than the tariff consumers are currently on.

- **Online/offline consumers** – under the narrow definition of cheapest tariff we propose that offline consumers will only be provided the information on the cheapest offline tariff, while online consumers will see both (i.e. where the cheapest tariff for an online consumer happens to be an offline tariff, the consumer should be provided with information on that tariff). Under the wide definition, offline customers will be told if the cheapest tariff is an online one.

- **Consumers with smart meters and any relevant time-of-use (ToU) tariffs** - consumers on smart meters should be given information on the cheapest ToU tariffs. Where the cheapest tariff for consumers with a smart meter is a ToU tariff, customers with a smart meter will be given information about the ToU tariff. If consumers do not have a smart meter, suppliers will not be able to tell whether they may save by moving to it and should provide only a generic message on possible savings if consumers move to a ToU tariff. **We are seeking views through this consultation as to whether consumers with smart meters and any relevant ToU tariffs that the supplier is offering require separate consideration in relation to this policy proposal.**

Our reasoning

6.14. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate – drawing on our own evidence and analysis and the evidence drawn from submissions and stakeholder engagement.

6.15. First, we first define the problem – by describing the environment that should prevail for consumers, and explaining how the current environment falls short of that standard, and why these deficiencies are material. We then explain why our updated proposal is an apt and proportionate means of addressing the problem identified – by explaining why regulatory action is a relevant consideration, and why we consider our proposal to be the most appropriate form of regulatory action in the circumstances having regard to alternative courses of action.

The problem

6.16. Consumers need to have access to clear information that enables them to engage with the market with confidence and make accurate decisions about their energy options.

6.17. Our research shows that an important barrier to switching tariffs while staying with the same supplier is lack of awareness that cheaper tariffs exist[137]. Some consumers think their supplier has put them on the best tariff they have on offer and so there is no point in engaging at all. Our policy aims to dispel this myth and encourage engagement at least in the alternative offers available from their current supplier.

[137] SPA Future Thinking, 'Options for cheapest tariff messaging on customer communications; Report of qualitative research', forthcoming.

6.18. There is a general disparity between the margins earned from legacy/sticky consumers and those earned from active customers[138].This policy aims to reduce the extent to which suppliers with a large sticky customer base can react to competition from other suppliers by shifting costs onto this customer base.

6.19. Many consumers are not confident enough to engage in the market and/or are put off by the perceived search costs and hassle around switching supplier[139]. For them, switching to their supplier's cheapest tariff may represent a more realistic way of benefiting from competition in the market. Some consumers are not at all aware of the savings that can be made from participating in the market in this way, and others know this is possible, but have not encountered a prompt or trigger to do so[140]. Receiving this information may increase consumers' awareness, and may also prompt some consumers to look beyond the tariffs their own supplier has on offer.

Addressing the problem

6.20. We are contemplating regulatory action because suppliers have not addressed similar problems in the past through voluntary initiatives, including our proposals from the Probe, which sought to improve consumer experiences in their interactions with suppliers. In addition, we are conscious that suppliers may adopt different approaches to the Clegg agreement.

6.21. This proposal will make it easier for consumers to engage with the market if there are cheaper tariffs available from their existing supplier, using personalised information on their consumption and without needing to change payment method and meter type. It will also provide consumers with information on the level of savings that could be made irrespective of payment method or other preferences (which are likely to be higher), but may involve changing payment type or moving to online bill management. This effectively provides a default option for consumers and will reduce the search costs that have been a barrier for many, by making relevant information more readily available ie reducing the effort/time consumers have to invest to compare tariffs.

6.22. We believe that this is an effective way of persuading consumers to switch to cheaper tariffs. This proposal aims to help disengaged consumers to identify cheaper tariffs. Our research suggests that providing consumers with information on cheaper tariffs available from their own supplier is effective for some consumers and is likely to encourage a degree of engagement with the market, and switching to cheaper tariffs[141].

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[138] See chapter two.
[139] Ipsos MORI (2012), 'Ofgem Consumer First Panel Year 4; Findings from first workshops (held in October and November 2011), January 2012.
[140140] SPA Future Thinking research on the cheapest tariff shows that some consumers are surprised that there may be savings, that suppliers don't automatically move them to the cheapest tariff.
[141] SPA Future Thinking, 'Options for cheapest tariff messaging on customer communications; Report of qualitative research', forthcoming.

6.23. This is part of a complementary set of initiatives, including proposals to improve regular communications from suppliers, which are aimed at giving consumers a stronger prompt to engage and to provide them with the information they need to assess alternative offers. This will help make things clearer, simpler and fairer for consumers.

Smart metering and ToU tariffs

6.24. Government's smart meter data access framework has the potential to interact with our policy proposals. For example, if a consumer opts out of sharing granular consumption data with their supplier under the new rules in the licence, this could mean that the supplier would not be able to evaluate whether granular ToU tariffs would be cheaper for that consumer. **We are therefore seeking views through this consultation as to whether our 'cheapest tariff' proposals need to separately consider consumers with a smart meter.**

6.25. We are also seeking views on whether the framework should explicitly cover the offering of ToU tariffs. These tariffs will only be the cheapest option where a consumer has a particular usage profile, generally where they use energy at off-peak times. Our current proposals would not prohibit suppliers from informing consumers that a ToU tariff is cheapest for them, but nor would they require suppliers to inform consumers that changing their pattern of usage could mean they would save money by moving to a ToU tariff. We also recognise that there may be concerns about suppliers offering a ToU tariff as the 'cheapest' without a consumer fully understanding the potential implications of this if their pattern of usage changes. Given that the market for complex ToU tariffs which use consumers' granular consumption data is still emerging, **we would welcome views as to whether and how these tariffs should be accommodated within the framework.**

Implementation

Implementation processes

6.26. As this is a new proposal, we recognise that it will need to be refined and that further work needs to be undertaken before we make final proposals. We do recognise that our proposal on supplier's cheapest tariff will result in costs to suppliers associated with providing personalised information on the cheapest tariff to each of their customers. Through this consultation we are giving suppliers the opportunity to comment on the likely effect of this proposal on their costs. In addition they will be able to comment on the draft licence conditions.

6.27. In order to inform the detailed design of this policy for final proposals, and to gain a better understanding of the costs of implementing this approach, we intend to include this messaging as part of any forthcoming field trials, and continue ongoing workshops[142] with our stakeholders.

Timetable

6.28. Subject to consideration of responses to this consultation, we envisage proceeding with a consultation on final proposals (including statutory consultation on licence modifications) in spring 2013. We expect full implementation of this proposal four months from the acceptance of the RMR licence conditions. This will mean this policy coming into effect at the same time as the new summary box on the Bill and the new Annual Statement.

6.29. We propose that this will give sufficient time for suppliers to make the changes to back office systems required to implement this policy. We seek views on this proposed timescale.

[142] The Consumer Bills and Communications Roundtable Group (CBCRG) terms of reference and objectives – http://www.ofgem.gov.uk/Markets/RetMkts/consumer-bills-and-comms-round-table/Pages/index.aspx

7. The tariff comparison rate

Chapter Summary

This chapter sets out our proposal to introduce a Tariff Comparison Rate (TCR). It also sets out our proposals in two related areas: personal projections and best buy tables.

Question 1: Do you agree with our proposal to introduce a price comparison tool?

Question 2: What is your view about the terminology we are proposing for the two price comparison metrics? Are they clear and easy for consumers to understand?

Question 3: In your view, does our proposal for the TCR strike an appropriate balance between different trade-offs in terms of simplicity, accuracy, confusion and saliency? Please explain the reasons for your view.

Question 4: Do you agree with our proposal for the different features of the Tariff Comparison Rate, and our related proposal on the personal projection? Do you have any thoughts on whether and how time of use tariffs should be accommodated in the TCR and personal projection? Please explain the reasons for your view.

Question 5: In your view, should suppliers be required to make available up to date information on TCRs for their tariffs? What is your view on the barriers to the publication of best buy tables, and how could we better facilitate publication by third parties?

Question 6: Do you have any concerns regarding the implementation of this proposal? How long after a decision has been made would you take to implement this proposal? What drives those timescales?

7.1. In this chapter we describe the fourth of our initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so stronger competition places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices and to rebuild trust and confidence in those who are not engaged and encourage them to participate.

7.2. In the December 2011 consultation we proposed to introduce a price comparison guide to help consumers compare the cost of energy tariffs and improve effective engagement with the market. Respondents to the consultation were broadly supportive of this proposal.

7.3. Our policy has developed in light of responses to our December 2011 consultation, but we still consider that a price comparison guide would benefit consumers. This section describes our proposal to introduce a TCR, and also our proposals in two related areas: personal projections and best buy tables.

Our proposals

7.4. We propose to introduce the TCR as a common currency for market wide comparisons of energy prices. Under our proposal, suppliers will be required to express each tariff they offer, including white label deals, as a single number that captures the tariff's relevant price elements for low, medium and high users. They will be required to refer to this single number as 'Tariff Comparison Rate' or 'TCR'.[143]

7.5. The personal projection will enable consumers to make an accurate comparison of energy tariff prices. The methodology that underpins the personal projection will ensure that comparisons between tariffs offered by different suppliers are like-for-like. The use of individual energy consumption in the calculation ensures that the projection is relevant to the consumer and would help to improve the quality of switching decisions. Suppliers will be required to refer to this as a 'Personal Projection'.[144]

7.6. For the TCR and the personal projection to be effective, they require binding, standardised rules for its calculation. Ofgem is well placed to set these rules because we can include them in licence conditions. We therefore propose to introduce rules governing how suppliers calculate and provide the TCR and personal projection. The draft domestic licence conditions accompanying this document outline our proposal on the TCR and personal projection.

7.7. We recognise that price is not the only factor that is relevant to consumers when they choose an energy tariff. We consider that the combination of the TCR, Tariff Information Label and information on supplier performance will enable consumers to see all relevant information in an accessible format before they select an energy tariff and supplier.

The TCR

7.8. We propose that the TCR is calculated as an estimated bill divided by the assumed consumption for a low, medium or high user of gas or electricity. To ensure comparability across suppliers, Ofgem would set the assumptions to be used for low, medium and high consumption in the calculation of TCRs[145]. Suppliers will be

[143] We welcome views from stakeholders about this terminology, and how clear and easy to understand it may be for consumers.
[144] We welcome views from stakeholders about this terminology, and how clear and easy to understand it may be for consumers.
[145] The consumption assumptions used for low, medium and high consumption will differ by meter type. For those with Economy 7/10 meters, a standard assumption about the proportion of consumption that occurs overnight would be required to enable TCRs to be expressed as a single figure. We currently propose that this should be 55 per cent.

required to inform consumers through regular personal communications[146] whether they are low, medium, or high users[147].

7.9. The TCR will be expressed in pence per kilowatt hour (p/kWh), and its calculation will include any standing charge and the charges for the units of energy consumed. TCRs will be calculated for each variant of a core tariff (i.e. for each payment type and with and without dual fuel discounts).

7.10. TCRs will be calculated as Great Britain averages[148] and include all non-contingent discounts and penalties, but will exclude the discounts and penalties that are contingent on the consumer's behaviour or other factors that cannot be known when the consumer enters into the contract.[149] Suppliers will be required to make clear where a TCR does not include a contingent discount or penalty.

7.11. Dual fuel tariffs will have separate TCRs for the gas and electricity elements. These TCRs will include any dual fuel discount, which should be split evenly across the gas and electricity elements.[150] The TCR will also include the cost of the non-energy element for tariffs that include a mandatory (tied) bundle, or for tariffs where taking the bundled product is the default option (ie where it is possible for consumers to opt-out but they must make an active choice to do so).

7.12. The TCR will not include the non-energy element of a tariff with a bundled product where the bundled product is opt-in (i.e. consumers have to make an active choice to bundle the product to the tariff). The TCR will not assign a value to other features, such as affinity partnerships with businesses that are active in other markets, charities, loyalty card providers, or schemes where the value of the features provided are difficult to estimate. Where bundled products are tied or opt-out in nature, suppliers would be required to provide information about the bundled product alongside the TCR. This would ensure that the consumer is aware of the tariff features that affect the value of the TCR.

7.13. In general, each time a tariff is created or the price of a tariff changes, the supplier will need to calculate (or update the calculation of) its TCR using our proposed methodology.[151] Hard copy and online communications would be updated

[146] I.e. bills, statements of account, price increase notifications, Annual Statements.
[147] Consumers will be classed as 'low' if their consumption is between zero and the mid-point between the 'low' and 'medium' consumption assumptions. Consumers will be classed as 'high' if their consumption is above the mid-point between the medium and high consumption assumptions. Consumers will be classed as 'medium' if their consumption is between the two mid-points described above.
[148] Specifically, TCRs would be calculated as a weighted average where the proportion of a supplier's customers in each region at a fixed date in the year would act as the weights (i.e. weights would sum to one across regions). This would ensure that the TCR would be based on the typical consumer in Great Britain that has chosen the tariff.
[149] For the purposes of this policy proposal, a contingent discount (or penalty) is one that depends on a consumer's decision after they have chosen a tariff (or a dual fuel tariff), or one that depends on the purchase of a product other than gas and electricity supply.
[150] To ensure that the nature of the tariff is clear to consumers, we would require suppliers and intermediaries to highlight that the TCR is dependent on taking both fuels.
[151] When calculating TCRs, suppliers must use the new prices where there has been a public price change announcement (even if the price increase does not yet apply to the customer because of the 30 day rule in

with the new TCR. For tracker tariffs that are updated infrequently, the TCRs will be updated at the same time that the price changes. TCRs will be updated at the end of each day for tracker tariffs with more frequent price changes (based on the daily average price).[152] It is not yet clear if TCRs would be appropriate for time of use tariffs and we would welcome stakeholders' views on this point.

7.14. The table below presents an example for the calculation of a TCR, based on a consumer who is on a standard electricity tariff and has annual consumption of 3,100kWh. This level of consumption means that the consumer is a medium user. To simplify exposition, we assume that the tariff is available in only two regions, A and B. Of these two regions, 65 per cent of the supplier's customers are in region A:

Table 1 - Example of the TCR calculation[153]

Tariff	Standing charge (p/day)	Unit rate (p/kWh)	Discounts / Penalties (all regions)	Consumption assumption (kWh)	TCR (p/kWh)
Standard Electricity	33 (A) 24 (B)	10 (A) 12 (B)	3000p/year (online) 500p/year on bill (late payment)	3300 (medium user)	13.09

TCR calculation	TCR (A) = ((33p*365) + (10p*3300) - 3000p) / 3300 = 12.73 TCR (B) = ((24p*365) + (12p*3300) – 3000p) / 3300 = 13.75 TCR = (0.65*12.73)+(0.35*13.75) = 13.09

Personal projections

7.15. Another element of our policy proposal is the personal projection. The personal projection builds on the rules of the TCR, but uses the consumer's actual consumption of gas and/or electricity,[154] and uses regional tariff charges to provide a projected annual cost for each consumer.[155] The personal projection will also account for the consumer's choices in the context of product bundling.[156]

SLC 23). In all other cases the supplier must use the charges that currently apply to each customer.
[152] Suppliers will need to communicate daily with intermediaries such as price comparison websites to ensure their data is up to date. Hard copy TCRs for these tracker tariffs will be updated once per week.
[153] Consumers would normally not see the TCR calculation, they would only see the TCR figure. The TCR calculation does not include the £5 late payment fee, as this is a contingent penalty. Suppliers would be required to publish this information alongside the TCR for this tariff.
[154] In cases where the supplier has actual meter reads for the previous 12 months. In all other cases the supplier will be required to use its best estimate of consumption for a 12 month period, taking into account all relevant factors.
[155] Suppliers will be required to estimate the consumer's usage where actual consumption is not available in line with the existing rules in Licence Conditions.
[156] This means that the personal projection for the consumer's current tariff will include the value of any bundle they opt for. Personal projections for alternative tariffs will include in their calculation the options that the consumer chooses. This condition is feasible because the consumer actively engages with a

7.16. Personal projections are expressed in pounds per year (£/year). They represent an estimate of the cost of the gas or electricity service that a consumer would incur in the following year if they stayed on the current tariff, based on their consumption in the previous year and the tariff features that they have selected[157].

7.17. Where a consumer's current fixed term tariff will expire within the next 12 months, an annualised personal projection should be provided for their current tariff. To ensure that the consumer is aware that their tariff will expire within 12 months, additional messaging would need to be provided alongside the personal projection.

Table 2 - Example of the personal projection calculation[158]

Tariff	Standing charge (£/day)	Unit rate (p/kWh)	Discounts / Penalties	Actual consumption (kWh)	Personal projection (£/year)
Standard Electricity	£0.33	10	£30/year (online) £5 on bill (late payment)	3100	£400.45

Personal projection calculation	Personal projection = (£0.33*365) + (£0.10*3100) - £30 = £400.45

Communication of TCRs and personal projections

7.18. We propose to require suppliers to include TCRs and personal projections for the consumer's current tariff on regular supplier communications. The TCR will be used as follows:

- Summary box on bill – TCR for the consumption category specific to the consumer[159];
- Annual Statement – the Tariff Information Label box will contain the TCR for the consumption category specific to the consumer; and

supplier or third party if he is to receive a personal projection.

[157] In cases where the supplier has actual meter reads for the previous 12 months. In all other cases the supplier will be required to use its best estimate of consumption for a 12 month period, taking into account all relevant factors.

[158] Consumers would normally not see the personal projection calculation, they would only see the personal projection figure. The personal projection calculation does not include the £5 late payment fee, as this is a contingent penalty. Suppliers would be required to provide this information to consumers when providing the personal projection for this tariff.

[159] For the avoidance of doubt, any reference to 'bills' also includes statements of account (i.e. the communications commonly used for direct debit and pre-payment meter customers).

- Price Increase Notification – the letter will inform the consumer of the new TCR for the tariff they are on.

7.19. In addition, the TCR will appear on Tariff Information Labels and all advertising materials. Labels will contain TCRs for low, medium and high consumers. On advertising materials, suppliers would be required to show TCRs for low, medium and high consumers. Suppliers could choose to give prominence to one or more of the TCRs by placing them in larger text. However, the TCRs for all categories must be clearly visible in the advertisement.

7.20. When communicating TCRs for alternative tariffs in marketing materials and advertisements, suppliers will be required to use consistent language and presentation. We will require the TCR to be presented on all advertisements and marketing materials as the most prominent form of price information. Where relative price claims are made (e.g. 'we're cheaper than supplier B'), the TCRs of comparable tariffs will need to be presented to substantiate the claim.[160]

7.21. Personal projections would be used as follows:

- Summary box on bill (along with the supplier's cheapest deal).
- Annual statement.
- Price Increase Notification.

7.22. In addition, suppliers will be required to use the personal projection methodology as far as possible when providing estimates to potential new customers in the context of face-to-face sales, telesales and online sales. We also propose to mandate that personal projections for alternative tariffs are included on regular supplier communications, and that the same methodology for calculating the personal projection must be used in calculating the supplier's cheapest deal and identifying the savings that could be made through switching to it.[161] Through our work in the Confidence Code, we will ensure that the rules applied to the TCR and personal projection of alternative tariffs are also applied by accredited third parties such as comparison websites.

Best buy tables[162]

7.23. We would hope to see the introduction of TCRs leading to the publication of best buy tables by third parties. While we do not propose to take a direct role in the production of these tables ourselves, we welcome views on whether there are barriers to this happening or whether there are steps we could take to facilitate their

[160] For example, we would require suppliers to clearly specify that the TCR presented in an advertisement or on other marketing materials is 'for a medium user' and 'depends on your energy use'.
[161] See chapter 6 on the 'supplier cheapest deal' for a detailed discussion of this proposal.
[162] Technically, the tables we refer to here are 'cheapest buy' tables subject to certain eligibility criteria. However, we retain the familiar term 'best buy tables' in our discussion.

production. For example, we seek views on whether it would be necessary for us to amend the Confidence Code (which governs comparison websites), and/or require suppliers to publish or provide third parties with TCR information for all of their tariffs in an appropriate format.

7.24. If we were placing a requirement on suppliers to compile up to date information on the TCRs of their tariffs we could further consider a range of rules around which tariffs should and should not be included in this information, to reduce the risk of best buy tables including tariffs that are about to expire or are close to their subscription limit rate. Again, we seek respondents' views on whether such rules and requirements are necessary. The table below summarises our working proposal.

Table 3 - Summary of the TCR, personal projection and best buy tables proposal

Element	Proposal
Communication of TCRs	TCRs would appear on suppliers' communications, best buy tables, adverts etc.
Communication of personal projections	Personal projections for the current and alternative tariffs would appear on suppliers' communications. The same methodology would be employed when suppliers provide estimates to consumers at other times, including via switching sites.
Units	£/year for personal projections, p/kWh for TCRs.
Discounts and penalties	Include non-contingent discounts and penalties in TCR. Contingent discounts and penalties excluded from TCR but will be explained in any accompanying text.
Dual fuel	Separate TCRs for the gas and electricity elements of dual fuel tariffs. Dual fuel discount included in TCR calculation.
Additional features	Exclude additional features such as loyalty points from the TCR (TCR based only on energy cost).
Bundling	Treatment depends on type of bundle. In general, where taking the bundled product is the default option (or mandatory) the TCR would include the cost of the bundled product. Where the bundle is an opt-in option, the TCR would exclude the cost of the bundled product.
Frequency of updating	Require immediate updating of TCRs online (TCRs for tracker tariffs to be updated at the end of each day). Hard-copy TCRs offline to be updated at least once per week.[163]
Publisher of best buy tables	Any third-party could choose to publish best-buy tables.
TCRs for low, medium and high users	TCRs would be provided for low, medium and high users. Communications from suppliers would tell consumers if they are low, medium or high users.

[163] This would not be a problem for the majority of tariffs because of SLC 23, which states that that there must be 30 days notice where prices increase. Permitted tariffs that track indices that frequently move may be more of an issue.

Our reasoning

7.25. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate - drawing on our own evidence and analysis and the evidence drawn from submissions and stakeholder engagement.

7.26. First, we define the problem – by describing the environment that should prevail for consumers, and explaining how the current environment falls short of that standard, and why these deficiencies are material. We then explain why our updated proposal is an apt and proportionate means of addressing the problem identified. To do this we explain why regulatory action is a relevant consideration and why we consider our proposal to be the most appropriate form of regulatory action in the circumstances, having regard to alternative courses of action.

The problem

7.27. Consumers should be able to compare the relative price of different alternative tariffs without the use of intermediaries or complex comparison tools. However, there are currently a large number of tariffs and complex pricing structures, and where consumers have no access to these intermediaries they face difficulties when comparing energy tariffs.

7.28. For a consumer to make an accurate comparison of their current tariff against alternative offers, it is essential that they know how much they currently pay for energy each year. This figure is the benchmark against which all alternative offers can be compared but it is currently difficult for consumers to find this information – they may need to look through several past bills and annual statements. Even when the consumer finds the information, there is currently no guarantee that the figure is correct as prices may have changed. Finally, it is not certain that the figure will be comparable with estimated annual costs provided by other suppliers.

7.29. Switching sites can, to some extent, help consumers to make consistent comparisons. However, while many consumers who do switch suppliers make use of switching sites, they are not available to or used by all consumers. Indeed, approximately 20 per cent of households in Great Britain do not have internet access in 2012[164]. Our latest tracking survey found that 34 per cent of those who say they have ever switched gas supplier found out about the tariffs available on a switching site while the complementary figure for electricity was 31 per cent[165]. Approximately 27 per cent of switches were completed online for gas and 25 per cent for electricity[166].

[164] Office for National Statistics, 'Internet Access - Households and Individuals', 2012.
[165] Ipsos MORI, 'Customer Engagement with the Energy Market - Tracking Survey 2012', pages 27 and 28, October 2012.
[166] Ipsos MORI, 'Customer Engagement with the Energy Market - Tracking Survey 2012', pages 30 and 31, October 2012.

7.30. For the large number of consumers that are unable to use switching sites, comparing the prices of different tariffs involves analysing and understanding the standing charge and unit charge elements of the tariffs. This makes comparisons difficult. The comparison can be even more complex if discounts, penalties or other features are not applied consistently across all tariffs.

7.31. This makes it difficult for consumers to shop around for better deals than the one they are on. In some situations this complexity may also lead to bad consumer experiences when they consider switching tariff [167]. Some consumers might be put off engaging altogether.

7.32. Both the complexity in the market and previous bad experiences present barriers to consumer engagement in the energy market. The lack of consumer engagement reduces competitive pressure on suppliers and may be detrimental to consumers.

Addressing the problem

7.33. Our proposal to introduce the TCR aims to prompt consumers to engage with the energy market. It allows consumers to access information on a number of tariffs which is presented in a consistent manner and this might encourage a consumer then to further investigate a tariff with a lower TCR than their own tariff. Our proposals to simplify and limit the number of tariffs and improve the information received by consumers are complementary to each other and would also make it easier for consumers to choose the best tariff for their circumstances.

7.34. Our proposal to introduce a personal projection addresses the difficulty faced by consumers in making accurate comparisons of tariff prices. The mandated methodology ensures that all personal projections will be comparable. By providing the personal projection on each bill and annual statement, our proposals will ensure that consumers have up to date information to hand whenever they wish to compare the price of energy tariffs. Requiring suppliers to use the personal projection during the sales process will ensure that the consumers know exactly how much they could save through a switch and so should improve the quality of switching decisions.

7.35. Both the TCR and the personal projection aim to make it easier for consumers to compare tariffs by expressing prices as a single number. In several recent qualitative consumer research projects, the idea of a 'common currency' for energy

[167] For example, our research with consumers has shown that some 'felt that the number of suppliers and choices [leads] to a sense of confusion which [prevents] people engaging in the market'. See Opinion Leader (2011), 'Ofgem Consumer First Panel Year 3, Report from the second set of workshops'. Similar concerns feature in the 2012 Consumer First Panel Report: Ipsos MORI (2012)'Consumer Engagement with the Energy Market; information needs and perceptions of Ofgem; Panel Year 4; Findings from the second workshops'.

prices has been viewed as something that would help consumers to engage with the market[168].

7.36. The TCR may encourage consumers to consider if their current tariff is the most appropriate for them, or if they should switch to a different tariff. Therefore one aim of the TCR is to improve consumers' understanding of relative prices.[169] The personal projection is designed to help consumers be more confident in their choice of tariff.

7.37. To enable the consistent comparison of relative prices, it is important that the TCRs and personal projections are comparable across energy tariffs and suppliers. Ofgem is well placed to ensure that the rules for calculating the TCR and personal projection are consistent and applied by all suppliers.

7.38. We recognise that the TCR is not a 'silver bullet' that will solve all the difficulties faced by domestic consumers when comparing supplier offerings. Indeed, we note that the TCR does not provide 'at a glance' tariff comparability. Consumers will need to do further investigation of those tariffs that look promising, using their own consumption information, to check if they provide a better deal for them. The TCR is likely to be more effective if it is possible to standardise the terminology used by energy suppliers when describing their tariffs, and if it is possible to improve the clarity of information received by consumers from their supplier. We are considering these issues as part of the RMR (see chapter 5 for a discussion of these proposals).

7.39. However, we consider that the TCR could play an important role in promoting effective engagement in the retail market, alongside our other proposals in the RMR package of remedies. We set out below our rationale for designing specific features of the TCR, personal projection, and best buy tables.

Terminology

7.40. We are proposing that suppliers will be required to use the terms 'Tariff Comparison Rate' and 'TCR'. Consumer reactions to these terms have been mixed. Some consumers found 'TCR' clear and easy to understand, while others asked for it to be changed and made clearer. We welcome views from stakeholders on this terminology.

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[168] Research events were held with a wide range of consumers from across Great Britain. Some events involved the Consumer First Panel while others involved consumers with no previous involvement in energy market research. The TCR concept was discussed to varying degrees as part of various research projects exploring options for improving tariff comparison and research into information remedies and improved customer communications – see appendix 6 on accompanying consumer research.
[169] The TCR would be based on standard consumption assumptions and so would not allow an accurate comparison for individual consumers. However, the metric could act as a guide to potential savings. Consumers would investigate the suitability of particular tariffs for their circumstances where a TCR suggests that savings might be available.

Units

7.41. The TCR and personal projection could be presented as an estimated bill or as an average unit rate. In both cases, it would be necessary to make an assumption about the amount of energy used by consumers. This issue has been explored in consumer research and we have considered the potential benefits and unintended consequences of each approach.

7.42. Expressing TCRs in pence per kilowatt-hour (p/kWh) is likely to minimise the risk of consumers being mislead by the information (i.e. consumers may believe that a TCR expressed in £/month would be their direct debit payment and would be surprised when their bill differs from the TCR). It may also help to educate consumers of the term kWh and role of consumption in determining the overall consumer's bill in advance of the roll-out of smart meters. Personal projections are expressed in pounds per year (£/year). This is likely to be more effective in prompting consumers to engage in the energy market, which is one of the objectives of this proposal.

Low, medium, and high users

7.43. TCRs could be based on the consumption of the medium consumer alone or could be based on the consumption of low, medium and high consumers.

7.44. The medium consumer approach, while more simple, could be less useful as a comparison guide than the low, medium and high approach. For example, the tariff that is the cheapest based on medium consumption may actually be more costly than alternative tariffs for some users with different consumption levels. Providing TCRs for low, medium and high consumers would mitigate this risk (but would not eliminate it). It would also meet consumers' expectations about seeing information that is more relevant to them.

Regional TCRs

7.45. At present, suppliers set different standing charges and/or unit rates in different regions. To some extent, these pricing differences reflect differences in the average cost to serve consumers in the different regions.

7.46. TCRs presented as Great Britain averages would help to achieve one of the aims of the TCR, namely to remove confusion from tariff price comparisons. It would also allow TCRs to be used in national media and in suppliers' marketing campaigns. We note that this approach could lead to significant regional price differentials and have chosen the weights to mitigate that risk

Simplicity, accuracy, confusion and salience

7.47. Consumers may use the TCR in different ways. Some consumers may compare tariffs directly using the TCR. Others may use it as a prompt to investigate further the relative prices for different tariffs, and find out if they are on the best tariff for their particular circumstances.

7.48. The different objectives of the TCR result in design trade-offs. For example, as a prompt, the TCR should be simple and salient, but as a comparison tool it is important that the TCR is also accurate.

7.49. The more accurate the TCR (e.g. providing regional TCRs rather than national or using several consumption categories), the less simple it is and a greater amount of information would need to be included on suppliers' communications and marketing materials.

7.50. On the other hand, the clearest prompt to engagement would be provided by a TCR in units of £/annum. However, as discussed above, this approach would risk confusing the consumer. The options we considered in the previous three sections set out in more detail these particular trade-offs.

7.51. Our proposal is to provide personal projections in £/annum, and provide TCRs in p/kWh. TCRs will be provided as an average across Great Britain for low, medium and high consumption categories while personal projections will be based on a consumer's consumption.[170] We are keen to understand whether stakeholders agree that our proposal strikes an appropriate balance between these considerations.

Implementation

7.52. We will continue to develop the TCR policy over the coming months, and welcome stakeholders' views on our proposal. In addition to considering responses to this consultation, and continuing our work with stakeholders to refine these proposals, the TCR will feature in our proposed field trial of the Annual Statement. This trial would provide some evidence on the likely effectiveness of our information remedies proposals and may provide some important insights into how consumers react to the TCR. This evidence would be a reliable indicator of the potential impact of our proposals as it would be based on the actions that consumers have taken, rather than what they say they would do. However, the trial may underestimate the impact of the TCR because TCRs would only be available for tariffs offered by the volunteer supplier(s).

7.53. We are proposing that the TCR would appear on a number of communications and note that suppliers will have to make some systems changes to bring this into effect. It is also important to build consumers' understanding of the TCR and a communications campaign may be required before the TCR is rolled out.

[170] Actual consumption in cases where the supplier has actual meter reads for the previous 12 months. In all other cases the supplier will be required to use its best estimate of consumption for a 12 month period, taking into account all relevant factors.

7.54. We are keen to understand the implementation challenges that suppliers would face and the likely cost impacts from the time we envisage that the RMR licence conditions are implemented. This would mean that suppliers would need to have a TCR for each of their tariffs from the date that the tariff numbers and the tariff information label proposals are in place. We propose giving suppliers a further two months before the TCR and personal projection information would be reflected on bills and Annual Statements.

8. Standards of Conduct for domestic consumers

Chapter Summary

In December 2011 we proposed the introduction of a revised set of Standards of Conduct covering all interactions between consumers and suppliers (and their representatives). In this chapter we confirm our intention to continue with this proposal and offer further details regarding how we see the Standards of Conduct working in practice.

Question 1: Do you agree that the revised Standards of Conduct (SOC) will help achieve our objectives?

Question 2: Is there a different name for the SOC that will have more meaning to consumers and can be used by stakeholders across the industry?

Question 3: Does our approach to enforcement mitigate stakeholder concerns about clarity and regulatory risk?

Question 4: Do you have any information regarding potential costs this may impose on suppliers?

8.1. In this chapter we describe the fifth of seven initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so the threat of switching places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices and to rebuild trust and confidence for those who are not engaged and encourage them to participate.

8.2. This chapter explains how we propose to introduce Standards of Conduct (SOC) into the supply licence. We also outline further details on how the SOC may work in practice. This includes proposals regarding our approach to enforcing the SOC and our expectations regarding supplier action in the context of the SOC. The key aim of the Standards of Conduct proposal is to rebuild consumer trust and confidence in suppliers so they are more confident to engage in the market. We also aim to improve the level of protection available to consumers irrespective of their level of engagement in the market.

Our proposals

Overview of our proposals

8.3. As part of the RMR package, we propose to introduce new SOC, which will require licensed suppliers[171] to treat consumers fairly and require them to take consumer needs into account in all their dealings with them. We consider this will lead to improved supplier behaviour and increased levels of consumer trust in the industry. We expect suppliers to demonstrate they have embedded the SOC into their organisation at all levels of the business. We envisage that over time, the SOC will bring significant changes to the culture and actions of suppliers.

8.4. If suppliers fail to comply with this obligation, Ofgem can take enforcement action. We are proposing to introduce a bespoke policy approach to enforcement for this proposal. We are not intending to include the approach to enforcement within the licence drafting.

8.5. We propose to introduce a new obligation on all electricity and gas suppliers (and their representatives) requiring them to meet a prescribed standard of conduct in all of their dealings with domestic consumers. The SOC are expressed with an overarching objective of treating consumers fairly. The SOC also contain a range of more specific principles including (but not limited to) requirements for suppliers to carry out their actions in an honest, transparent, appropriate and professional manner; and that suppliers provide accurate information and ensure customer service arrangements and processes are fit for purpose. See the draft domestic licence conditions for more information.

8.6. We propose that the SOC licence condition includes an obligation on suppliers to inform customers, on an annual basis, how they will apply the principles outlined in the SOC to their business. This will help consumers understand what specific actions they can expect from a supplier in relation to the SOC. Suppliers, Ofgem and other organisations can help increase consumers' awareness of the SOC, and we will consider how best to provide consumers with a high-level understanding of the Standards of Conduct. We consider this will help to make consumers more aware of the existence, and meaning, of the SOC.

8.7. For the avoidance of doubt, the SOC do not impose restrictions on the level of supply prices that energy suppliers charge as a means of ensuring fair treatment. This exclusion applies to 'Charges for the Supply of Gas/Electricity' rather than all charges.

8.8. Under our proposals, electricity and gas suppliers will be expected to develop and maintain ways of embedding the fair treatment of customers into their business

[171] For the avoidance of doubt, any references to a 'supplier' or 'suppliers' should be interpreted as a reference to a licensed supplier and matters relating to the regulation of licence-exempt suppliers are outside the scope of this document.

processes and management reporting. The required standards and how they should be given operational effect will not be prescribed by Ofgem.

8.9. We propose to provide some clarification about the terminology used in the SOC. This would involve producing limited guidance around existing legal definitions of key terms within the SOC including what we mean by 'appropriate', 'professional manner', etc. This would provide suppliers greater clarity regarding these terms. Suppliers will still be solely responsible for ensuring that the concept of fairness is embedded within their organisation including how this is made operational within their business.

8.10. We also plan to provide further information about how we would expect to apply the definition of 'Representative' in practice, in regard to compliance with the SOC. In summary, whilst we propose using the existing term 'Representative'[172], without prejudice to other licence conditions[173] that use the term, as a matter of policy, we would intend to focus the SOC on more direct and express relationships between a supplier and another person (including chains of sub-delegation arising from such a relationship), such as a person directly appointed as an agent. This is because we feel these relationships are the most important interactions with a consumer. On this basis, depending on the circumstances of the case, we do not generally envisage focusing on the relationships between a supplier and a broker or switching site which may arise via the payment of commission or other indirect arrangements.

Approach to enforcement for the Standards of Conduct

8.11. As the proposed new SOC will be given effect through a licence condition, it will be enforced by the Authority. We are proposing to introduce a bespoke policy approach to enforcement specifically to apply to the SOC. We will take a proportionate approach to investigating issues in line with the criteria set out in chapter 3 of our Enforcement Guidelines[174].

8.12. We propose that our assessment of the seriousness of a potential breach will include consideration of whether a reasonable person, intent on complying with the fairness objective of the SOC, would have acted in the way the supplier did in its interactions with customers. To this end we will have regard to the supplier's actions and considerations (including at senior level) in (i) the development of new policies or processes, and amendments to existing policies and processes; (ii) the monitoring of its implementation of new initiatives and operation of existing policies and processes; and (iii) the taking of remedial action where any adverse consequences for customers came to light. This will mean that we will usually ask suppliers for

[172] Which is defined as 'any person directly or indirectly authorised to represent the [licensed supplier] in its dealing with Customers'.
[173] For example, the marketing licence condition: SLC 25.
[174] For more information, see the following link:
http://www.ofgem.gov.uk/About%20us/enforcement/Documents1/Enforcement%20guidelines%202012.pdf

contemporaneous documents so we can make this assessment before opening investigations.

8.13. Depending on the extent to which we think the supplier can demonstrate via contemporaneous documents that they acted reasonably during all of these stages, we will be more or less likely to take enforcement action. Enforcement action could be based on failings in any or all of these stages. In line with the procedures set out in our Enforcement Guidelines, we propose to consider this in the round with other factors, such as the degree of harm, or potential harm, to consumers.

8.14. We are currently undertaking a review of Ofgem's enforcement policies and procedures, which will take the SOC enforcement approach into account and may lead to further revisions to the Guidelines. We will publish our initial thinking on the review in March 2013.

The role of the Ombudsman Services: Energy

8.15. As set out in chapter 2 of our Enforcement Guidelines, we would not necessarily take enforcement action in light of individual or isolated consumer complaints. Our focus is more likely to centre on systemic weaknesses in suppliers' actions. As Ofgem has limited functions in dealing with individual disputes between consumers and licensed suppliers, we therefore see a role for the Ombudsman Services: Energy (Ombudsman) in applying the SOC when dealing with individual cases referred to it.

8.16. We note that some stakeholders have raised concerns that the approach taken by the Ombudsman could result in setting a form of precedent for supplier actions. The remit of the Ombudsman for energy is not the same as in other industries, for instance financial services. They determine cases individually and treat them on a case by case basis as reflected in their terms of reference[175]. For this reason, we do not consider the Ombudsman would set precedent in their rulings. The Ombudsman is independent and assesses the SOC in a different context to Ofgem (as the independent regulator). Therefore decisions of the Ombudsman do not impact on Ofgem's interpretation of licence conditions. However, we would generally look to work with the Ombudsman to help foster a shared understanding of our objectives and expectations relating to the SOC. This is already part of the Memorandum of Understanding between the Authority and the Ombudsman.

Our reasoning

8.17. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate - drawing on our own evidence and analysis and the evidence drawn from responses to consultation and stakeholder engagement.

[175] Their Terms of Reference say '...the Ombudsman shall not be bound by any legal rule of evidence or by the past conduct or decisions of, or the past Remedies or Awards imposed by the Ombudsman'.

8.18. First, we define the problem – by describing the environment that should prevail for consumers, and explaining how the current environment falls short of that standard, and why these deficiencies are material. We then explain why our updated proposal is an appropriate and proportionate means of addressing the problem identified – by explaining why regulatory action is a relevant consideration, and why we consider our proposal to be the most appropriate form of regulatory action in the circumstances having regard to alternative courses of action.

The problem

8.19. Consumers consider gas and electricity supply to be essential services as they are not products they can easily do without. Therefore, it is important for consumers to have confidence that when they interact in the market they will receive accurate information, can easily contact their supplier and when they do have dealings with their supplier, they will be treated fairly. Issues should be dealt with promptly.

8.20. Our research shows that consumer trust in energy suppliers and the industry is low. Recent qualitative research by Ipsos Mori found that only 6% of consumers say they completely trust their supplier[176]. This was backed up by our recent research which has found that the overall perception of the energy industry is negative and rarely rises above neutral[177]. Moreover, it is not uncommon for consumers to have interactions with energy suppliers that fall short of their expectations or seem unfair. Some consumers are prompted by such experiences to switch supplier.

8.21. We also found that when consumers experience problems with one supplier this can impact negatively on perceptions across the market as a whole. Therefore, for some consumers, interactions with suppliers that do not meet their expectations erode trust in other suppliers and the industry, and can actually act as a barrier to them engaging in the market[178]. Results from our latest research[179] show that, in general, consumers have limited interactions with their suppliers and many consumers felt that they have 'no real relationship with their suppliers'. Therefore, each interaction can have a large impact on a consumer's impression of a supplier and the industry. Moreover, the impact of given interactions can be magnified as consumers also form perceptions of the industry based on experiences relayed by friends and family.

8.22. Concerns around consumer trust in suppliers - whether due to perceptions of unfairness, or other concerns - are a material problem because of the effects on consumer engagement, which contributes to the erosion of overall competitive pressures within the market.

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[176] Ipsos Mori, Consumer Engagement Tracking Survey, October 2012.
[177] Insight Exchange, Consumer research and collaborative engagement on Standards of Conduct – Domestic consumers, October 2012.
[178] Ipsos Mori, Consumer First Panel Year 4, October 2012.
[179] Insight Exchange, Consumer research and collaborative engagement on Standards of Conduct – Domestic consumers, October 2012.

8.23. On this basis we consider it important that the RMR package is designed to improve consumer trust in the energy market and that the principle of fair treatment is fundamental to addressing this problem. In order to have trust in the market consumers expect protections to be in place that require fair treatment[180].

Addressing the problem

8.24. We are proposing regulatory action because voluntary interventions through the existing SOC[181] have not, in our view, addressed the problem or met our original objectives. The original SOC covered the need for consumers to be treated fairly, to have full and accurate information and be helped in trying to find a better deal and switch supplier. Although consumers have noted some improvements, our qualitative research suggests that levels of consumer trust in the energy markets have not improved over the last few years. It is clear that suppliers could do more to fully embrace the spirit of the current SOC. Further, our Consumer First Panel research shows consumers may be negatively impacted by a wide range of contacts with their supplier, many of which are not covered by the existing SOC or current licence conditions.

8.25. As part of our SOC policy, we are proposing to use a principles-based approach to regulation. We think the alternative option of detailed and prescriptive rules for the SOC is impractical as it is likely to be incomplete; it places too much reliance on regulatory design and not enough onus is placed on the behaviour of suppliers. Principles-based regulation allows suppliers to be flexible and innovative in the way they deliver the SOC. It has the benefit of focusing suppliers on what consumers need rather than on understanding how Ofgem interprets a prescriptive rule.

8.26. We are proposing a licence obligation backed by enforcement because the potential reputational and financial costs associated with this will help ensure compliance with the SOC. This also ensures that senior management and Board level attention are given to the SOC. By making the SOC enforceable, we will ensure that suppliers are obligated to successfully deliver the Standards.

Next steps and implementation

8.27. We do not intend to provide suppliers with a transition period within which to implement the SOC. We think it is important for rebuilding consumer trust that the SOC come into force as soon as possible. In line with the positive steps already taken by some suppliers, we would also encourage suppliers to consider taking more immediate steps on a voluntary basis with a view to ensuring that consumers are treated fairly and to help rebuild their trust.

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[180] Ibid.
[181] Energy Supply Probe - Proposed Retail Market Remedies, 7 August 2009.
http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Retail%20package%20-%20decision%20document.pdf

8.28. We expect that over time the proposed SOC should result in very significant changes in culture and practice within supply businesses. It follows, that what is reasonable for a supplier to have accomplished in transforming its processes and systems to meet the fairness principle will change over time. We will take this into account in dealing with any licence breach allegations.

9. Protecting consumers on fixed term offers

Chapter Summary
This chapter sets out our proposal for rules to be applied to fixed term offers in the domestic retail market, particularly regarding automatic contract rollovers and price increases and other adverse unilateral variations. These rules are intended to provide additional protection for consumers and give them more confidence to consider fixed term offers.

Question 1: Do you agree with our proposal for rules to be applied to fixed term offers in the domestic retail market?

Question 2: Do you agree with our proposed strategies to mitigate concerns regarding increases in network charges?

Question 3: Is 30 days the appropriate notification period for mutual variations? Should there be any exceptions to our proposals for mutual variations (e.g. direct debit amount variations)?

Question 4: Are there any expected implementation issues or costs associated with this proposal?

Question 5: Do you agree with our proposed timetable for implementation of our proposal?

9.1. In this chapter we describe the sixth of our initiatives designed collectively to meet the challenges identified through our review of energy retail markets. Our objective is to promote the effective engagement of consumers so stronger competition places an effective constraint on supplier pricing and behaviour. Achieving this objective requires measures to provide consumers with simpler choices, clearer information and fairer treatment so that those who are already engaged in the market can make good choices. It also requires measures to rebuild trust and confidence in those who are not engaged and encourage them to participate.

9.2. This chapter sets out measures to improve consumer trust and engagement in the fixed term market, in particular automatic contract rollovers (‘auto-rollovers’) as well as price increases and other adverse unilateral variations. It should be noted that all the proposals in this chapter are applicable to suppliers and extend to any white label providers of these suppliers.

Our proposal

Automatic contract rollovers and associated measures

9.3. We propose a prohibition on auto-rollovers to fixed term offers. In the absence of action on the part of a consumer[182], the supplier will be required to ensure that the consumer becomes subject to the supplier's[183] cheapest[184] evergreen tariff given their payment method, meter type and whether their access is offline[185].

9.4. Our proposed rules on fixed term tariffs will require that suppliers must offer at least one evergreen tariff for each type of time-of-use (ToU) meter for which they offer a fixed term tariff. This will ensure that any fixed term consumers on a ToU tariff need not be defaulted to a non-ToU tariff. For non-ToU meters, our proposed rules will also require suppliers to provide evergreen tariffs for these[186]. Since our proposed tariff cap is location specific, suppliers would be able to provide appropriate bespoke evergreen tariffs alongside their fixed term tariffs to ensure that certain customers (for example those with exceptionally high energy usage) can be rolled onto an appropriate evergreen tariff.

9.5. We propose a 42 calendar day switching window with no termination fees or notification periods[187].

9.6. In addition, we propose the following rules to ensure that a consumer looking to switch has their prices kept constant during the switching period:

9.7. The consumer would benefit from the same price (i.e. the price of their current tariff, with the supplier from whom they are switching) until the switching has taken place, in the case if within 20 working days after the contract end date, the existing supplier receives notification under industry processes that a new supplier intends to start supplying the consumer within a reasonable period of time.

- This same price will also apply if a consumer enters into a new contract with their current supplier (or another part of the same company group) which comes into effect within 20 working days from the date the fixed term contract ended.

[182] I.e. either expressly agreeing to rollover terms to one of a supplier's open tariffs during the 42 calendar day switching window or entering into a new contract.
[183] For the avoidance of doubt a supplier's tariffs include those of any tariffs of a related 'White Label' provider and vice versa.
[184] Accounting for appropriate discounts.
[185] An offline customer would need to be transferred to an offline tariff. An online customer would be transferred to the cheaper of an offline and online deal.
[186] Furthermore, our proposal for tariff simplification is also relevant to the types of tariff which must be offered by suppliers . See chapter 4 for further information.
[187] I.e. there will be no requirement for the consumer to notify their supplier if they intend to switch supplier.

- The tariff to which a consumer transfers must be one of those available from a supplier's capped core tariff limit, so a supplier will not be able to extend the duration of a closed fixed term tariff.

9.8. At the beginning of the switching window, consumers must receive an 'End of Contract Notification' which complies with the arrangements for these notifications set out in chapter 5. Where a supplier wishes to seek a customer's express agreement to a rollover during the switching window, the notification would have to be combined with additional information, including a statement to make clear that the customer is not obliged to agree.

9.9. We propose to include provisions such that consumers in debt have 30 working days to pay off debts in the event that their supplier objects to them switching, to ensure that consumers in debt could still switch away and receive 'price protection' for the interim period.

9.10. We propose to clarify existing rules for deemed contracts to make clear that consumers cannot be required to give notice in order to exit a deemed contract, cannot be charged (or threatened with) a termination fee for exiting a deemed contract and that a deemed contract may not provide for any fixed term period to which the consumer is bound.

9.11. We propose requiring suppliers to ensure that they have contractual terms that reflect the prohibition on auto-rollovers to fixed term offers and other rules described above.

Price increases and other adverse unilateral variations

9.12. We propose a prohibition on price increases and other adverse unilateral variations on all fixed term offers, with the following exceptions:

- Variations which occur automatically, only in a manner which is fully linked to fluctuations in a published and transparent stock exchange quotation or index, or a financial market rate that the licensee does not control. For the avoidance of doubt, fixed term tariffs linked to a supplier's evergreen tariffs will not comply with this exception.

- Variations which are set out in advance and which are scheduled to occur automatically by a precise amount (or amounts) and on a precise date (or dates), which is not subject to the licensee's discretion.

- A combination of these exceptions[188].

9.13. We noted previously[189] that our proposals could prevent changes in network charges from being automatically passed through to consumers who were on fixed term contracts. We note that our proposal still allows for fixed term tariffs with ex ante automatic variations, which could be synchronised with estimates of expected variations in network charges[190]. We acknowledge this concern, however, and have recently published our decision in relation to mitigating network charging volatility[191]. The measures we are introducing are intended to improve the predictability of allowed network revenues, which will improve suppliers' ability to price network charges into their fixed term offers. In addition, we continue to work with the industry to consider potential improvements to the charging methodologies (including proposed modifications to reduce volatility and increase predictability of charges).

9.14. We recognise that exceptional circumstances may arise where it would be in the interests of consumers for this prohibition not to be applicable, eg where there are significant and unforeseen increases in network costs which are not controllable by suppliers, or where our proposals may limit the introduction of more dynamic ToU arrangements in fixed term contracts[192]. Case by case derogations may be considered by the Authority from the prohibition on price increases and other adverse unilateral variations, where it can be shown that allowing these variations is in the consumer interest; in cases where derogation were granted, the supplier would need to comply with the PIN rules contained within SLC 23.

9.15. In the event of such a derogation, where there follows any price increase or other adverse unilateral variation related to a fixed term offer, we propose that consumers are notified in writing, 30 calendar days in advance, to inform them of the changes[193]. Please see chapter 5 for further details on the information requirements of these notices. These notification rules would also be applicable to all price increases and other adverse unilateral variations, where they relate to evergreen tariffs.

9.16. If the consumer wishes to manage this adverse variation, then they may decide to change to another tariff with their existing supplier or another supplier. If a consumer decided to switch, our December 2011 proposals and our existing rules were intended to ensure a consumer is subject to the current price until the switch

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[188] It should be noted that our proposal for amendments to SLC 23 incorporate the same exceptions for fixed term tariffs, such that variations in price under these exempted tariffs would not require the issuing of a Price Increase Notification (PIN) for each automatic variation.
[189] The Retail Market Review: Draft Impact Assessments for Domestic Proposals, December 2011: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=72&refer=MARKETS/RETMKTS/RMR
[190] These estimates would need to be scheduled to occur by a precise amount and on a precise date.
[191] Decision on measures to mitigate network charging volatility arising from the price control settlement, October 2012: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=CV_Decision.pdf&refer=Networks/Policy
[192] Such ToU arrangements should still be consistent with the consumer protection requirements of the gas and electricity directives, regarding notification of price increases and other adverse unilateral variations.
[193] This is consistent with our proposals from December 2011, as well as the rules already set out in SLC 23.

has been completed. To simplify the process for consumers and allow this policy to work as intended, we propose to:

- Remove the existing requirement for a consumer to notify their supplier of their intention to switch, on or before the date the price increase or other adverse unilateral variation is scheduled to take effect.

- Ensure the price the consumer is subject to during the switching period remains constant by applying the same price protection rules set out above.

9.17. We also propose to clarify existing rules regarding termination fees for fixed term tariffs, to ensure that a consumer would not be subject to a fee for switching supplier in response to a price increase or other adverse unilateral variation. Our intention is to ensure that consumers are always free to leave when a price increase (or other variation) has occurred[194].

9.18. In line with the aims of our clearer and simpler information proposal, and given the possibility that suppliers may seek to agree mutual variations with customers in light of our proposed prohibition on price increases and other unilateral variations, we propose to clarify and tighten some existing rules to ensure that:

- Consumers are notified, in writing, about proposed mutual variations, 30 calendar days in advance (we are aware that this provision may impact on direct debit amount variations and are seeking views on this point).

- Suppliers inform consumers that they are under no obligation to agree to a mutual variation.

- The variation can only be binding following express agreement[195] from, and initiated by, the consumer[196].

- The supplier must confirm any agreement with the consumer, in writing, within five working days (or as soon as is reasonably practicable thereafter).

[194] This is in line with the requirements of the gas and electricity directives.
[195] In December, our proposal was that consumer consent must be 'in writing'; our current proposal is that this consent could take any format.
[196] We are additionally proposing further amendments to SLC 23 in chapter 5, to ensure that a PIN is not triggered following consumer agreement to a proposed mutual variation.

Our reasoning

9.19. In this section we set out our reasoning as to why we consider our proposed action to be necessary and proportionate – drawing on our own evidence and analysis and the evidence drawn from submissions and stakeholder engagement.

9.20. First, we define the problem – by describing the environment that should prevail for consumers, and explaining how the current environment falls short of that standard, and why these deficiencies are material. We then explain why our updated proposal is an appropriate and proportionate means of addressing the problem identified – by explaining why regulatory action is a relevant consideration, and why we consider our proposal to be the most appropriate form of regulatory action in the circumstances with regard to alternative courses of action.

The problem

9.21. Consumers should be able to understand the principal terms of tariffs within the fixed term market and not feel helpless in view of price increases or automatic contract rollovers. The current market is not aligned with this principle[197]. The complexity and risk of taking on a fixed term product also means that only more engaged consumers are likely to take these products. This exacerbates the overall segmentation of the market.

9.22. Common practices with regards to auto-rollovers are undermining consumer engagement in the market[198]. These practices include:

- 'Opt-out' approaches to auto-rollovers which risk consumers being placed on to unsuitable fixed term offers. Since these fixed term offers have termination fees consumers can become effectively 'locked in'. These practices also allow suppliers to offer initial attractive deals to consumers, with the expectation to rollover these consumers on to contracts with less favourable terms.

- Not all consumers are given adequate notice periods to assess their options and switch supplier should they decide to.

- In general, the principal terms and conditions a consumer can expect at the end of their contract are unclear in suppliers' marketing materials, the contract's terms and conditions and/or communications at the point of sale.

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[197] See our draft Impact Assessment.
[198] As set out in our Consultation on practices concerning Fixed Term Offers, January 2011, Reference (09/11): http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=110&refer=Markets/RetMkts/Compet

- Suppliers' practices vary from one another. The lack of homogeneity among the fixed term tariff practices contributes to increase the complexity of the retail energy market.

9.23. As indicated in our consumer research[199,200], consumers lack a full understanding of fixed term tariffs and feel helpless in view of price increases and other adverse unilateral variations. We previously undertook tariff comparability research to explore options for presenting tariffs. Our qualitative research[201] indicates that consumers generally assume that fixed term tariffs are also fixed price, and therefore may misunderstand the terms of their contract and how these could vary. Some consumers also had concerns about being 'locked in' to contracts and facing termination fees. These factors adversely affect trust, comparability and engagement in the market.

9.24. In addition, we have concerns that many tracker tariffs in the current market are not in alignment with general consumer protection legislation[202] and the provisions set out in SLC 23 regarding notification of price increases and other adverse unilateral variations.

Addressing the problem

9.25. In view of these concerns regarding fixed term offers, we are proposing several measures to provide additional consumer protection and improve trust in, and understanding of, the fixed term market. We have considered a range of alternative options to our proposal.

9.26. Our analysis has been informed by consultation responses to our December 2011 consultation. Responses (both from suppliers and other groups) were broadly in favour of the policy intent in our December proposal, with some disagreements regarding implementation of these proposals[203]. In view of this analysis, as well as responses received, the proposal included in this chapter remains broadly similar to that presented in our December 2011 document.

9.27. We have considered a range of less prescriptive policy alternatives to implementing a prohibition on auto-rollovers to fixed term offers, such as regulating the length of the rollover contract period, or relying on improving existing rules around fixed term offers. However, none of these alternatives could address the negative impact of auto-rollovers on consumer engagement and competition in the fixed term market.

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[199] Consumer First Panel Year 4, February 2012: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=53&refer=Sustainability/Cp/CF
[200] Ipsos MORI, Customer Engagement with the Energy Market - Tracking Survey 2012, October 2012.
[201] Tariff Comparability Qualitative Research, December 2011: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=72&refer=Markets/RetMkts/rmr
[202] E.g. 2009 Gas and Electricity Directives, and the Unfair Terms in Consumer Contracts Regulations 1999.
[203] For a more detailed review of responses, see our draft Impact Assessment.

9.28. We have also considered a range of alternative options to our proposals for price increases and other adverse unilateral variations. These options were intended to ensure the alignment of fixed term offers with relevant consumer protection legislation as well as SLC 23 (e.g. through issuing guidance or specific licence provisions, but not a full prohibition). However, under these alternatives, consumers may still be exposed to tariffs which are misleading or misunderstood.

9.29. This proposal should provide predictability and additional protection for consumers as well as improving trust in, and understanding of, the market. In doing so, we hope to build consumers' confidence to engage with the fixed term market. Our proposal should reduce barriers for consumers accessing fixed price products, thereby providing potential certainty to those consumers. Our Impact Assessment indicates that we expect the benefits to outweigh any adverse impact or unintended consequences.

Implementation

9.30. This proposal will be applied through amendments to current standard licence conditions. Draft amendments have been included in our draft domestic licence conditions. The timetable for subsequent implementation is discussed below.

Implementation processes

9.31. We recognise that there may be implementation issues and costs for suppliers, associated with implementing these measures, particularly in terms of altering the fixed term offers they present to the market.

Timetable

9.32. Subject to consideration of responses to this consultation, we envisage proceeding with a consultation on final proposals (including statutory consultation on licence modifications) in spring 2013. On this basis, subject to consultation responses, we would envisage that licence modifications and other proposals would come into effect[204] from summer 2013.

9.33. We propose that new fixed term contracts that are signed on and from the date of the licence modifications coming into effect would be required to comply with our proposed rules for fixed term offers.

9.34. We are proposing that implementation of these rules in the terms and conditions of any fixed term offers, available to new and existing customers, must be completed by suppliers and they must have practices in place to fully reflect

[204] This incorporates the 56 day period required by legislation before a licence modification can come into effect.

applicable fixed term rules, within six months of the new/amended licence conditions coming into effect.

9.35. Any existing contracts expiring within this six month period should be subject to the proposed prohibition on auto-rollovers to fixed term offers. Consumers should be transferred onto contracts reflecting the rules proposed in this chapter. Our proposed rules regarding price protection, termination fees and notification periods during the 42 calendar day switching window should be adhered to in this transitional period.

10. Market Cheapest Deal

Chapter Summary

This chapter sets out our early thinking on how the Market Cheapest Deal scheme might work, were it to be implemented. We propose to work with stakeholders to develop the details of the scheme so that suppliers and others can work with us to trial it later next year.

Question 1: Do you agree that we should trial a Market Cheapest Deal initiative?

Question 2: Do you consider there are other approaches we should consider to address the particular issues with engaging sticky and/or vulnerable consumers? If so, what are they?

Question 3: Would you be willing to work with us in conducting the trial?

Developing the Market Cheapest Deal scheme

10.1. There are a number of logistical and practical challenges we would need to answer before we could move to implement an initiative that aims to provide a sub-set of customers with personalised information on the cheapest tariffs for them.

10.2. Firstly, we would need to consider which customers should receive this information. Our working assumption is that to begin with, this initiative would be targeted only at the most sticky customers (for example, those who have been with their current supplier for more than 3 years) and some categories of vulnerable customers (for example, those in receipt of the Warm Homes Discount).

10.3. We also need to consider how 'cheapest deal' is defined. Here our working assumption is that we would use the same rules that we propose for the Supplier Cheapest Deal policy set out in chapter 6 in this document. Our view at this stage is that eligible consumers should be given information about several (2 or 3) of the cheapest tariffs in the market based on this narrow definition. That is, where the cheapest deal is based on the customer's consumption level, meter type, payment method and respects their decision to manage their energy account off-line, where this is the case. They should also be told of the cheapest deal available across the entire market using the 'wide definition', that is, if they were prepared to switch payment method and/or go online.

10.4. We then need to consider how the relevant information would be collated and transferred within this scheme. This is where Data Protection and other legislation need to be considered, as well as practical and cost issues. Our initial view is that:

- Suppliers might be required to provide information about their tariffs to a database held centrally by a third party. This central agent would build and ensure the accuracy of a model using rules agreed with Ofgem, to allow the calculation of the cheapest market deals based on any particular customer's information[205];

- Suppliers would be required to insert the details of eligible customers into this model on an annual basis, with the model generating the cheapest deal information for each supplier; and
- Suppliers would then be required to pass this information to their eligible customers, along with prescribed associated messaging and signposting to switching services.

10.5. This outline approach needs further development. Questions remain, for example on:

- whether the most appropriate messenger for this information is the supplier or whether suppliers should only act as a post box, with the message coming from another source, such as a consumer organisation;
- who pays for, and the governance/ownership of, the central agency;
- how much the scheme is likely to cost.

10.6. As part of the roll-out of smart metering, the government intends to appoint and licence a Data and Communications Company (DCC) to procure and manage all communication of data to and from smart meters in domestic premises. It may be possible for this body to play a role in enabling suppliers to identify the Market Cheapest Deal for their customers. We will explore this option as we develop our thinking on this proposal.

10.7. While there are many questions to answer, the arrangement sketched out above illustrates that there may be a way to implement a scheme of this nature without suppliers breaching Data Protection legislation (for example regarding customer consumption and address details) and without suppliers sharing price information or being able to manipulate the information which is presented to eligible consumers. This arrangement is also consistent with and recognises the limits on Ofgem's vires in respect of providing advice to consumers.

10.8. Given the challenges associated with such a scheme, we will be looking to work with the industry and relevant third parties to trial a Market Cheapest Deal initiative. We propose to set up a working group to design the scheme. Once we have a design in place, and before deciding whether to implement the scheme, we would work with industry to set up a trial of the initiative. The primary purpose of the trial will be to understand how effective the scheme will be in increasing effective engagement for the consumers at which the initiative is targeted. The trial should

[205] We note the job of the central agent will be made simpler if our proposal to cap the number of tariffs per supplier is implemented.

also help us better understand the likely cost of the scheme and in finalising the details of how the scheme should work.

Alternatives and complementary ideas

10.9. We have considered whether there are other approaches to assisting the most sticky customers engage in the market. We think that the creation of one stop shop advisory services may go some way towards meeting our objective, but are concerned that without clear information on the personal savings they will make from switching, sticky customers may not make use of these services. We also consider that there may be ways in which technological developments and initiatives such as MIDATA could be used to get relevant information and support to the stickiest customers. However, we would be concerned that any scheme which relies on consumers opting in to share their consumption data, (for example with a switching site in order to receive Market Cheapest Deal information) might weaken the effectiveness of the scheme in obtaining engagement from the most sticky and vulnerable consumers.

10.10. We welcome respondents' views on how alternative arrangements might work and will consider these ideas as we take our work in this area forward.

Appendices

Index

Supplementary appendix (published separately) – 135a/12

Draft Impact Assessment for the updated domestic proposals (published separately) – 135b/12

Draft domestic licence conditions for the Retail Market Review proposals (published separately) – 135c/12

Appendix 1 - Consultation Response and Questions

1.1. Ofgem would like to hear the views of interested parties in relation to any of the issues set out in this document.

1.2. We would especially welcome responses to the specific questions which we have set out at the beginning of each chapter heading and which are replicated below.

1.3. Responses should be received by **21 December 2012** and should be sent to:

- RMR@ofgem.gov.uk
- Retail Markets
- Ofgem
- 9 Millbank
- London
- SW1P 3GE

1.4. Unless marked confidential, all responses will be published by placing them in Ofgem's library and on its website www.ofgem.gov.uk. Respondents may request that their response is kept confidential. Ofgem shall respect this request, subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.

1.5. Respondents who wish to have their responses remain confidential should clearly mark the document/s to that effect and include the reasons for confidentiality. It would be helpful if responses could be submitted both electronically and in writing. Respondents are asked to put any confidential material in the appendices to their responses.

1.6. Next steps: Having considered the responses to this consultation, Ofgem intends to design our final proposals. Any questions on this document should, in the first instance, be directed to:

- David Hunt
- Retail Markets
- Ofgem
- 9 Millbank
- London
- SW1P 3GE

CHAPTER: One

There are no questions in this chapter

CHAPTER: Two

Question 1: Do you agree with our characterisation of the problems in the retail energy market?

Question 2: Do you agree with the findings of our evidence base?

CHAPTER: Three

Question 1: Do you agree with our rationale for the proposed RMR package?

Question 2: What are your views on the proportionality of the proposed RMR package in the light of the evidence we have presented?

Question 3: Do you agree with our reasons for not proceeding with the alternative options set out below?

CHAPTER: Four

Question 1: Are our rules to reduce the number of tariffs appropriate? Have we set the cap on core tariffs at the right level? Should a different cap be set for time of use tariffs? What derogations from our tariff cap would be appropriate?

Question 2: What surcharges should suppliers be able to offer without this counting as an additional core tariff, and why? How could these be defined in a licence?

Question 3: Are our rules to simplify tariff structures and discounts appropriate? Should they only apply to open tariffs or be extended to cover dead tariffs too?

Question 4: What categories of dead tariffs should be derogated from our proposals, if any? Are any other measures required to avoid any consumer harm?

Question 5: What would be the implementation issues and costs of our proposals?

Question 6: Is our proposed timeframe for implementation appropriate?

CHAPTER: Five

Question 1: What are your comments on the degree of prescription proposed, and on the design of the documents and messaging?

Question 2: What are your views on the appropriateness of content requirements for each of the communication channels?

Question 3: Should Ofgem explore further ways in which suppliers might increase the effectiveness of online/paperless communications?

Question 4: Should Ofgem consider making further recommendations, or issuing best practice for enhancing the impact of Annual Statements by looking at messaging and co-branding of envelopes?

Question 5: Do you agree with the view additional contractual information can be included on an additional page on the Annual Statement?

Question 6: What are your views on the classification of duel fuel for the purposes of the template designs?

Question 7: What are your views regarding including energy efficiency advice in Annual Statements?

CHAPTER: Six

Question 1: Do you agree with our view that the cheapest tariff message should include both supplier's cheapest tariff for their payment method, consumption and meter type, and the cheapest overall tariff from their supplier irrespective of their current circumstances, personalised by consumption?

Question 2: Do you agree with the approach to tariff eligibility criteria proposed for supplier's cheapest tariff?

Question 3: We seek views from stakeholders on whether consumers with smart meters and any relevant time-of-use tariffs that the supplier is offering require separate consideration in relation to this policy proposal.

Question 4: Do you have any suggestions regarding additional rules which they consider relevant for the construction of the cheapest tariff messaging?

CHAPTER: Seven

Question 1: Do you agree with our proposal to introduce a price comparison tool?

Question 2: What is your view about the terminology we are proposing for the two price comparison metrics? Are they clear and easy for consumers to understand?

Question 3: In your view, does our proposal for the TCR strike an appropriate balance between different trade-offs in terms of simplicity, accuracy, confusion and saliency? Please explain the reasons for your view.

Question 4: Do you agree with our proposal for the different features of the Tariff Comparison Rate, and our related proposal on the personal projection? Do you have any thoughts on whether and how time of use tariffs should be accommodated in the TCR and personal projection? Please explain the reasons for your view.

Question 5: In your view, should suppliers be required to make available up to date information on TCRs for their tariffs? What is your view on the barriers to the publication of best buy tables, and how could we better facilitate publication by third parties?

Question 6: Do you have any concerns regarding the implementation of this proposal? How long after a decision has been made would you take to implement this proposal? What drives those timescales?

CHAPTER: Eight

Question 1: Do you agree that the revised Standards of Conduct (SOC) will help achieve our objectives?

Question 2: Is there a different name for the SOC that will have more meaning to consumers and can be used by stakeholders across the industry?

Question 3: Does our approach to enforcement mitigate stakeholder concerns about clarity and regulatory risk?

Question 4: Do you have any information regarding potential costs this may impose on suppliers?

CHAPTER: Nine

Question 1: Do you agree with our proposal for rules to be applied to fixed term offers in the domestic retail market?

Question 2: Do you agree with our proposed strategies to mitigate concerns regarding increases in network charges?

Question 3: Is 30 days the appropriate notification period for mutual variations? Should there be any exceptions to our proposals for mutual variations (e.g. direct debit amount variations)?

Question 4: Are there any expected implementation issues or costs associated with this proposal?

Question 5: Do you agree with our proposed timetable for implementation of our proposal?

CHAPTER: Ten

Question 1: Do you agree that we should trial a Market Cheapest Deal initiative?

Question 2: Do you consider there are other approaches we should consider to address the particular issues with engaging sticky and/or vulnerable consumers? If so, what are they?

Question 3: Would you be willing to work with us in conducting the trial?

Appendix 2 – Glossary

A

Annual Statement

A written document that suppliers must provide to each customer, each year. The Annual Statement contains a range of key tariff information, including tariff name, consumption over the previous 12 months, estimate of annual cost for the next 12 months and details of any premium or discount that applies to the tariff.

Automatic contract rollover (‘auto-rollover’)

Where, due to the terms of a contract, a supplier has the ability to extend~~s~~ the duration of an existing Fixed Term tariff or apply a new Fixed Term tariff without consumer’s positive assent.

Annual Bill

The amount that a customer would have to pay for gas and/or electricity over one whole year.

Authority

The Gas and Electricity Markets Authority

B

Barrier to entry

A factor that may limit a firm’s ability to enter the market.

Barrier to expansion

A factor that may limit a firm’s ability to increase in size.

Big 6

The name collectively given to the six companies that hold supply licences and supply most of the energy to domestic households in the GB market. They are: Centrica plc (three retail brands, British Gas, Scottish Gas and Nwy Prydain in England, Scotland and Wales respectively), E.ON UK, Scottish and Southern Energy (SSE), RWE npower, EDF Energy and ScottishPower.

Bundled Products (Bundles)

An ‘opt in’ bundle for the purpose of this proposal is when consumers can add on additional services/products to their energy offering.

A 'tied' bundle for the purpose of this proposal is a form of pure bundling where it is tied/mandatory to buy the entire bundle to receive all the products and services offered, i.e. the specific energy offering is only available with this particular bundled form.

An 'opt out' bundle for the purpose of this proposal is a when a consumer is presented with an entire bundled product and they are required to 'opt out' of the additional services if they wish to only purchase the energy element of the bundle or if they wish to 'opt out' of any one of the elements of the bundled product.

C

Code of Practice

A set of guidelines and principles to be followed by members of some profession, trade, or group. In this case, energy suppliers.

Cooling-off period

Usually refers to a period of time after the consumer has entered into a contract or signed up to a tariff during which they can reverse their decision without incurring any cancellation fees.

Core tariff

The charges for supply of electricity/gas combined with all other terms and conditions that apply, or are in any way linked, to a particular type of contract for the supply of gas/electricity to a domestic customer excluding certain matters such as dual fuel discounts, variations in charges relating to payment method, appropriate surchages and optional additional services.

Cross subsidise

The part financing of one product or activity by another.

D

Dead tariff

An Evergreen Tariff that is not an Open Tariff.

Deemed Contract

A contract deemed to be in place pursuant to paragraph 8 of schedule 2B to the Gas Act 1986 and/or paragraph 3 of schedule 6 to the Electricity Act 1989, e.g. where a customer takes a supply of electricity and/or gas otherwise than under a contract that has been expressly entered into with a supplier.

Department for Energy and Climate Change (DECC)

The UK government department responsible for policy in the fields of energy and climate change.

Derogation

An exemption from or relaxation of a rule.

Direct debit (DD)

A method of payment where a fixed or variable amount is taken from a bank account each month, quarter or year.

Domestic customer

A customer that uses energy for non-commercial purposes.

Domestic energy suppliers

Companies who sell energy to and bill domestic customers in Great Britain.

Dual Fuel (DF)

A type of energy contract where a customer takes gas and electricity from the same supplier.

Dynamic Teleswitching (DTS)
A particular type of electricity meter where the tariffs have a control unit that allows the supplier (or distribution company) to switch the metered supply remotely by radio teleswitch. The Radio Teleswitching Access Provider controls the radio switches, and therefore heating load, following instructions from the supplier.

E

Economies of scale

Where the average costs of producing a good or providing a service falls as output increases.

Economy 7 / Economy 10

A type of tariff that has different unit rates for consumption during the day and during the night. The number following 'Economy' refers to the number of hours for which night-time rates are available.

End of Contract Notification

A communication from a supplier to a consumer, indicating that the fixed term period of the consumer's energy supply contract is due to expire, and setting out the arrangements that the consumer will default to and the options available to the consumer to act in response to this notification.

Evergreen contract

A supply contract of indefinite duration which may be terminated by the customer by giving notice in accordance with the contractual terms, e.g. 28 days' notice

Ex-PES

The previous Public Electricity Supplier (PES) for one of the 14 electricity regions in England, Wales and Scotland. From privatisation in 1990 until 1998 the ex-PES had a monopoly of electricity supply and distribution in their designated areas. Local distribution is still a monopoly regulated by Ofgem, however, competition has been introduced in supply, and so these 14 suppliers (consolidated now into five) are known as ex-PES suppliers. The 14 regions are detailed below, together with the name of today's ex-PES company for each region.

Region	Supplier Group
London	EDF Energy
Seeboard	
SWEB	
East Midlands	E.ON UK
Eastern	
Norweb	
Midlands	RWE npower
Northern	
Yorkshire	
Scottish Hydro	SSE
Southern	
Swalec	
Manweb	Scottish Power
Scottish Power	

F

Fixed price tariff

A tariff that guarantees that the price paid per unit of gas or electricity used will not change for a given period of time.

Fixed term tariff

A tariff with a fixed end date.

Fuel poverty

Those households who need to spend more than 10 per cent of their annual income on fuel to maintain an adequately heated home are considered to be in fuel poverty.

G

Green Deal

A scheme that allows householders to improve the energy efficiency of their homes and repay the cost through energy bills.

Green tariff

A tariff that is promoted primarily on the basis of its association with renewable energy sources and/or climate change mitigation

I

In-area customers

Customers of an electricity supplier who are located within the supplier's original ex-PES region.

Incumbent suppliers

See ex-PES suppliers

Intermediary

An organisation that can help consumers to switch energy tariffs

K

kWh

Kilowatt-hour is a unit used to measure energy consumption in both electricity and gas.

L

Loyalty discount

A discount that is paid at a pre-specified point in time if the consumer does not switch energy suppliers.

M

Market Segmentation

The process of splitting customers, or potential customers, in a market into different groups, or segments.

Market Share

The proportion of total customers (usually as proxied by the number of meter points) within a market that are registered to a particular supply group.

Mutual variation

An amendment to the terms and/or conditions (including price) of a consumer's energy supply contract, agreed with the consumer. The consumer would not be obliged to accept the proposed variation. The variation can only be binding following express agreement from the consumer.

MWh

A megawatt hour. Equal to 1000 kWh.

N

New entrant

An entrant that does not have an incumbent customer base.

Non Time of Use tariff (Non-ToU)

A tariff that is not a Time of Use (ToU) tariff.

O

Office of Fair Trading (OFT)

The body established by the Enterprise Act 2002 (which replaced the office of Director General of Fair Trading) with functions that include enforcing consumer protection law and competition law, reviewing mergers and conducting market studies.

Ombudsman Services: Energy

Ombudsman Services: Energy means the Ombudsman Services provided to Energy Suppliers and Energy Network Operators. The Ombudsman's principal aim is to receive complaints made by complainants in accordance with the *Ombudsman Services Terms of Reference* and to consider and, where appropriate, investiage such complaints in order to encourage and/or facilitate the terms of their resolution, settlement and/or withdrawal.

Online tariff

A tariff for the supply of electricity/gas which may only be entered into via a website, and/or a tariff which must be managed fully or partly by a customer via a website.

Open tariff

A Tariff that is available to new and existing customers at any given time.

Out-of-area customers

Customers of an electricity supplier who are located outside of the supplier's original ex-PES region.

P

Personal projection

The estimated cost of energy to a consumer over a 12 month period, based on a specified methodology and the best available information about that consumer’s consumption.

Pre-payment

A method of payment where consumers pay for credit to their account. Their meter deducts credit from the account based on the amount of energy used by the consumer and the rates that apply to the consumer’s tariff.

Price Increase Notification (PIN)

If a supplier increases the price of a tariff, then under Ofgem’s licence obligations it must notify the consumer at least 30 days in advance of the date on which the price increase takes effect.

S

Self regulation

Industry regulation without Ofgem’s binding licence conditions. However, if self regulation is not operating as Ofgem would hope, licence conditions may be introduced.

Smart meter

A meter that provides measured gas or electricity consumption data for multiple time periods, and is able to provide the relevant supplier with remote access to such data.

Small suppliers

Suppliers which operate in the domestic gas and electricity market but do not hold significant market share. This can refer to all suppliers other than the Big 6.

Standards of Conduct (SOC)

A written policy and procedure that outlines broad standards of integrity and business ethics.

Standard credit

A method of payment where the consumer receives a bill for their energy use over a number of months and pays their bill by cash or cheque.

Standing charge

In respect of the supply of gas/electricity to a customer's premises, a monetary amount that is continuously chargeable to a customer on a daily basis and which is chargeable in addition to charges arising on the basis of a unit rate.

Standard Licence Conditions (SLCs)

The legally binding conditions that licensed gas and electricity suppliers must meet to supply to domestic and non-domestic customers, in accordance with the Gas Act (1986) and Electricity Act (1989).

Surcharge

An additional and exceptional charge added to the usual charge(s).

Switching

The process of changing gas or electricity supplier, or changing to a new tariff with the same supplier.

Switching window

The period in which a consumer is eligible to switch supplier, in response to an End of Contract Notification, in which they will not be subject to any Termination Fees or be required to notify their supplier of their intention to switch.

T

Tariff

The charges for supply of electricity/gas combined with all other terms and conditions that apply, or are in any way linked, to a particular type of contract for the supply of electricity/gas to a domestic customer.

Tariff Comparison Rate (TCR)

A metric that would allow consumers to compare the price of energy tariffs on a like-for-like basis.

Tariff Information Label

A table of key facts that would allow consumers to compare the price and non-price features of energy tariffs on a like-for-like basis.

Tariff Structure

The way in which a tariff's charges are structured. For example, some tariffs have a single unit rate whilst others have more than one unit rate (multi-rate).

Termination (exit) fees

Where part of their contract, these are the contractually agreed price a customer must pay if
they terminate their contract before the agreed contract end date.

Third Package

The term 'Third Package' refers to a package of EU legislation on European electricity and gas markets that entered into force on the 3rd September 2009. The purpose of the Third Package is to further liberalise European energy markets. DECC is primarily responsible for its transposition in Great Britain and must do this by the 3rd March 2011.

Time of Use tariff (ToU)

A tariff where the charges vary by the time when the energy is consumed, for example through different unit rates for energy consumed during the day and during the night.

Tracker tariff

Currently, this is a tariff where the price per kWh for gas/electricity will vary in reference to other prices or indices. This can be for example the price of another tariff from another supplier. In this consultation we are proposing to change the scope of fixed term tracker tariffs. These tariffs will no longer be able to track the price of tariffs offered by suppliers, but only a published stock exchange quotation or index or a financial market rate over which the supplier has no control.

U

Unilateral Variation

An amendment to the terms and/or conditions (including price) of a consumer's energy supply contract, which is provided for in the contract and is at the sole discretion of the supplier.

Unit Rate

The monetary amount that is chargeable in respect of each unit of gas/electricity consumed.

V

Variation

An amendment to the terms and/or conditions (including price) of a consumer’s energy supply contract.

W

White label tariff

A tariff offered by a licensed energy supplier but uses the brand name of a non-licensed entity (excluding a brand name of the corporate group to which the licensed supplier belongs). The price and terms of the tariff may replicate those of the licensed supplier or may be modified to suit the specific needs of the brand. The legal relationship between the customer and the licensed energy supplier remain unchanged irrespective of the brand utilised for sales and marketing purposes

Appendix 3 - Feedback Questionnaire

1.1. Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Please add any further comments?

1.2. Please send your comments to:

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