

# Energy market investigation Final Report

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# Our findings – an overview

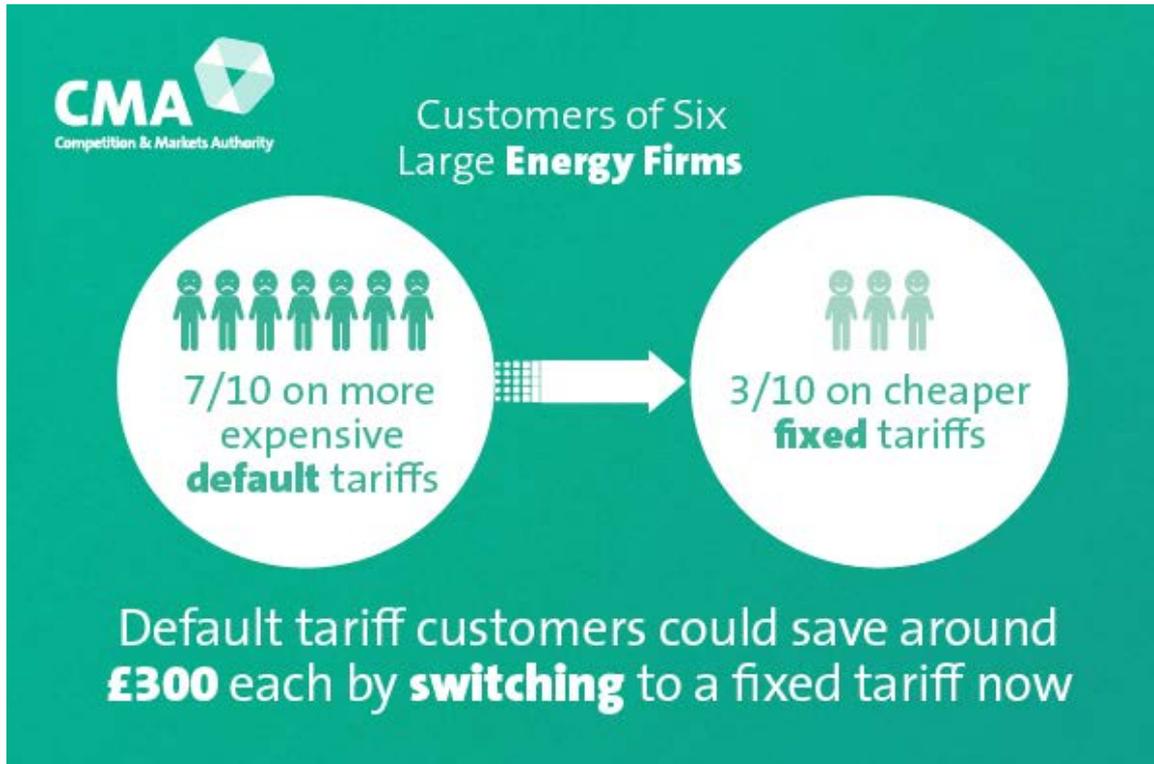
- Aspects of the gas and electricity markets that are working well.
  - In the wholesale markets, there is no evidence that companies are able to exploit market power.
  - In the retail markets, there has been growth in new entrants.
- Some prior concerns have not been found to have had a harmful effect.
  - Vertically integrated firms, which both generate and retail energy, enjoy at most only a modest benefit from it.
- Substantial competition problems in three main areas.
  1. The demand side of retail markets – a lack of customer engagement
  2. The supply side of wholesale and retail markets - regulations and technical constraints restrict competition.
  3. The broader regulatory framework – hinders the timely development of policies and regulations that benefit customers.

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New entrants now  
make up 13% of  
the domestic energy  
market in both gas  
and electricity

# Our findings – low customer engagement

- Large numbers of customers do not shop around or switch supplier.

Our survey of 7,000 customers showed 34% had never considered switching supplier and 56% had never switched supplier, did not know if it was possible, or did not know if they had done so.

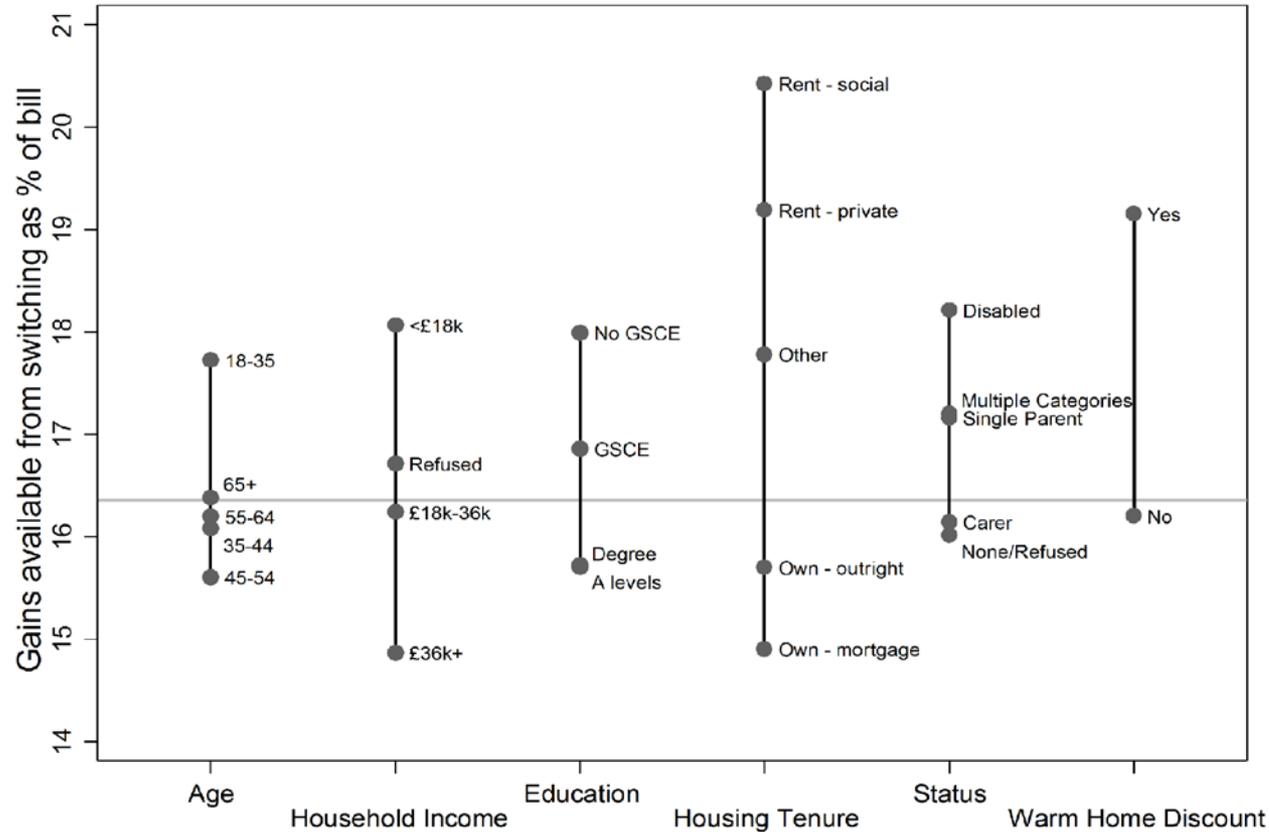


Other possible causes include lack of confidence in PCWs, no access to internet, primitive metering and confusing and inaccurate bills

Problems more acute in certain categories of customers (eg vulnerable customers)

Similar issues with microbusinesses – 45% on default electricity tariffs

# Our findings - demographic variability



# Our findings

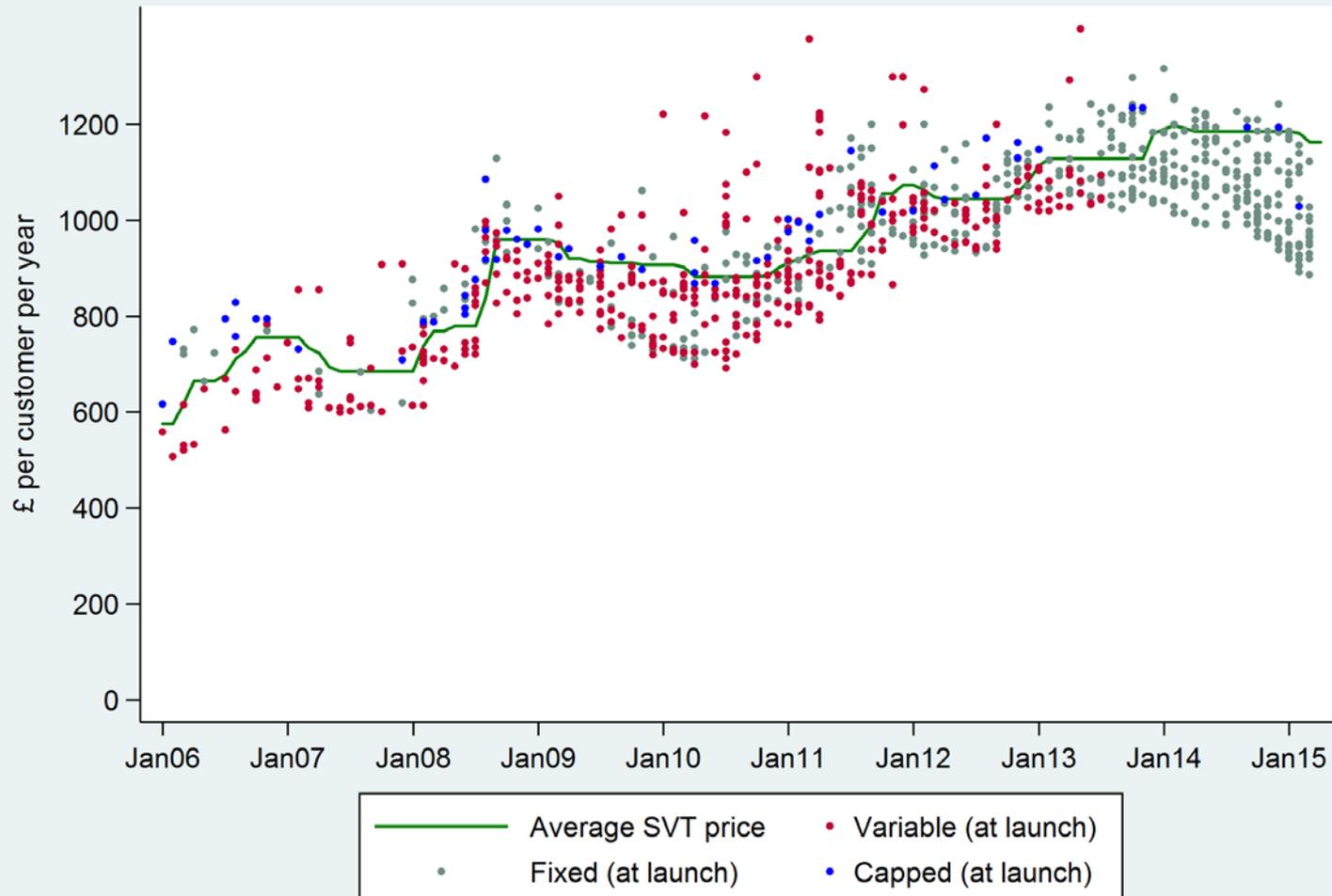
- Technical constraints (Prepayment infrastructure)
- Issues arising from the regulatory framework
  - Some regulations insulate companies from certain costs, dulling incentives to improve efficiency (eg Gas and electricity settlement)
  - Some aspects of the structure and governance of the regulatory framework increase risk of policies that are not in customers' interests.
  - Issues relating to code governance.
  - Issues relating to policy development.
  - Issues in the regulation of wholesale markets.

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At privatisation there were two codes which governed the industry, there are now 11 codes comprising over 10,000 pages of rules

# Our findings – adverse effects on competition

- Weak customer response give suppliers market power over inactive customers
  - Retail profitability above the competitive level
  - New entrants have a limited market share
- Pre- payment customers (around 16% of all customers) particularly disadvantaged
- Various aspects of the regulatory framework give rise to adverse effects on competition

# Our findings - estimate of detriment for customers



Based on typical domestic consumption of 3200kwh/year for electricity and 13500kwh/year for gas.

# Our findings - estimate of detriment for customers

- The competition problems are having a substantial detrimental impact on domestic customers.
- We estimate:
  - suppliers made excess profits of around £650 million a year over 2012 to 2014.
  - Microbusinesses paid about £180 million a year more than they would have done under well-functioning markets over 2007 to 2014.
- The detriment arising from problems with the regulatory framework is more difficult to quantify but is likely to be very substantial.
  - DECC estimates that climate and energy policies will add 37% to the retail price of electricity paid by households in 2020.

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Overall domestic customers have paid an average of £1.4bn a year more than they should have from 2012 to 2015

# What is to be done?

- Hopeful signs
  - Recent rapid growth of smaller suppliers
  - Smart meters could make a big difference starting 2020
  
- We need to continue to promote engagement
  - But this may take too long for certain customers who can afford it least
  
- A package of retail remedies designed to achieve four overarching aims:
  1. Create a framework for effective competition
  2. Help customers to engage
  3. Protect those who are unable to exploit the benefits of competition
  4. Future proof our remedies by building a robust regulatory framework

# The whole remedies package

- A holistic package of remedies to address the competition problems identified.
- Over 30 remedies in total, imposed through our order-making powers, undertakings from companies or recommendations to DECC and Ofgem.



# Pre-payment price cap

Price cap will be in place for more than 4 million prepayment meter customers, until the end of 2020.

This is where competition is working particularly badly and where there is a high proportion of vulnerable customers.

Smart meters will make a huge difference by removing technical constraints and reducing costs.

Designed so as to allow competition beneath the level of the cap, allowing suppliers to achieve a normal return on capital.

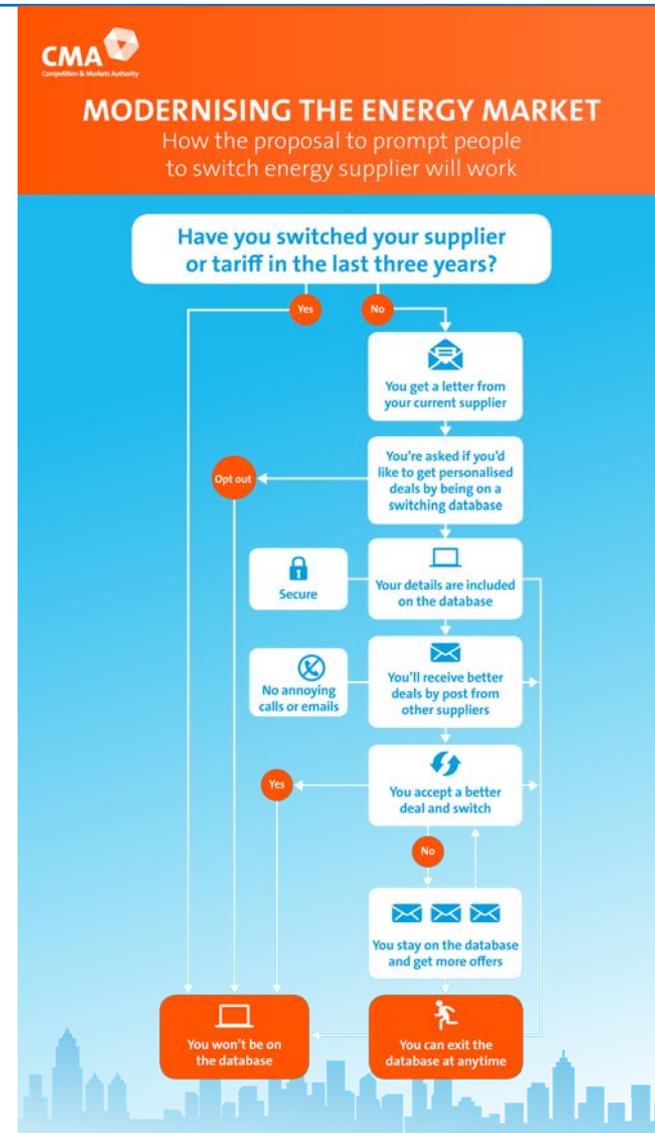


# Data base remedy

This is a bold new idea. This is the remedy that goes right to the heart of the problem.

It targets the customers who are most in need of help, ie that have not switched for a long time.

- Customers can opt out at any time
- Suppliers will be able to send personalised offers by letter to these customers
- The data base will be closely managed by Ofgem

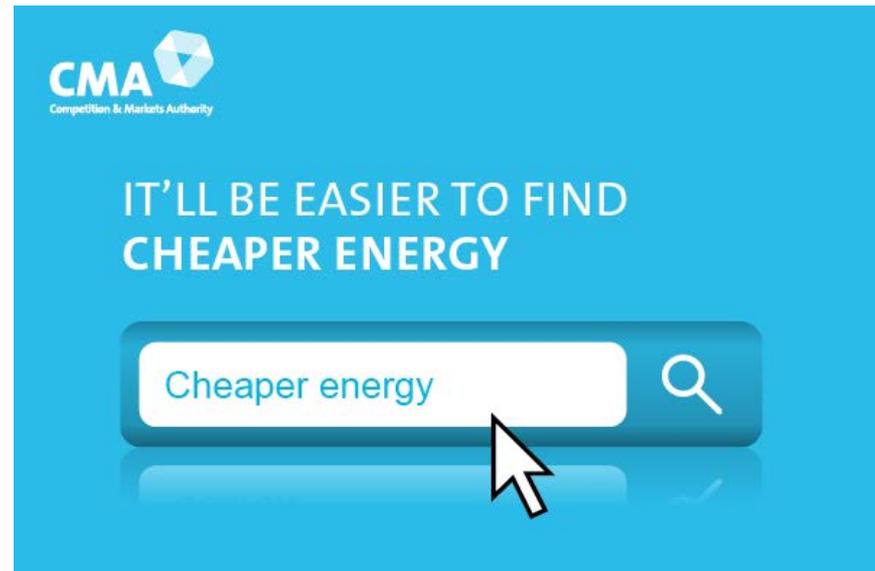


# Ofgem testing

Many reforms have been implemented over the past few years without adequate testing.

Some of these reforms have led in our view to poor outcomes.

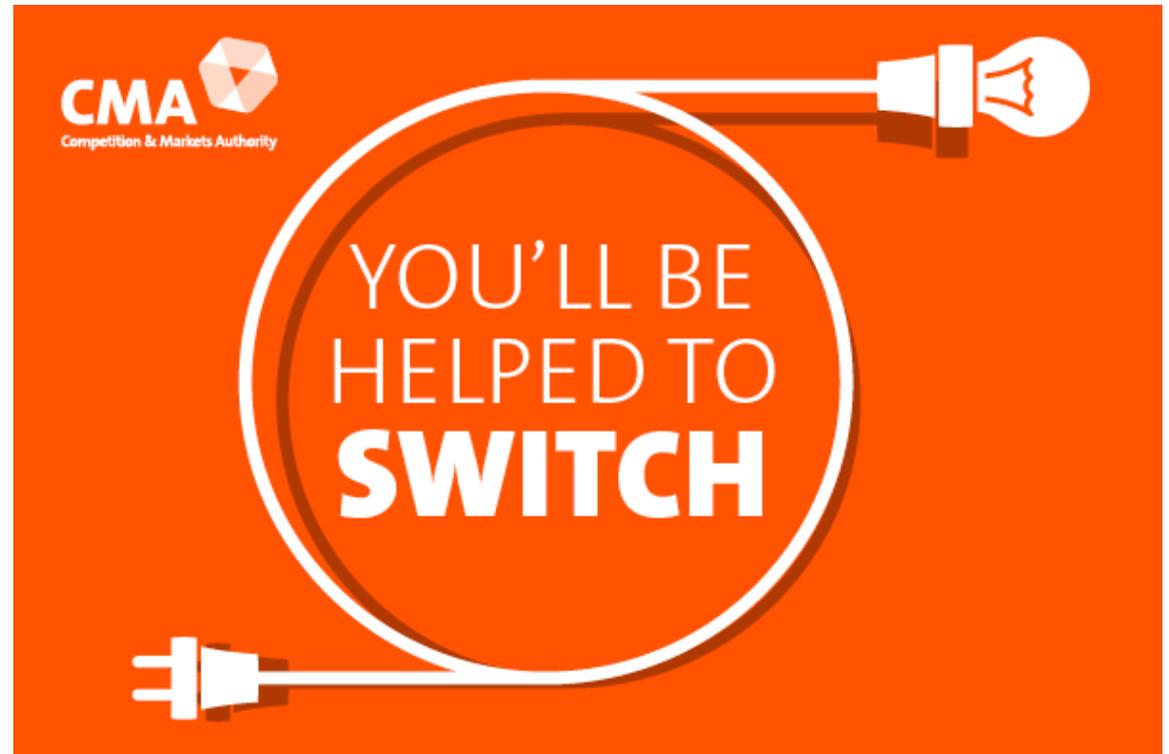
We will help Ofgem work with suppliers to test any new interventions using Randomised Controlled Trials.



# PCWs that work better

PCWs will automatically get access to customers' meter number.

If customers' give consent, PCWs will be able to request their usage data from suppliers and use it to give more accurate quotes.



# Microbusiness

A set of remedies covering:

- An order on suppliers to disclose their prices publicly
- The prohibition of restrictive clauses that lock in customers.



# Future-proofing by building a robust regulatory framework

## Reset of the regulatory framework:

- More robust and transparent analysis underpinning decision making
- Recalibrating the roles of DECC, Ofgem and the industry

## A set of remedies covering five areas:

1. Legislation to clarify Ofgem's duties and objectives;
2. Ofgem to publish opinions on policy proposals and DECC and Ofgem to publish joint plans for implementation of policies;
3. **Ofgem to publish an annual report analysing the impact of policies and regulations;**
4. The Six Large Energy Firms to provide better financial information; and
5. **Changes to the governance of the industry codes.**



# Next steps



- Window for appeal until 24 August
- Remedies implementation – CMA (eg price cap, database remedy)
  - Implementation of remedies by December 2016
- Remedies implementation – DECC and Ofgem (eg regulatory framework)
  - Implementation asap.

# Next steps – timing of retail remedies

Timing	Remedies taking effect
2016	Removal of certain regulations dulling competition (PCWs, tariff restrictions)  Measures to alleviate the technical constraints on prepayment infrastructure
2017	Price cap for prepayment customers
2018	Database remedies
2019	New measures taken following Ofgem testing
2020	Substantial completion of interoperable smart meters' roll out

# Our final report – conclusion

- The last major output from the most comprehensive and wide-ranging investigation of the energy market since liberalisation.
- **Our measures will help more customers get a better deal and bring the energy market into the 21st century.**
- Ofgem will have a more authoritative voice in the market. This will lead to more robust decision making, avoiding committing the same mistakes and anticipating future challenges

