

Tim Jarvis
Director General
Ofgem

30 August 2024

RE: Standing Charges: domestic retail options – Call for Input

Dear Tim,

Please see below for my response to the specific questions raised in this call for input. I have provided to answers where I think my input may be useful, and put N/A where I have no relevant commentary on the question. Prior to providing those answers, I want to take the opportunity to say how pleased I am to see Ofgem taking onboard the views of consumers and consulting on moving certain costs away from standing charges and on to unit rates.

As your document states, this is just a shuffling of costs which will benefit some while negatively impact others, but it provides more freedom to low-income, low-usage households to take control of their energy bills.

I will say that I hope this is only the start. A £20-£100 shift is a good beginning but standing charges are almost £350 per year at the moment, up from less than £100 pre-crisis. I'd like to see further consultations for moving more of the costs back to unit rates in the future.

Additionally, I'd be remiss if I didn't highlight that over 350,000 people signed a petition calling for the removal of headroom allowance and for a reduction in profits in the energy market. The End Fuel Poverty Coalition investigation that found over £420bn in energy industry profits across a 5 year-year period highlights that we as a nation are being taken for a run by energy giants and it is Ofgem's job to stop this kind of profiteering. On this point, I'd like to remind you that a price cap which gives a positive % of other costs as a calculation for the EBIT allowance invites a high-cost market, as suppliers are not incentivised to reduce their costs if it just means lower profit levels. This effect was perfectly displayed during the peak of the crisis, when everyone was struggling the big energy suppliers saw profits rocket. This effectively pits suppliers against consumers.

The current EBIT calculation has a floor of c.£20 plus a 1.1% addition of the other costs in the cap, per household. This intuitively incentivises energy suppliers to keep their costs high, as they will receive higher profit allowances under the price cap. A fairer and better calculation for EBIT would be to provide a cap (say £50) and then deduct a percentage of costs, therefore as costs reduce across the energy supply industry the allowance for EBIT would increase. This would incentivise suppliers to lower their costs. This sort of system is exactly how almost every other industry in the world works, lower costs = higher profits.

If you'd like to discuss this proposal further, please contact me at Richard@TheRegulatorGuy.co.uk.

Kind regards,

Richard Winstone
The Regulator Guy



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Responses to the questions posed

Question 1: Do you have any views on our case for change?

Yes, I agree that standing charges need to come down. I do not agree that £20-£100 is enough, but I am hopeful that you'll lean far more toward the £100 than the £10 proposed change. A customer can only have so much control over their energy bills when they are forced to pay almost £1 per day just to be connected to the grid. This is especially damaging for low-usage households who find it near impossible to reduce their consumption any further.

I'd like to see household standing charges be reduced back to the previous levels of around £100 per year. I know that this would push costs onto usage charges, and I am also aware that there are some high-usage, low-income households that would be negatively impacted, but as per one of your previous consultations, there are around 5 million low-income, low-usage households that would benefit from these changes and only around 1 million low-income, high-usage households that would be negatively impacted. It is your responsibility to work with government to ensure reasonable support is offered to those on low-incomes with high-usage and then to set the cap to a level that supports to majority of the population.

Question 2: What are your views on the range (£20-£100) of operating costs we are considering shifting from standing charges to unit rates? Should it be higher? Within this range, is there a value you would favour and why?

As stated previously, my feelings are that this is not enough of a change, we'd be better seeing £150-£200 being moved from standing charges to unit rates. This would mean looking at the network costs in the electricity standing charges and making adjustments to moving them to unit rates. It feels odd that electricity standing charges are almost twice the size of gas standing charges, but you're proposing to move twice as much away from gas standing charges than electricity standing charges.

Additionally, we need some commitment from Ofgem that standing charges aren't going to creep up again by adding further costs to the price cap. Since the beginning of the crisis, Ofgem have added or increased around 20-25 costs in the price cap. Most reviews of elements of the cap seem to result in a statement saying "it was miscalculated back in 2019, we're increasing it". Some of these costs have been one-offs, some have been temporary which later become merged into another cost and some are just permanent changes. A portion of them have been added as additional costs to the standing charges. If this pattern continues we could see standing charges creep back up toward the £1 per day value, so we need commitment from Ofgem that this won't happen.

Question 3: What are your views on the trade-offs and impacts we have identified for consumers and suppliers? Should any of these take more or less significance in our assessment, and are there any important impacts we have not considered?

Customer impacts

I find a few things interesting from this analysis. Firstly, you identify that low-income households realise the largest income-weighted gains from reductions in standing charges. This is intuitively obvious and feels like it should be used as a justification for further moves from standing

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charges to unit rates, allowing low-usage households to actually take control of their extreme energy bills.

Secondly, you've provided a variety of numbers, but no access to the original data, making it difficult to verify the information being given. I have no idea how you figured out that 3.7m people would receive a reduction of -£4 to -£19 on their annual bills, but I will say that if more people benefit than suffer from a change, and there isn't an extreme negative for those that are worse-off after the change, then the change should be implemented and new consultation should begin to see how we help those that are now struggling more with their energy bills.

In response to comments regarding low-income households with health-related high energy usage. Whilst I obviously do not want to see their bills increase, it is worth noting that this particular group of people receive various pieces of government support to assist with the fact that their energy bills are higher, such as the warm home discount, winter fuel payments (although there is obviously some controversy on this at the moment), cost-of-living payments etc. I'm not saying to discount the affects of these changes on this group of people, but the additional financial support that they receive over low-income, low-usage households should be considered when discussing moving standing charges to unit rates.

Supplier impacts

My first comment is that the use of the phrase "reasonable profit" being littered over Ofgem documentation over the last 6 months is insulting to all consumers, especially after you started a consultation process to reduce the excessive profits back in 2021 and concluded that consultation in 2023 with a decision to increase the profit allowance for suppliers. Profits are not reasonable at the moment partially due to decisions you've made, so, by your own definition, Ofgem is failing at its core responsibility.

Secondly, I do not agree with a reconciliation mechanism. If a supplier begins to suffer because their customer mix isn't conducive to profitability after this change has been made, then that is a commercial issue that Ofgem shouldn't be involved in. The supplier would then be motivated to offer tariffs that incentivise high-usage customers away from competitors, this is known as "competition", which is something we've seen very little of in the energy supply market over the last 3 years.

Question 4: What are the changes required, if any, to the price cap to facilitate a reduction in the level of the operating costs charged through the standing charge?

As mentioned previously, you need to incentivise suppliers to reduce their operational costs. These costs are reported to Ofgem and are used in calculating the price cap figures. They are also used in calculating the EBIT allowance and Headroom allowance, which are calculated a percentage of other costs (including these operating costs) added together. You incentivise suppliers to keep their operating costs high because they can get higher EBIT and headroom allowances by having higher costs (the costs are passed on to consumers in the price cap anyway). If you want to reduce operating costs in the energy supply market then you need to have a cap that ensures suppliers make a loss when their costs are too high, as every other company in every other industry experiences. The current system is a cash cow for large energy suppliers that can absorb short term costs.



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Question 5: Could mandating suppliers to have at least one low or no standing charge tariff available to customers help promote competition in this area of the market?

Yes, this seems like a great idea. Suppliers should also be mandated to offer at least 1 fixed rate tariff at all times, allowing customers that want certainty over their energy bills the opportunity to secure a deal. This tariff doesn't necessarily need to be cheaper than the current price cap level.

Question 6: How could we create flexibility in how costs are recovered between the unit rate and standing charge without reducing the protection provided by the cap?

N/A

Question 7: In enabling greater diversity in standing charges on default tariffs, what, if any, safeguards would be needed to protect vulnerable consumers?

Many vulnerable customers are low-income, they need protection from the current price cap prices, which are focused on increasing investment in our energy supply market. Reducing, or even removing, the standing charges will enable these customers to exert control over their energy bills.

The price cap needs to become less about profit and more about protecting customers, which means reversing many of the decisions Ofgem have made over the last 3 years.

Additionally, we need a more rapid return to a competitive market in the energy supply sector. The extension of the BAT limits this, as does the high barriers to entry for new entrants to the energy supply sector. I completely understand that we do not want another market with too many suppliers that are not financially stable and collapse under extreme circumstances, however Ofgem have over-corrected and ended in a market that sees the Big 6 having over 90% market share again, up from less than 60% prior to the energy crisis. This gives them monopoly powers in the market and puts them in a position not to require acquisition of new customers as there aren't customers flooding away from them. Overall, I believe that a competitive market needs to be a priority for Ofgem and that competition needs to be focused on tariff prices rather than customer service standards (although this work should still continue).

Question 8: What are the key considerations we should take into account in developing options for smoothing spend for prepayment meter customers?

N/A

Question 9: Do you have any views on our considerations for the allocation of network and policy costs?

I am concerned that Ofgem are not considering reviewing DUoS residual charges and instead are hoping and praying that these costs will reduce in future years anyway. Expectations cannot be trusted, in paragraph 5.7 you acknowledge that networks costs increased much faster than 2019 forecasts, which is why we have such extortionate standing charges now. We need Ofgem to be more proactive and change things if they are not right today. This means not hoping that the DUoS charges drop off in future years and instead consult to limit them now, identify what is



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causing excessive charges for consumers and take action to ensure consumers are actually protected.

I'd like to see network and policy costs more fairly distributed to unit rates, but I'd also like to see them reduce. That being said, I understand that network costs are likely to increase in the coming years. To allow consumers the freedom to control their energy bills, it'd be beneficial for these network costs to be moved to unit rates.