Energy and Climate Change Committee

Oral evidence: Energy prices, HC 773
Tuesday 26 November 2013

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Watch the meeting

Members present: Mr Tim Yeo (Chair); Ian Lavery; Dr Philip Lee; Mr Peter Lilley; Christopher Pincher; Sir Robert Smith; Graham Stringer; Dr Alan Whitehead

Questions 193-321

Witness: **Andrew Wright**, Interim Chief Executive Officer, Ofgem, gave evidence.

Q193 Chair: I would like to thank the staff and Committee members for their support and Sir Robert Smith for his work as replacement Chairman during my absence.

All right. I think you would like to make a brief opening statement. Is that correct?

Andrew Wright: Yes, if I may.

Chair: We rather messed you around a bit this morning. We are glad to see you today.

Andrew Wright: That is all right, I totally understand. I am glad to see you as well.

First of all, I want to say that I completely understand why people feel frustrated and angry about rising energy bills. Prices have more than doubled over the last 10 years, at a time when incomes have been squeezed and consumers are not convinced that the price increases that they see are either fair or justified.

There is a deep distrust of anything the energy companies do or say, and partly that reflects the history. That is to some extent their own fault: there is a legacy of years of aggressive doorstep selling, for example, and you see poor customer service and confusing tariffs. All these things have compounded that mistrust of energy suppliers. When anyone tries to take action by changing supplier, they then experience a market that is both confusing and difficult to navigate. Consumers have a perception that the market is not working well, and we agree: we think that the retail market is not working as well as it should. That is why we have put retail market reforms in place, to try to make the market simpler, clearer and fairer. Given all that, it is not surprising that consumers jump to the conclusion that price rises are being driven by profiteering, and that is the basic problem we have. The question is: what do we do about it and where does Ofgem fit into that?

From the public, we often hear the question, “You are the regulator. Why are you not regulating?” I think there is a pretty clear answer to that. We work within a public policy framework, which is set by Government, of competition and markets and not price controls, and in that framework we do not have the power to require companies to reduce their prices. Our job is to make competition and markets work effectively, and that is what we are trying to do. I mentioned the retail market reforms; we are also trying to remove barriers to entry for new suppliers by making the wholesale market work more effectively; we are trying to improve transparency and build in trust and confidence about what is going on; and, as you know, we have launched a competition assessment with the OFT and the CMA to try to reach an understanding of exactly what is going on in this market that is accepted by everybody—but it is not our job to challenge that policy framework. That is legitimately something for political debate; it is, rightly, for politicians and for Government to discuss. We are very happy to support whatever Government of the day and however they want to develop that policy. That is the opening statement that I want to make.

Q194 Chair: Am I right in thinking that National Grid is one of the bodies that you keep an eye on?

Andrew Wright: Yes, absolutely.

Q195 Chair: What competition does National Grid face?

Andrew Wright: National Grid with its operations within the UK is predominantly a monopoly that is regulated by us through explicit price controls.

Q196 Chair: What special steps do you take to look at the charges that National Grid make?

Andrew Wright: The price controls that National Grid operates under are set through a two to three-year process involving scrutiny of all its costs and its business plans. We only improve that price control after extensive consultation.

We also put in place a series of incentives, which means that if National Grid delivers value for consumers by reducing costs by improving its performance and service, then they benefit from that. So there is an incentive on National Grid to deliver what is necessary for consumers as well. All of that together should give consumers assurance that they are getting good value for money from National Grid.

Q197 Chair: How far do you drill down? Do you look at any individual projects that National Grid is involved in?

Andrew Wright: We certainly drill down. We examine their costs in great detail and we certainly do look at individual projects, particularly the large strategic projects that are a significant part of their capital expenditure. For example, the projects to connect the islands—that is not actually National Grid—but projects like the bootstraps, the sub-sea projects to connect Scotland with England, for example. We look at these types of projects very closely on a case by case basis; the companies need to make a needs case and they need to convince us that the costs they are putting forward are efficient. On top of that, even once we have agreed those terms, the companies operate under an incentive framework. If they deliver those costs more cheaply than they had assumed—and we hope they do do that—then consumers will benefit immediately, and the companies also have an incentive. So there is a win-win from companies working more efficiently, but obviously we do not want to set that bar at a level that is easy for the companies to outperform.

Q198 Chair: National Grid quoted a price of £13 million to connect some houses that were going to be developed in my constituency, which worked out at a price of more £10,000 per house. When there was some protest from the developer about this, they reduced the charge from £13 million to £5 million. Does that suggest that they are operating in a tightly regulated and controlled market?

Andrew Wright: Is this in the gas distribution business?

Chair: Electricity.

Andrew Wright: Electricity. Obviously I do not know the specific example, but certainly connections are a part of that and we have a framework in place on two fronts, not only to make sure that companies are offering reasonable quotes for connection and respond quickly and promptly to consumers, but connections is a part of the market that we are seeking to open up to competition. Companies are incentivised not only in delivering efficient low-cost connections but also in opening that up to the market. I can give you further information on what we are doing on connections if you wish.

Q199 Chair: Would you not consider that if a price charged by a monopoly can change from £13 million to £5 million, there is something seriously feeble about the regulation of that monopoly?

Andrew Wright: I do not know the specifics of that particular case.

Chair: Whatever the specifics were, they reduced the price by 60%. They are getting a bit of a protest.

Andrew Wright: I am not going to come to snap judgment about an individual case.

Chair: I am not asking you to come to a judgment. I am saying if it is true that they can reduce their price by 60%, there is something seriously defective about your regulation of National Grid.

Andrew Wright: I do not know the specific circumstances.

Q200 Chair: I am not asking you to know the specifics. Is there any possible conclusion that if a monopoly supplier can reduce its price by 60%—

Andrew Wright: I would like to know the full facts.

Chair: —if that is true, would that not show that Ofgem are seriously defective?

Andrew Wright: No, it does not show that Ofgem is seriously defective; not at all. I would need to see the specifics of that case before I reach a snap judgment. I have been involved in regulating this industry for long enough to know that it is a good idea to get the full facts before making a judgment.

Q201 Chair: Indeed it is. One of the facts of this case was that a development of over 1,000 houses has not taken place at a time when I think it is universally agreed we urgently need more housing.

Coming back to the question of wholesale prices, about which there seems to be a fair amount of disagreement, not to say confusion, it was suggested to us by one of the Big Six that you had revised your position on wholesale prices, rising from 1.7% to 8% for gas and 13% for electricity.

Andrew Wright: That is not the case. I think we are talking about two different things.

First the 1.7% is our assessment, based on our 18-month hedging model that we use in the Supply Market Indicator of how much the costs for a typical supply business would have increased year on year. So that is the 1.7%, and we have not revised that figure.

The 8% is something where we did not revise the numbers. This was something we had in a fact sheet on our website beforehand, which indicated the change in the price of winter energy from one year to the next. So those are looking at two different things. Whether or not the consumer or the supply company sees the full 8% or a lower number depends on the extent to which companies had hedged their position in advance, so it is not surprising that you see a range of impacts of wholesale costs. Generally there is a consensus that wholesale costs have gone up slightly—not hugely—over the last 12 months and, depending on how companies bought in that market, some will see very modest increases, such as EDF and npower, and others will see more significant increases. That also depends on how well they bought power the year before. If the base is lower they may see quite sharp increases as well.

Q202 Chair: It is possible to see sufficiently clearly how well they have bought their power?

Andrew Wright: The companies are providing us with a range of information. I think they are providing us with more transparency than we have ever seen, and they are providing information through the corporate segmental statements. I think we can get a pretty good idea of what is happening to the companies' wholesale costs.

Exactly why the wholesale costs are doing what they are doing for particular companies is less clear. That depends on individual decisions, individual contracts that they sign, some of which might be long-term contracts. I think it has been observed that it depends on how they manage their internal portfolios and their relationships with their own trading and generation arms.

Q203 Chair: Do you think that they have exaggerated the impact of wholesale costs on their pricing?

Andrew Wright: I have no reason to suspect they have. What we have seen is the sort of outcome that you would expect. Some companies have announced low increases that are close to or even below the level through our 18-month hedge model; some of them are higher. We would expect companies to have different approaches to purchasing different hedging strategies. Some of them will be more successful than others. That is the nature of six companies competing in a market. We would not expect them all to have identical costs. We are looking at relatively small differences between them, given the volatility of the market.

Q204 Graham Stringer: To what extent have network prices contributed to the latest round of price increases?

Andrew Wright: Most companies have talked about network charges being up about 10%. Network charges represent just over 20% of the bills. So they would have contributed perhaps 2% to 2.5% to the price increases.

Q205 Graham Stringer: What is going to happen next? There seems to be a different view from Ofgem compared with the energy companies. You are saying they will stabilise. They are going to say they are going to increase quickly.

Andrew Wright: We have been pretty clear about what we think is going to happen. Overall, taking network charges as a whole, following the increase in charges to 2014-15, we think that network charges will be broadly flat in real terms, so they will go up roughly in line with inflation between 2015 and the end of the decade. We are able to say that partly because price controls are in place for the transmission and the gas distribution companies and we have seen the business plans for all of the companies for their electricity distribution businesses, most of which show significant reductions in electricity distribution charges for the first year of the next price control, which starts in 2015. We have pretty good visibility. There is some uncertainty over it and most of that is driven by these large strategic transmission projects, such as connecting the islands, connecting England and Scotland and so on, which might lead to modest increases, but we have a pretty good picture.

On the figures that have been produced, I think only one company in the industry has produced these figures long-term. We do not recognise those figures and we have told the company that we think that those figures do not represent a true picture of where network charges are going over the next seven or eight years.

Q206 Graham Stringer: Then can I take that as a guarantee that post-2015 the prices will not go up?

Andrew Wright: Yes. You can see from the price controls that we have put in place that that is going to be the case. I think the last piece of the jigsaw, the piece that was not there—and with respect to the company involved, probably the information was not fully available when they made their forecast—is now there. We have now published those business plans. We have approved one of the business plans through the fast-tracking process, so we have better visibility of where those network charges are going. The only uncertainty is the strategic investments. If there is a very heavy degree of investment in wind generation—for example, if we end up connecting the islands and investing in sub-sea cables around each of the coasts to try to improve connections between England and Scotland—then there could be some modest upward driver in those charges, but generally speaking our view is absolutely correct.

Q207 Graham Stringer: That is an interesting point. As I am sure you are aware, there is a row going on about what the costs of renewables are within energy bills. Do you account separately for the extra costs for joining up renewables? Is that accounted separately, and how would the consumer know if it is accounted separately?

Andrew Wright: Yes. The investment in transmission and distribution charges is driven by a number of factors. One is obviously strengthening, reinforcing, replacing, and upgrading the network; the other is repowering Britain for the low-carbon economy. A significant part of that is shifting from power stations in the Yorkshire coalfields to power stations in remote locations where windfarms are located—offshore north of Scotland. That is a significant driver of transmission investment in particular. That will not appear in the direct schemes for supporting renewable generation. Some of that cost is borne by the generators and some of it will be borne by consumers as a whole.

Q208 Graham Stringer: How will the consumer know that they are paying for that? You say you know what the accounting is. How will the consumer know? You can separate out the direct costs of the different renewable initiatives. How will the consumer know about that particular cost within the networks?

Andrew Wright: The costs that go into network charges are hugely transparent. There is a vast amount of information that tells you what is happening to costs; what is driving those cost increases. The companies have to provide strong justifications. We have to convince ourselves that the business plans that they put forward, and indeed the individual cases for strategic investments, are in the customers' interests and provide good value for money for the customers. All that information is potentially available.

Disaggregating the exact cost that is being driven by investment in renewable energy, for example, would not be a straightforward thing to do because a number of different factors contribute to investment. Undoubtedly there is a degree to which the increase in transmission and distribution charges is being driven by investment in low-carbon generation. The direct connection costs for offshore windfarms to bring it in onshore will be borne directly by the generators themselves.

Graham Stringer: This Committee had a view at variance with that. In its earlier report it thought that the methodology for determining the charges from the suppliers was overly complex. Do you agree with the Committee that the methodology for determining the charges is over-complex? Do you think that in itself leads to an increase in charges, because there is uncertainty about what the energy companies are going to be charged?

Andrew Wright: Are you talking about the charges from the network companies?

Graham Stringer: Yes.

Andrew Wright: There are two issues around the charges levied on suppliers. One is concerns about complexity. The other is concerns about predictability. We have worked hard with the network companies to try to improve the transparency of charges and to give a better indication to suppliers of what will happen to their network charges. I cannot give you details off the top of my head, but we have made a number of changes to the process for setting charges, which will reduce the degree of uncertainty about future electricity, gas distribution and transmission charges.

Q209 Sir Robert Smith: In your opening description of the bleak situation that we face in terms of the breakdown of trust and the lack of transparency and understanding of what is going on as people face the challenge of heating their homes, did it seem to you that perhaps it would have been an idea to have gone further in implementing BDO's recommendations to help rebuild that trust?

Andrew Wright: The first thing I would say is that Ofgem has led the way in increasing transparency in this industry. From 2008 with the probe, when we shone a light on the companies' accounts in that document, to 2009, when we put in place a licence condition requiring the companies to publish separate corporate segmental statements, to the continual publication of the Supply Market Indicator, and the improved information that we require companies to give consumers, we have been committed to improving transparency and building trust and confidence in this market.

Q210 Sir Robert Smith: You did say in your opening remarks that it had not worked.

Andrew Wright: Yes. For a start, I think many of the measures that we have put in place in the Retail Market Review are only just coming into place. If you look at the market now, it is a much simpler market than it was even a year ago and certainly a hell of a lot simpler than it was a couple of years ago. If consumers were to go into the market now they would find that it has never been easier to choose and change supplier than it is today. That is not necessarily saying it is easy enough, but it has never been easier than it is today and that is because of the actions that Ofgem has taken and—

Q211 Sir Robert Smith: On the trust and transparency side of it, when people see their bills going up they are very suspicious of what is going on within the companies' accounts. The BDO recommendations were designed to at least pull that out into the public domain.

Andrew Wright: We have accepted the Committee's recommendation that we look again at that. We have published a fresh consultancy report on how we can improve the transparency in the industry, looking not only at the BDO recommendations again but also seeing whether there is more that can be done. Just to recap on that, we took the view that it would not represent good value for money for consumers to accept some of the BDO recommendations. We heard what the Committee had to say on that and we are revisiting that conclusion. We want to see whether we have it right, in terms of both the costs and the benefits.

Q212 Sir Robert Smith: You did say, in terms of how you calculated the costs and benefits, you could publish the costs that you have taken into account, but I do not think that you have.

Andrew Wright: It was a more subjective assessment than that. It was more a question of looking at how difficult it would be to get information that would give us that additional level of trust that the companies were not doing anything untoward in their trading profits. Generally speaking, there is no reason to think that they are doing anything untoward. I do not think that they are—

Q213 Sir Robert Smith: But when there is a breakdown in trust—

Andrew Wright: I understand.

Sir Robert Smith: —there may not be a rational reason for the breakdown in trust, but the breakdown has happened, so you need to go that further mile to try to restore trust.

Andrew Wright: I completely understand that point and I agree with you. That is why we are going the extra mile in revisiting this question and asking ourselves whether there is something of value that can be done.

It is worth saying that three of the companies have provided more information on trading data, particularly those for whom it is easy to do so because they are generally more focused on the UK business.

Q214 Sir Robert Smith: What is the timescale for this consultation?

Andrew Wright: I think the consultation closes on 6 December, and we obviously will need to consider the consultation responses and come up with our conclusions some time fairly early in the New Year. We are not delaying on this in any sense.

Q215 Sir Robert Smith: You recently published summaries of the energy companies' annual statements for 2012. For the record, how have energy company profits changed between 2011 and 2012?

Andrew Wright: Overall, the profits across generation and domestic and non-domestic supply have fallen slightly over that period. Within that we have seen an increase in the domestic supply profits—the numbers are in my pack here, but I think the headline is a 75% increase. That represents an increase in margins from just over 3% to about 4.5%. Had that increase not happened, arguably bills could have been 1.5% lower. That is the scale of that increase in profits. Looking at the drivers of that, obviously a key driver was the colder weather in 2012 compared to 2011, as we made clear in the report. Clearly companies' profits to some extent are sensitive to what happens in the weather.

Q216 Sir Robert Smith: So as people's bills go up when it is cold, the profits go up.

Andrew Wright: Yes. If you want to come back to standing charges, that is a consequence of companies keeping standing charges at a level that is probably below the true level of their fixed costs. I am not necessarily going to challenge them doing that. Generally speaking, companies do tend to make more profits when they sell more energy but weather is obviously a two-way risk for them.

Q217 Ian Lavery: I wonder what you are actually going to challenge these Big Six companies on. Your response to Sir Robert, with regard to profits, was that it is basically 4.5% not 3%. From your own report it seems to be okay that the Big Six energy companies have made £23 more in average profit from each household in 2011. That is an increase of 75% to the consumer.

Andrew Wright: I never said it was okay.

Ian Lavery: It seems to be okay. You implied that is was okay.

Andrew Wright: I did not imply that it was okay.

Ian Lavery: Also, the dual fuel bill has increased from £53 in 2012—that is profit per household—to £105 this year. That is absolutely ridiculous. We should be focusing on these people who cannot afford to heat their homes. It is generations now since people have not been able to heat their homes. It is 2013 and we have a situation where people cannot heat their homes. They cannot afford energy. Is it right when people say that Ofgem is a toothless tiger? It is right when they say that it is not fit for purpose because regulation is not working within the Big Six?

Andrew Wright: First of all, I had not said that this level of profit is right or acceptable, nor have I approved it. If the companies ever imply that we think 5% or any other level of margin is right, then we have never said that. We think companies need to earn the profits that they make.

Q218 Ian Lavery: You said you would not challenge them.

Andrew Wright: No. I have said we think companies need to earn the profits they make by providing good, efficient service, reducing costs, improving performance and winning customers in a competitive market. They should have no entitlement to any level of profit.

Q219 Ian Lavery: What about the consumers? Are you counting this or is it just how much profit or how acceptable the profits are with the basic—

Andrew Wright: As we say, the way we challenge companies is by making changes to the market to make it more competitive, to ensure that competitive pressure bears down on these companies, both from new entrants and from consumers engaging more effectively in the market. The changes we have made will make a big difference to consumers. They are the most significant changes since competition was introduced. That is the public policy framework in which we operate. If you think that we should go further and you think that we should be looking at regulating these companies directly, then that is certainly a legitimate debate for politicians to have.

Q220 Ian Lavery: I think it is right for the man and woman on the street and families to be able to afford electricity and gas. It is not the case anymore. What are you going to do about it?

Andrew Wright: We will do what we can within the public policy framework that is set out for us. We are not elected politicians. We work under a statutory framework set by Parliament and by Government. If you want to change that statutory framework to something that leads to us being able to control prices directly, then that is certainly something that is appropriate for Government and politicians to debate. It is not right for us as unelected regulators to change that public policy framework without that mandate of being elected.

Q221 Ian Lavery: To a degree then, basically Ofgem is a toothless tiger and—

Andrew Wright: No. We take actions to make the market more competitive, which is our mandate, what we are set up here to do. We do what we can to benefit consumers within the public policy framework that has been set for us. That is our job and we should not stray outside of that because we do not have a statutory remit to do so.

Q222 Chair: You referred to the increase in transparency in the market now and claimed a significant role for Ofgem in achieving that. Do you not think that if the industry returned to the structure that existed after privatisation, where there were no vertically integrated companies but you had generators on one side and suppliers on the other side, that that single step would be the greatest move towards transparency and restoring trust in the energy companies that could be taken?

Andrew Wright: First, the industry that has been arrived at has not happened by accident. It has happened because the companies view it as the most efficient and effective way in which to organise their businesses. Potentially there are benefits to consumers from doing that. If it reduces companies' costs for trading and hedging electricity, for example, and if you have an effective competitive market—I agree that is a big "if", or two big "ifs"—consumers should benefit from that. If we constrain how companies organise themselves, then there is a risk that we are stopping companies finding ways of delivering benefits for consumers, lower prices for consumers.

Having said that, if you were to separate there is a price to be paid. I think there is a price to be paid from competition and markets in general, and privatisation in general, from a relative lack of scrutiny and transparency. Clearly, if those companies were separate, it would be far easier to see what their cost of purchasing energy was and, for the generation companies, what their cost of selling energy was. As it is at the moment, we do have to rely to some extent on ensuring that the companies have robust transfer pricing arrangements and we have done a lot through the segmental statements to try to make sure that that information is available.

It is worth emphasising what we are doing on liquidity as well. The idea of the liquidity reforms is to try to ensure that new entrants and independent generators have the access to the market that they would have in the sort of structure that you spoke about, so trying to get the benefits of a disaggregated market without having to go through the disruption of that level of structural change. If it works, then that will be a far quicker and easier way of bringing those benefits to consumers.

Q223 Chair: I do not think that the argument that vertical integration has come about because it is in the interests of consumers is one that many consumers would support, although it may be claimed as one of the reasons why the companies wish to do it. A lot of other industries manage without vertical integration. Tesco does not own a large number of food manufacturers or farms but they are regarded as acting competitively in the interests of their consumers.

Just to go back to the point, are you saying that you think it would not be an advantage to consumers—both in terms of trust and in terms of keen competition—for the present vertically integrated structure of the industry to be ended?

Andrew Wright: First of all, the gas market is not vertically integrated. There is a degree of ownership of upstream gas but, in general, upstream gas is owned by parties who are not active in end supply, and that represents about two-thirds of the dual fuel bill. For electricity then, yes, that is. I think it is more complicated than that. There are potential benefits from vertical integration both to companies and to consumers. Generally speaking, the way that effective competitive markets should work is that what is in the interests of the company should ultimately benefit consumers. If it does not, then the market is not working well. That is why we are here talking about retail competition today as well as prices as a whole. There are benefits and potentially there are costs associated with that. One thing that is absolutely certain is that it would be a very disruptive change to the industry. It potentially would undermine confidence in investment at a time when we need it.

The last thing I would say is there is an appropriate framework for looking at these types of issues, and that is a market investigation reference. Once again I think it would be difficult, if not impossible, for a regulator such as us to make such a major strategic change without first going through the process of the market investigation reference to the Competition Commission, or the CMA when it comes into play.

Q224 Christopher Pincher: Continuing on the theme of increasing competition, you said that Ofgem will monitor the impacts of its RMR proposals. I have here the letter that you sent to the Secretary of State on 5 November, in which you say that with CMA and with the Office of Fair Trading you will be preparing a framework for an assessment of competition. You say in the letter that that assessment will need to assess consumers' abilities to access, assess and act on information. Why is it not appropriate then to set some quantitative targets around the success of RMR? Why would that not help consumers to access, assess and act on information?

Andrew Wright: We have not said that it is not appropriate to set quantitative targets. I think it is worth saying that it is far easier to set a framework of the sorts of things you should be monitoring to see whether the market is improving or not improving. It is a far harder question—and to a significant extent a political question—to answer the question of how good is good enough and, for reasons that have been mentioned before, whether the standards that you would expect from a market in an essential public service ought to be higher than perhaps other competitive markets. I think those are really big and important questions that we are going to need to address.

The risk associated with setting quantitative targets, as with any targets, is that you risk distorting the behaviour of the supplier so they focus on achieving those particular quantitative targets rather than focusing on for instance competing with other companies on providing excellent service to consumers, operating more efficiently, which is really what you want them to do. Competition should not be that difficult. It should be companies simply trying to do the best for their customers.

Q225 Christopher Pincher: I hear what you say but I am a little confused, Mr Wright, because I have here a quote from Ofgem that says, "While we are clear about the broad outcomes that we expect from RMR we do not consider it would be appropriate to set specific quantitative targets for success". So why did you just say that you have never said that?

Andrew Wright: The reason I gave is the reason why I think there is a real risk associated with specific quantitative targets. Personally, I am not going to rule out that there may be some quantitative targets that we set. I do not want to pre-empt the work that we are doing with the OFT and the CMA. We are doing this work at the moment and one question we will look at is: how good is good enough? Generally speaking, one of the really important things is to monitor key indicators; make sure they are going in the right direction and that things are improving rather than deteriorating.

A lot of this is trying to get a vicious circle moving in the direction of a virtuous circle. It is trying to get building consumers' trust so they engage more in the market, so that suppliers do a better job in the market in meeting their needs, so that consumers' trust is further built and that then leads to even more engagement. It is trying to get that vicious circle moving in the right direction. Once that dynamic happens, I think we can be a lot more confident that this market will be meeting consumers' needs. At the moment I think we are seeing the opposite happening.

Q226 Christopher Pincher: Just so we can be clear, it is not true to say that you will not look at setting quantitative targets and, not wishing to pre-empt the review that you are doing with the CMA and OFT, you may well end up applying quantitative targets.

Andrew Wright: I will say today that we have not ruled out setting quantitative targets. It is one of the things we are looking at as a part of this study, but we do recognise that there are risks in doing that that you end up getting companies focused on hitting those targets rather than delivering good value for money for consumers.

Q227 Christopher Pincher: You might consider, for example, setting a baseline number of switches after a certain period of time?

Andrew Wright: Yes. Or indeed a target on the extent to which consumers are being active in the market, whether or not they are switching, comparing suppliers or moving to a better tariff with their current supplier. I think there may be a number of other metrics we might want to look at as well.

Q228 Christopher Pincher: That sounds like a positive change from Ofgem's previous position.

Can I ask you about foreign models of organising and running electricity systems? Some of us have just come back from Canada where we looked at the way the Saskatchewan market operates. It is somewhat different from ours. It may not be the right one but it is different. On 29 October, in answer to the question "Would it be sensible to look at foreign markets?" you said to the Committee, "There is already a pre-existing framework for the type of review you are talking about". Can you give us a bit more information about that?

Andrew Wright: Yes, that was referring to making major structural change to the market. The sort of model that was being spoken about was a central buyer of wholesale power who then sold that on to competing supply businesses, or alternatively some form of retail franchise model focusing on getting effective generation competition and servicing those—a number of alternative models might be considered.

I think there are two legitimate ways of addressing that. One is through the political process and the other is through a market investigation reference to the Competition Commission. The work we are doing with the CMA, the competition assessment, is not a full-blown market investigation reference. That might be the outcome of that work but that is not what it is and we cannot be expected to do the full-blown market investigation reference in such a short period of time. So to look at those types of issues, I think that would be the right framework to do it.

Q229 Christopher Pincher: Ofgem could do that?

Andrew Wright: We could refer the industry for a market investigation at the Competition Commission, yes. That would be one of the potential options that might happen at the end of the study that we are doing. There are other actions. Another might be that we decide we are going along the right lines and what we need to do is carefully monitor what is happening.

Q230 Christopher Pincher: You went on to say, "It is not something that we would sensibly be able to do ourselves, not least because the companies would most likely challenge us and we would end up at the Competition Commission".

Andrew Wright: Maybe I was not sufficiently clear. What we could do is refer the industry to be looked at by the Competition Commission. The Competition Commission has a broader range of powers and would be able to look at, say, significant structural change. If we were to do that through our own powers, through licence changes for example, it is highly likely that we would be challenged and those particular licence changes would be referred to Competition Commission in any case. But there is a framework for looking at more general competition concerns and that is a well-established one that applies across the whole economy, not just electricity and gas.

Q231 Christopher Pincher: Do you think Ofgem ought to have the power to conduct those sorts of investigations rather than simply being able to refer? Otherwise, as you will appreciate, consumers reading this evidence, listening to this inquiry now, will feel that the companies have Ofgem over a barrel; that it does not dare act in their interests.

> ***Andrew Wright***: No. I think there is a well established framework that has been in place for a number of years where concurrent regulators like ourselves—and indeed the OFT previously, until the merger with the CC to form the CMA—would conduct market studies. If they felt that the problems that they found could not be addressed through the sorts of changes within their powers, they would then refer that for a study by the Competition Commission who would have a broader range of powers and the possibility of recommending the sorts of structural changes that it would not be appropriate for us to do.

Q232 Christopher Pincher: I appreciate that that is the framework.

> ***Andrew Wright***: That is the same framework that exists for the other sector regulators. It is the framework in which we operate. It is a framework that has only just been changed and adapted through the Enterprise and Regulatory Reform Act.

Q233 Christopher Pincher: I appreciate that may be the framework, but to pick up on what Sir Robert said, the level of concern among consumers is such that it is incumbent upon you, as the regulator in this particular area, to go that extra mile. It does sound as if you are passing the buck.

> ***Andrew Wright***: We are not passing the buck. I think it is simply the framework. If we felt that we had exhausted our powers and our ability to make the changes that are needed to make this market work effectively, the appropriate course of action set down in the legal framework is for us to refer it to the Competition Commission. As you know, a couple of the companies have said that we should do that.

Q234 Mr Lilley: In your opening comment you emphasised very much that the general public does not have any trust or confidence in the energy companies. Yet in your discussion of the Retail Market Review, you have talked simply about ensuring that the companies do offer the fairest and best possible deal to consumers. Should it not also be a question of enabling consumers to have sufficient information to see whether or not they think the companies are offering the best possible deal?

> ***Andrew Wright***: Yes.

Q235 Mr Lilley: Will that not require you to publish the profits of companies and, indeed, to give an indication of what a reasonable level of profit in a competitive market would be?

> ***Andrew Wright***: RMR is broad-ranging reforms. It includes addressing poor behaviour by the companies through the standards of conduct, and giving consumers information on whether or not there is a better deal available for them from their current supplier. It involves a variety of prompts and alerts to try to get the consumers engaged in the market

and a whole load of rules simplifying the market, such as limiting the number of tariffs and making the tariffs that are offered simpler and easier to understand. I think all these things together will make a big difference.

Mr Lilley: You have ignored the question. Can you go back to the question?

Andrew Wright: I was about to address the question. In terms of providing information about profits, I think that is important because it helps build trust and confidence in the market, but it is not the case that the company that makes the least profit is necessarily offering the best value for money. It may well be the case that the company that is the most efficient, offering the best services, will also be the most profitable company. In many other markets you will find that is often the case. I think an unnecessary focus on profit in consumer choice potentially would not necessarily be in the consumers' interests. But I do agree that consumers need good information on costs and profits in order to give them confidence that these companies are not profiteering at their expense.

Q236 Mr Lilley: At present there is a widespread belief that the main reason prices or tariffs have doubled over the last 10 years, as you mentioned, is that they have been driven up by companies increasing their profits. If that were the case, of course, their profit level would be roughly 50% or more. Could you not publish some information that would tell us whether that is true or not?

Andrew Wright: We have published that information. We have published—

Q237 Mr Lilley: But you have made statements that it is untrue. It surely cannot be helpful. If the public is under a severe delusion then the public should be put right, and if the public is correct, then something should be done about these excess profits, but we cannot just pretend it is not an issue.

Andrew Wright: As the corporate segmental statements, which we have required companies to publish for the last four years, show, there has been an increase in profits over that four year period, but the vast majority of the increase in prices has been driven by other factors—wholesale cost increases, cost of network charges, the cost of environmental schemes and programmes and renewable support. Those are the main drivers of the increase in bills. We are not satisfied with that. We think there should be pressure on these costs. Companies should be incentivised to incur those costs efficiently. We do not think there is any entitlement to any level of profit. That is why we are trying to make the market work effectively. But that information is in the public domain; it is already there. You can see it from the companies' accounts and their segmental statements and from information that we have provided. In general, the companies' margins have remained under 5% over that period. I am not saying that is an acceptable level of margin, by the way.

Q238 Mr Lilley: This information has not, by and large, filtered through to our broadcasting media, which are supposed to educate us but don't. Will it be possible to give a clear picture as long as we have this vertical integration? Surely you can only give a clear picture of what the profit level is and where it is arising if you have a distinction between generation and supply?

Andrew Wright: Yes. There is a market in wholesale gas and electricity and, although it is not perfect, I think it gives a reasonable view of what the wholesale price of power and gas is, particularly for gas, which is a highly illiquid market with very little vertical integration. We have published information on this. We have information on our website that tells you that, although prices have doubled for the last 10 years, the main driver of those price increases has been the increase in wholesale energy costs. It is not the only driver. There have been other factors as well.

I think we have been transparent about alerting consumers. In 2009 with Project Discovery we were very clear that we saw the direction of energy prices as being upwards. We took the view that there needed to be changes to the markets to ensure the Government meets all of its objectives. Those are now in train. So there is a lot of information out there explaining what is going on. If you think we can do more then we can certainly look into that.

Q239 Mr Lilley: Harking back to what Mr Stringer was saying on transmission costs, we are told by National Grid and others, in several different documents we have received, that something like £24 billion to £25 billion has to be spent on renewing and extending the transmission network between now and the end of the decade. Given that it is £25 billion and there are roughly 25 million households, it is £1,000 per household. How is that that is not going to put any upward pressure on the cost per household?

Andrew Wright: It will put some upward pressure on the cost per household. When I spoke about the impact of network charges, that was network charges overall. Within that there is an increase in the charges associated with transmission. At the moment transmission only represents a relatively small part of the bill—4% or so—and that is going to increase quite significantly pro rata because of this very large investment. It is over £30 billion if you include the investment by the Scottish companies as well.

The reason why that is not impacting on the bills is due in part to our effective regulation. That is being delivered at a low cost of capital because there is a great deal of trust and confidence in the regulatory regime that we have set up, which enables us to bear down on the return that these companies earn. There are other factors including improved efficiency of delivery of this, but some of it is being paid for through higher bills to consumers as well. It is a mixture of those three things, but clearly it is not going through pound for pound on the customer's bill or anything like that.

Q240 Mr Lilley: It must ultimately because it has to be the customers paying.

Andrew Wright: These are long-life assets and the returns are earned over a long period of time, I think in excess of 40 years. The reason we are able to put in place a regime that allows those assets to be paid back over 40 years is the trust and confidence people have in our regime. The belief that if we do a deal on regulation with the companies that we will stick with it and that we are going to have a consistent approach to regulation, going forward.

That is critical to our ability to be able to deliver these large investment programmes in a way that does not impact unduly on consumer's bills. These are long-life assets and they will be paid for over a long period.

Q241 Chair: Building on Mr Lilley's concerns here. If it is the case that National Grid, the monopoly supplier of transmission, can adopt the approach, "We will think of a number, safe in the knowledge it is not going to get challenged or even scrutinised by Ofgem. Then if we get a developer who objects to this we can cut the price by 60%," it is not surprising there is a huge figure—was it £25 billion?—by the end of this decade.

Andrew Wright: As you know, that is not the way that network price regulation works. We do not just accept the numbers they give us in the first instance. There are a lot of incentives in the process for them to give us the right number. If they do end up delivering the programmes more cheaply than they had assumed in their business plans, consumers benefit from that immediately. We want to give them the right incentives. We want them to deliver their outputs more cheaply and at a lower cost for consumers than they put forward. So these are all important parts of this framework, which delivers such good value for money for consumers.

Q242 Dr Lee: Do you think we are better off as a nation having one monopoly owner of the grid?

Andrew Wright: The electricity distribution and transmission is a natural monopoly. There is—

Q243 Dr Lee: No, hang on a minute, in America quite a large part of the network is owned by co-operatives. Do you think that is potentially a better way of doing things? There seem to be some parallels between National Grid and BT here, in that the roll out of broadband by BT is far from perfect, yet they are the only ones who own—with the exception of a bit of cable here and there—pretty much all of the fibre optic cabling. Therefore they basically have us by the cojones, in the same way that National Grid seems to have us by the cojones.

Andrew Wright: Electrical transmission is a natural monopoly. That is a fact of life. It would make no sense to build a BT national grid.

Q244 Dr Lee: In which case what are you regulating then?

Andrew Wright: We are regulating them to ensure that they deliver outputs or that they operate in a way that is in the interests of consumers.

Q245 Dr Lee: But there is no competition.

Andrew Wright: There is no competition but we regulate their prices directly.

Q246 Dr Lee: What is your benchmark?

Andrew Wright: The ultimate benchmark is the setting and appropriate return on invested capital, which we set—

Q247 Dr Lee: What is that?

Andrew Wright: The latest return on invested capital—we have set a return on equity for National Grid was 6.7%, if I have my figures right. We have just been through another one. I may be wrong.

Q248 Dr Lee: At a time when bank base rates have just been reduced to 0.25%?

Andrew Wright: No, that is return on equity. Obviously the business is significantly funded by debt. The overall weighted average cost of capital would be close to 4% and—

Q249 Dr Lee: Okay. But that is still 16 times more than the rate that the European Central Bank has just set.

Andrew Wright: This is the return on equity, and we judge their return relative to equity returns within the market over the long-term.

Q250 Dr Lee: How do you arrive at that benchmark of that being an acceptable return on equity?

Andrew Wright: By looking at equity returns the comparable businesses get in the market.

Q251 Dr Lee: Do you compare with the co-operative returns in America, where there are predominantly co-operatives owning the transmission network?

Andrew Wright: We do compare. There are several checks and balances on that. First of all, we are not the only regulator looking at regulating networks. You talked about Ofcom and others.

Q252 Dr Lee: If it is a monopoly provider presumably you can only have international comparisons.

Andrew Wright: Yes.

Q253 Dr Lee: Therefore, which international comparisons would—

Andrew Wright: We have international comparisons and I think our network costs—

Q254 Dr Lee: Which ones do you compare with?

Andrew Wright: The return on equity that the network charges in the UK for shareholder owned businesses, as opposed to co-operatives, I would compare favourably with those in the United States.

Q255 Dr Lee: All right, so you do compare National Grid's return on equity with the return that, say, the co-operatives in America do, also the co-operatives in New Zealand, or—

Andrew Wright: No, National Grid is a shareholder owned company. Once again we can revisit the public policy framework.

Q256 Dr Lee: So who are you comparing with?

Andrew Wright: It was decided 25 years ago that the appropriate ownership model was to privatise these companies.

Q257 Dr Lee: I am not talking about the past, I am on about now. Who do you compare National Grid with? What are your benchmark comparisons, with share ownership, transmission networks in other countries?

Andrew Wright: Are you talking simply about the return on capital? We compare it against all other similar regulated utilities, particularly in the UK because obviously the market conditions in the UK are fairly specific.

Q258 Dr Lee: So you compare with BT?

Andrew Wright: We would compare it with the returns offered by Ofcom, the CAA, and by Ofwat and, ultimately, the Competition Commission acts as the body of appeal for those decisions.

Q259 Dr Lee: So they decide that 4% is an acceptable return?

Andrew Wright: Yes. Recently the Competition Commission, for example, looked at Northern Ireland Electricity. Northern Ireland Electricity appealed their price control set by the Northern Ireland regulator to the Competition Commission, and they took a view on the appropriate cost of capital and return. Indeed, we are looking again at the returns that we are doing for the distribution companies in the light of that.

Q260 Dr Lee: In summary, you do not determine that 4% is an acceptable return. The Competition Commission do.

Andrew Wright: We determine it, but we determine it within the context of what is happening in the equity markets, so what returns similar companies give, which ultimately is a benchmark—

Q261 Dr Lee: Hang on a minute, you have just said it is a monopoly provider. How on earth can you compare that with an equity market that, by definition, is a market? I do not see how you can compare returns with an equity market—

> ***Andrew Wright***: No, National Grid has to compete for investment against other privately owned companies.

Dr Lee: Oh, come off it, if it is a monopoly provider it is going to be getting investment. If you know you are going to get a 4% return then you—

> ***Andrew Wright***: Sure, so we take—

Q262 Dr Lee: Why do they have to compete?

> ***Andrew Wright***: We adjust for those factors but the ultimate benchmark—

Q263 Dr Lee: How do you adjust for those factors?

> ***Andrew Wright***: Ultimately, an equity investor is going to have to look to see whether or not it wants to invest in National Grid or invest in an alternative company.

Q264 Dr Lee: Look, you can have a cheque from me. I will invest in National Grid, guaranteed 4% return, monopoly provider.

> ***Andrew Wright***: It is not a guaranteed 4% return.

Q265 Dr Lee: You just said it is.

> ***Andrew Wright***: No, it is not a guaranteed 4% return; it is a 4% return if they deliver the outputs efficiently for consumers.

Q266 Dr Lee: Yes, but what is your benchmark for them delivering that efficiently? I do not understand. You keep saying this is a benchmark and we are here to regulate to get a better return for the customer. Against what?

> ***Andrew Wright***: Because we scrutinise their business plans—

Q267 Dr Lee: Who are they competing with?

> ***Andrew Wright***: They are not competing. They are a monopoly, and what we are seeking to do is to try to put in place price controls that deliver good value for money for consumers that incentivise National Grid to reduce costs, improve its performance, improve its outputs and provide a return to its shareholders that is fair and in line with the returns elsewhere in the market for similar investments.

Q268 Dr Lee: Define "fair".

> ***Andrew Wright***: The checks and balances for that. There is a process where the Competition Commission will do exactly the same as us and will come up to its own view. Ultimately, that is the body for appeal. That appeal is available not only to the companies but is available to people who represent consumer groups as well. If anyone thinks that we are presenting too generous a rate of return for these companies, they do have the opportunity to appeal that, whether it is supply companies or whether it is consumer groups.

Q269 Dr Lee: Finally, so you think that having a monopoly provider is a good system?

> ***Andrew Wright***: I think it is inevitable when you are looking at a natural monopoly business, like transmission and distribution. If we could introduce competition in this market we would look at ways of doing that. We do it in parts of the value chain.

Q270 Dr Lee: That then begs the question, does it not, that if you are going to have a privately owned, shareholder owned company arrangement, perhaps that arrangement is not appropriate for the transmission of electricity and gas?

> ***Andrew Wright***: I think the combination of private sector incentives, combined with our effective incentive based regulation, has delivered huge value for money for consumers. Network charges have halved over the first 15 years since privatisation. They have gone up since on the back of the significant investment that has been needed. Over that period we have seen a 25% reduction in outages and we have seen the networks increasing in their size and extent. That has delivered tremendous value. Our network charges are among the lowest in Europe. That is partly because of our effective incentive based regulation that we have put in place. We have a really good track record on this and I am prepared to defend it to the hilt.

Q271 Chair: Reverting again to the ultimate cost to consumers of the scale of the capital investment that is needed in transmission and distribution, which clearly over the long-term is significant. There is another angle: it is not just about the charges that might be made by the monopoly providers, but it is also about the need. We have just been through an interesting process in Suffolk where National Grid proposed to build a new set of pylons across an area of outstanding natural beauty, allegedly to take account of the extra demand for transmission capacity that would result from the construction of offshore wind and nuclear power stations. It was perfectly apparent to anyone who looked at it that this provision was grossly premature—there was no possibility of any need for it well into the 2020s—but because it conveniently fitted into National Grid's timetable for capital investment, there was apparently a window. They put up the proposal, signed off by Ofgem with its guaranteed return on capital. I have to say that the system does give National Grid an incentive to say, "Let's spend more sooner," because they have the guaranteed return.

It has turned out in the last month that they do not need it after all. It was perfectly obvious to everyone that this was not needed. It was simply a way of National Grid inflating their profits. Because it happened to be very challenging and totally unacceptable environmentally, it was scrutinised rather more closely. It was a pity, was it not, that Ofgem did not look more carefully at whether this extra capacity for which the consumer is eventually going to pay, was needed?

Andrew Wright: Firstly, National Grid does not have an incentive to bring investment forward. If they can invest later then they will benefit from that. They will benefit from that from the shared incentives that I talked about before. It is not in their interests to invest ahead of need. It was in their interest to invest just in time. They have presumably reassessed the needs case and changed their decision on that. Once again, I am not hugely familiar with the specific case but I am aware of it.

The incentives are there to ensure that National Grid delivers its outputs as efficiently as possible and invests as close to need as possible. Obviously, there are risks on the other side, investing late, and those risks are quite significant. If you have a nuclear power station built at Sizewell that is not able to get its power away, then that is a serious issue. So you would expect National Grid to be looking early at these long lead time projects. You will be familiar with the Beauly-Denny and the North Yorkshire lines. They took more than a decade from original planning discussions through to completion. These are large, important, complex and appropriately well scrutinised investment decisions that National Grid needs to look at early.

I do not know the specifics on this particular case and why they have changed their approach, but the incentives are not there for National Grid to invest as much as possible as soon as possible. The opposite is true.

Q272 Chair: It is a pity that it was left to volunteer campaigners working in their spare time to uncover the fact that this extra capacity was not needed, rather than that job being done by Ofgem at the time the proposal was originally made.

Andrew Wright: I think that is a little unfair. As you well know with the nuclear power programme, originally there was meant to be at least one and perhaps two nuclear power stations built before the end of this decade. That was the original plan we were working to. With the benefit of hindsight, you could argue that was never going to happen. It is quite clear that investment in the new generation of nuclear power stations has been delayed somewhat from the original expectations. Similarly, there have been changes in expectations on offshore windfarms as well that you will be well aware of.

This is a changing environment and National Grid is incentivised to deliver these investments as close to need as possible: not too early, not too late. If they deliver it just in time then they will benefit most from that. Obviously, they are incentivised to deliver it at as low a cost as possible as well.

Q273 Chair: This particular proposal saw the light of day in September 2009. I do not think there has been any stage in the last four years that any even moderately astute observer of the energy scene would have thought that a nuclear power station was going to be built in Suffolk before 2025.

Andrew Wright: I am not here to defend National Grid's actions. I think you can ask National Grid to come in and answer their own—

Q274 Chair: It is complacency and feebleness in the face of excessive charging by National Grid.

Andrew Wright: That is absolutely wrong. National Grid has to respond to the connection request if EDF is asking for a connection for Sizewell B in 2019 or whenever it is. National Grid has a duty to respond to that. National Grid cannot say, "We do not think you can deliver that. We are taking a judgment about your business plans." That is not their role. Their role is to respond to the connection requests that come in. I do not know the details of this specific case but, knowing how National Grid behave and knowing what incentives they have on them, I suspect that is what they were doing.

Once again, it is not our or National Grid's job to question the plans that have been brought forward by generators with a request to connect into the network. It is National Grid's job to respond to those requests.

Q275 Chair: Is it not your job to pass judgment about whether very expensive new capacity is actually needed? There has been no stage in the last four and a half years—

Andrew Wright: We do—

Chair: —let me finish the point—when it could credibly have been claimed that Sizewell C would be completed by 2019. At no stage whatsoever has there even been a remotely credible suggestion.

Andrew Wright: We do do that. We absolutely do do that. Certainly, in the last—

Q276 Chair: But you forgot to do it in this case?

Andrew Wright: No. At the last price control, a lot of capital expenditure in the core business plans was taken out and put into uncertainty mechanisms. That means National Grid has to come to us and demonstrate the needs case on a case by case basis. That is also true of the Scottish generators with respect to the Ireland connection. We have seen quite a lot of those processes going on at the moment. For example, the connections to the Western Isles and the Moray Caithness connection. We have taken out a lot of that contingent investment that depends very much on specific generation investments and scenarios developing, and put it into uncertainty mechanisms for further scrutiny.

We also scrutinise what is in the core business plan as well. That is not the end of the story because National Grid is incentivised to deliver outputs on time or just in time, not to over deliver and not to deliver ahead of need. All of those incentives are in place. There is a difficult balance to make between, on the one hand, being accused of standing in the way of investments needed to connect renewables and nuclear power stations, and on the other hand making sure you have a flexible enough system to enable National Grid to respond to these large and difficult investments.

Q277 Dr Whitehead: Energy companies are moving customers who are in debt and cannot pay their energy bills on to prepaid meters. That is effectively disconnection by the back door, is it not?

Andrew Wright: Energy companies have an obligation to consider whether it is safe or practicable to install a prepayment meter when they do so. That includes taking into account the likelihood of self-disconnection. If that was happening on a systematic basis, an avoidable basis, then companies would potentially be in breach of their licence conditions.

Q278 Dr Whitehead: Do you have data on the extent to which different companies are moving customers on to prepay meters?

Andrew Wright: Increasingly, customers are being moved on to prepay meters in response to—I think you have seen the report that we published on the levels of debt in the industry. Levels of debt are increasing for obvious reasons. As a result we are seeing increasing penetration of prepayment meters. Millions of customers welcome prepayment meters, because they provide a means by which they can control and keep on top of their energy expenditure. It is clearly a concern if some of those customers are effectively self-disconnecting. I think companies have a duty to consider the individual circumstances of individual customers when installing a prepayment meter. If there is a risk that they are going to self-disconnect they should not be installing the prepayment meter.

Q279 Dr Whitehead: Do you have comparative data, company by company, of which company is putting what people on to prepaid meters and under what circumstances?

Andrew Wright: As you have seen from the report that we published a few weeks back on debt and disconnection, we certainly put information requests into the companies. We monitor their activity on debt recovery, debt and disconnection, the terms under which customers are expected to repay debt, making sure they take proper account of ability to pay and so on. We do all of that. We rely on a mixture of that monitoring activity, feedback and complaints from companies and consumer groups to detect if something is going wrong in that process. I am sure there will be individual instances when things do go wrong. What we are looking for, for a licence breach, is clear evidence of systematic abuse and systemic breach that is avoidable.

Q280 Dr Whitehead: Do you have data, company by company, so that you can look at trends in disconnection by companies, so you can start down a path of deciding whether a—

Andrew Wright: Yes. As you are aware, self-disconnection is pretty difficult to detect. We certainly have data, company by company, about disconnection but self-disconnection where somebody on a prepayment meter decides to not charge up their prepayment meter is difficult to detect in a world before smart meters. Therefore it is difficult to monitor. As I think some of the companies mentioned to you, they have processes in place to try to pick this up, but they are relying on vends—on the payments people make—to detect that. Obviously, there is a lag between picking up where somebody is not paying to charge up their meter and recognising there is a problem. A smart meter world potentially provides a solution to that.

Q281 Dr Whitehead: There is a stage before that, is there not, where companies may be putting people on to prepaid meters for different reasons and perhaps having different company policies about what it is that triggers such a move to a prepayment meter?

Andrew Wright: When companies put customers on prepayment meters, whether it is for debt recovery reasons or for other reasons, they are meant to have regard to that customer's individual circumstances. We do not have evidence that any company is systematically not fulfilling that obligation at the moment. If anyone does have evidence then obviously we would like to see it and we will take action on it.

We do monitor what companies are doing and we do report on it as well, through the debt and disconnection report that we published a few weeks ago.

Q282 Dr Whitehead: Do you have comparative data on which companies are placing people on to prepaid meters and for what purpose?

Andrew Wright: I would expect that we do have that information. We certainly know what the trends are in terms of numbers of customers on prepayment meters. We know we have information about the levels of debt for different companies. I am hesitating because I am not 100% certain that we know the reasons why companies are putting additional customers on prepayment meters and linking that into debt recovery, or customers volunteering to go on prepayment meters, or customers being put on prepayment meters in the first instance because of their credit positions.

I will come back to you and let know what our monitoring activity is and how detailed it is in this area because I do not know.

Q283 Dr Whitehead: You say you have no reason to believe that any companies are getting close to breach of their licence conditions by—

Andrew Wright: If we felt the companies were putting prepayment meters in place in circumstances that were not safe or practical then potentially that would be a breach of their licence conditions. As with all our licence conditions, we monitor compliance. We rely both on our monitoring and individual instances being reported to us by Members of Parliament, by consumer groups and by customers themselves.

Q284 Dr Whitehead: You have no proactive way to try to stop this?

Andrew Wright: We do. We do an awful lot of work with companies in trying to ensure they meet best practice in this area. I can give you the full information on exactly what we have been doing. We have done a great deal of work over many years, including publication of the vulnerable customer strategy that we put in place, and trying to improve performance in relation to vulnerable customers in general. That includes their handling of debt and disconnection. There are a number of licence conditions in place that they have to adhere to. They tend not to be very specific in nature but that is not all we rely on. We work very hard with the companies, in line with our duty to have regard to vulnerable customers, to try to make sure they are operating best practice in this area. Generally speaking, the companies work very closely with us and are very co-operative on trying to ensure that the vulnerable customers are treated reasonably well. As energy prices are increasing this obviously becomes more important.

Q285 Dr Whitehead: As far as standing charges are concerned, we have previously raised in Committee reports the issue of standing charges and, in particular, the suggestion that a standing charge is likely to penalise a low energy user and essentially reward a comparatively high energy user. Obviously that has a particular impact on those in fuel poverty who are using relatively low amounts of energy or trying to use relatively low amounts of energy, but are stuck with a standing charge on top of that, regardless of what they are using. What steps are Ofgem taking to address that particular issue?

Andrew Wright: Just to clear up some misreporting here, Ofgem does not require companies to have a standing charge. What we have done is require companies to have simple tariffs comprising, at most, a standing charge and a unit charge because we think that helps consumers understand. Previously a lot of companies had very complicated two-tier unit charges, which effectively did no more than disguise the standing charge in the first few units. We thought that was not fair to consumers because it was not being straight with them. It pretended that there was no standing charge when, for the vast majority of consumers, there was. It also made comparison of prices very difficult. In some cases it was even more complicated than that, with seasonal sculpting of these unit charges as well.

Companies are quite entitled not to have a standing charge if that is what they want to do. There is nothing we have done to stop them doing that. Indeed, I think there are some offers out there that are just unit charges. The approach we have taken on this is not to determine what companies do. Companies are entitled to recover their fixed costs through a standing charge if that is what they want to do. Once again, I think to go further than that would be us making a decision to effectively require companies to cross-subsidise one group of customers at the expense of another group of customers. That would not necessarily be beyond our vires but beyond our role as a statutory and elected regulator.

Q286 Dr Whitehead: Do you accept that there is a potential problem—

Andrew Wright: If you moved to a process of all costs having to be recovered through a single unit charge, inevitably that means that high users would lose out and low users would benefit from that. There would be a point at which people would be neutral, which would be close to typical consumption. So that would be the consequence. I would not necessarily say—

Q287 Dr Whitehead: Is that something Ofgem ought to be thinking of?

Andrew Wright: It is worth saying that fuel poverty is often associated with high energy usage, so it is not necessarily the case that that benefits disadvantaged customers. Because it is an implicit cross-subsidy between one group of customers and another, potentially it would be challengeable under the legal framework under which we operate. If that is a policy decision the Government wants to make, I think it would be one more appropriately made by Government. The comparison is the premium on prepayment charges. I think there is a similar issue there where we have a requirement on companies that those prepayment charges are cost reflective. It would be going beyond that requirement if we were to effectively say that prepayment customers had to be cross-subsidised by the rest of the customers.

What we are saying here is that if companies are putting standing charges in place that are cost reflective, then that is consistent with our duties. It is a redistributive policy that more probably belongs with Government.

Q288 Dr Whitehead: There are ways in which you can deal with the possible issue of cross-subsidisation without simply standing back and saying, "If you want to have a standing charge you can have one and we are not going to do anything more about that." There are things you have within your power to move beyond that, surely?

Andrew Wright: There is a range of standing charges from zero up to quite a lot. Certainly we would encourage consumers—particularly those on low incomes—to look very carefully at the standing charge. Clearly, if you are a low consumption consumer, not a low income consumer, you would tend to select those companies with lower standing charges. The retail market reforms we put in place mean it is easy to do that. A lot of the debate around standing charges has resulted as a fact of us making those standing charges transparent. Previously they were hidden from view, nobody knew they were there. They had exactly the same effect but nobody knew they were there. I think it is an interesting debate about whether or not standing charges should be allowed for distribution benefiting one group of customers compared to the other, but I do not think it is a decision that ought to be made by a statutory independent regulator.

Q289 Dr Whitehead: We had some correspondence just recently from a member of the public who stated that their energy supplier had increased the bill even though they thought they were on a fixed tariff. Is that simply a matter of the customer misunderstanding or is that something that Ofgem ought to look into, in terms of clarity about the type of product for somebody who is purchasing and the extent to which energy companies have a requirement to stick to what it says on the tin as far as their products are concerned?

Andrew Wright: I completely agree with you. That is why we have introduced a licence condition that is already in effect. That says that fixed term products must be fixed price. So "fixed" means fixed now as a result of RMR.

Q290 Dr Whitehead: All costs relating to what comes on to the bill of the customer?

Andrew Wright: If you sign up to one of the deals that you see advertised today, fixing your tariffs until the end of 2015 or whatever it might be, then that is an absolute fixed price and the company cannot change that without the prior agreement of the customer. That is a rule that we have put in place in RMR. Previously there were these so-called guaranteed tariffs that, in our view, were potentially misleading. Companies would guarantee that the price would be—let's say—no higher than 3% below the standard tariff. The customers were signed up at very low prices and they subsequently found those prices increased. The use of the word "guaranteed" often meant that consumers thought they were getting a fixed term, fixed price deal when in fact they were getting no more than a guarantee that it would not be any higher than the standard tariff.

I agree with you that that was potentially misleading. It is one of the factors that has led to the erosion of trust in the industry. We have put that right.

Q291 Sir Robert Smith: One of the impacts of the standing charge coming in is on the prepayment gas meters, where many people on lower incomes do not use the gas over the summer months and then when it comes to needing the heat suddenly they have to put in a whole load of money just to get the meter back up to scratch.

Andrew Wright: Yes. First of all, I think that is potentially an issue. The standing charge tends to be a daily standing charge. I can see how that could have an effect and how that could be annoying and difficult. Overall, if they are above a certain very low level of consumption, they will pay no more than they would have done under the previous complicated two-tier tariffs.

Q292 Sir Robert Smith: Over the whole year?

Andrew Wright: Over the whole year. But I can see how that can create an inconvenience and irritation.

Q293 Sir Robert Smith: For people on low budgets it is not just an inconvenience and an irritation, it is a cash flow crisis because they cannot heat their home.

Andrew Wright: That is an interesting point. If you permit me I would like to take that away and consider whether something could be done to address that particular issue, because it is not something that has been brought to my attention before. But I can understand the consequences of that.

I am aware of the technological limitations of old tech prepayment meters and the difficulties of making this work effectively. Once again, smart meters obviously provide a way forward there. I will take that away, look into it and see if anything can be done to reduce that issue because I can see how that would potentially create a cash flow issue for people.

Q294 Dr Lee: As you are no doubt aware, there has been quite a lot of activity in the energy policy period and then discussion about it between parties, particularly since the Opposition Leader announced his policy on freezing energy prices. What is Ofgem's response to Ed Miliband's suggestion of price freezing?

Andrew Wright: At the first level I am going to repeat what I said before, that it is the public policy framework under which we operate or under which another regulator operates. It is for the Government of the day to determine. It is absolutely right that these big issues are being debated by politicians and absolutely right that these options should be considered. We will work with whatever Government to make sure that the policies that are have operate in the interests of customers. We have obviously yet to see any detail of what the Labour Party proposes. We would be happy to work through that to make sure it is practicable. The sort of things we would consider is: does it have an adverse impact on consumers? That includes: does it have an adverse impact on the investment that is needed?

Q295 Dr Lee: Sure. I gather you have over 25 years of experience in the energy utility market. You must have an opinion on the merits of price fixing. As you might not be surprised to hear, I feel price fixing just displaces price increases. So what is your opinion?

Andrew Wright: I have talked already about price regulation as opposed to allowing markets to look at it, and price regulation clearly is an option, but it is obviously necessary to allow companies to recover the revenues that they need to be able to run their businesses effectively. They should have no guarantee of profits or of cost recovery, but an efficient business serving customers well should be able to recover the costs that they incur. Clearly any arrangement that does not allow them to do that potentially puts at risk investment in the industry, puts at risk the proper functioning of the industry and potentially becomes a windfall perhaps rather than necessarily a price regulation mechanism.

Once again, if that is the route the Government wants to go down then that is for Governments to decide, but we think it is important that there is a stable regulatory framework under which consumers and investors can make effective decisions in a marketplace.

Q296 Dr Lee: Okay. What you are saying is that they are going to need to retain the same income, therefore, for 20 months they will not and for the preceding period and for the period afterwards they will adjust accordingly?

Andrew Wright: Yes. There are two debates going on here. One I guess is whether or not we or anyone else should have the ability to regulate the end prices of customers. I think the other debate is whether or not there have been windfall profits, which effectively need to be clawed back from the companies. Those are two separate debates. Those are debates for politicians and not ones for us, but clearly we are concerned about maintaining investor confidence and, indeed, the confidence of consumers.

Q297 Dr Lee: Former Prime Minister John Major waded into it and suggested a windfall tax. Do you have an opinion on that?

Andrew Wright: I will have an opinion at a very high level, recognising a couple of things. First of all, a windfall tax needs a windfall. I think that is the first thing you need to establish; secondly, you need to be very careful not to undermine the regulatory contract that we have worked hard to establish, whether it is on networks or on generation, which means that efficient companies doing well, delivering benefits for consumers, potentially profit from that. Anything that undermines confidence in the market is detrimental to consumers. When considering such policies I think you need to be very careful about those consequences. I think that is true of politicians from any party, and a general point.

Q298 Dr Lee: You have a monopoly provider, National Grid, and you have six companies that hardly have changed their proportion of electricity and gas in the market. They are pretty stable. “Static” is probably a better word in terms of the proportion of electricity and gas each company delivers. So the definitions of the word “windfall” and “fair and proportionate” are in the context of the fact that these are essentially companies that have pretty guaranteed market shares, and a company like National Grid that has 100% monopoly virtually market share. The definition of a windfall in those terms is very difficult to make, is it not?

Andrew Wright: It is not difficult to make in terms of the regulated network. We regulate those companies and we set their prices. We do not give these companies windfalls. If they earn above their allowed cost of capital equity return it is because they have delivered additional benefits for consumers, either by reducing prices or delivering more outputs or improving service. I would not call that a windfall. I would call that a proper incentive for these companies.

Q299 Dr Lee: I detect that with price fixing, windfall taxes and everything else, you are not overly enthusiastic. Is that because you think the current system in play delivers a good return for the customer and for the taxpayer?

Andrew Wright: No, if we thought that the level of competition in the retail market was acceptable, we would not be making the dramatic changes to the retail market that we are making and we would not be doing the competition assessment with the OFT and CMA. For the last five years we have said that there needs to be action to improve the competition in the retail market and, indeed, action to improve access to wholesale market liquidity as well. These are things we have been taking action on.

There is a long way from saying the market is not working effectively as it should be to saying that there is a large windfall here. I think that would need to be established before you even start thinking about it.

Q300 Dr Lee: Specifically with windfall taxes, your earlier answer with regards to transparency of trading, to my mind. was somewhat opaque. It was like you did not really know everything about the trades and, indeed, if you knew about the positions that each company were taking, you could have anticipated where we are now in terms of discussing price rises. So it gave me the impression that you did not know about all of the trades and positions that companies are taking with regards to the wholesale market. Was that a fair—

Andrew Wright: Yes. It is fair to say that we do not know every individual trade that the company makes. That is absolutely fair, but you would not expect us to do that in the context of the competitive market.

Q301 Dr Lee: Building on that, is it possible that if a Government of the day announced that they were going to apply a windfall tax that these vertically integrated companies would, therefore, move all of their profits—shall we say—northward into their supply and trading arms and leave virtually an operating loss? And incidentally, I think EDF had an operating loss on its retail arm one year. So, therefore, there is no windfall tax because there is no windfall because there is no profit. Is that possible?

Andrew Wright: If you will forgive me, I am not going to start speculating about how companies might react to a policy that might be put in place by a current or future Government.

Q302 Dr Lee: I am not on about speculating. Is it possible that they could do that?

Andrew Wright: We do not control how the companies arrange and organise their affairs.

Q303 Dr Lee: I am not saying you do. I am asking you whether you think it is possible for them to move their profits into part of their company in their structure, so there would be no windfall tax. If you were trying to tax profits, which is essentially what John Major is suggesting, is it possible for them to move their—

Andrew Wright: It would not be possible for them to do it easily—

Dr Lee: But it is possible?

Andrew Wright: —through our segmental statements. I cannot say absolutely, because I am—

Dr Lee: So it is possible?

Andrew Wright: No. You are asking me to give an absolute assurance about something that I cannot give an absolute assurance about, because you are talking about how companies themselves organise their affairs.

Q304 Dr Lee: Forgive me, but Ofgem regulates the markets. Yes, is that right?

Andrew Wright: No, we supervise the market.

Q305 Dr Lee: Okay. You supervise the market, yet you are not able to tell me whether they are able to move their profits around?

Andrew Wright: No, we put in place the corporate segmental statements to give a clear picture of where the companies are making their profits between the retail business and the wholesale business. As I have said, there is no evidence that the companies are doing anything untoward.

Q306 Dr Lee: I am not suggesting there is. I am asking you whether it is possible.

Andrew Wright: As I have said, we put in place a lot of checks and balances to make sure the evidence that they are providing provides an accurate picture. But can I give you an absolute guarantee that the companies cannot find a way around that? No more than I suppose if you had someone from the HMRC giving you an absolute guarantee that companies cannot find a way around tax rules. It is impossible for me to do that. If they do, we will seek to respond to it.

Q307 Dr Lee: In the light of your responses to the first two questions on price freezing and windfall taxes, on which I will let listeners and viewers conclude what they want to conclude, I made a suggestion a few weeks ago about the benefits of a not for profit corporation being introduced into the retail and transmission sectors in an article in the *Observer*. The arrangement currently exists, particularly in New York, in Pennsylvania and other parts of America, also in New Zealand. What is Ofgem's view of co-operative arrangements in retail and transmission?

Andrew Wright: First of all, there are co-operative arrangements in retail. You had a representative of Co-operative Energy here speaking in front of you a few weeks ago.

Dr Lee: But it is very small.

Andrew Wright: Small but growing, but it is an option that is available. It is a brand that I hope people trust and are aware of. They have competitive offerings in the market and it is an option that consumers have to switch to, so those options do exist already and there are other not for profit players in the market as well. I would—

Q308 Dr Lee: But in the transmission there is not.

Andrew Wright: As I have said, in transmission there is a regulated monopoly of for profit companies. Our job is to make sure that the prices they charge and the service they deliver to consumers is absolutely as it should be.

Q309 Dr Lee: My understanding is that the set-up in New York and Pennsylvania is delivering low-cost transmission costs to consumers—

Andrew Wright: I think we are delivering—

Dr Lee: —and we have heard the Chairman's example in Suffolk about transmission. If a co-operative had owned the transmission network in Suffolk, I should not think that that project would have gone anywhere near as far along the line as it did. I am trying to tease out of you whether you think that there is, in your experience of—it is retail and transmission, because they are joined together, obviously by definition. If you only have one wire to each property, one pipe to each property, how on earth can you have competition in that market?

Andrew Wright: You have effective regulation of that market.

Q310 Dr Lee: You only have two commodities, electricity and gas.

Andrew Wright: The policy of putting monopoly utility networks into the private sector to be regulated by independent regulators, using incentive-based regulation, is a policy that has served this country well for the last—

Q311 Dr Lee: You think it has served us well?

Andrew Wright: I think it has. As I have mentioned before, up until a few years ago, we saw year on year reductions in network charges. Network charges have halved over the first 15 years since privatisation, at the same time as improving outputs, reducing power cuts and increasing the size of the network. There have been increases over the last few years, largely driven by the scale of the investment, and partly because the low-hanging fruit on cost reduction has been taken, so it is not possible to take half the costs out of these businesses again, having done so once already. If you look at our network charges in relation to the rest of Europe, then we have among the lowest network charges of anywhere in Europe, both in gas and in electricity. I think it has served consumers very well. America has a great diversity of regulatory models, some of which have been consciously modelled on the UK approach to network regulation; others are very different.

Q312 Dr Lee: Sure. I would agree with you that privatisation, CGB, but the gains have been had is my point. We are now at a position where we have a privately-owned company and a monopoly-like cartel-like oligopoly, however you want to describe it, retail energy companies. I wonder whether we have reached a point where the market is no longer delivering for the customer, whether we have reached a tipping point at which we perhaps want to say, "Okay, we have driven out all of the waste that was encountered under the CGB over a couple of decades. We are now at this tipping point where we need to perhaps revisit the way in which we structure—"

Andrew Wright: As far as network regulation, there is something true in what you say. We had to a certain extent reached a tipping point where the emphasis needed to be less on delivering further cost reductions and more on delivering investment and delivering smart solutions. That is one significant reason behind why we introduced the RIIO approach—RIIO is Revenues equals Innovation Incentives and Outputs—so the idea is to ensure that companies are properly incentivised, not only to reduce costs but also to deliver those improved outputs, whether it is connecting windfarms or delivering smart grid solutions for consumers.

As you saw from the fast-track announcements that we made for WPD just a couple of days ago, I think that is also proving to be a tremendous success. The companies are stepping up to the plate in terms of engaging with consumers and other stakeholders and putting in place innovative solutions to delivering the improved outputs for consumers. I would say the same for retail markets.

Forgive me for harping on about smart meters, but the requirement for an active demand side, the opportunities afforded by smart metering technology suggest to me that there is potentially a greater role for markets and competition, going forward, than there was in the past. If we were in a technologically static situation then I might agree with you, but I do not think we are. We are at the threshold of a smart meter revolution in the industry, but we have only just begun on that path and I think that would be the wrong time to give up on competition in markets.

Q313 Ian Lavery: Just very briefly, Dr Lee mentioned the trading of the energy companies. There seems to be some sort of mystery behind the trading. As a regulator, are you absolutely convinced that the trading is being carried out in a wholly transparent fashion?

Andrew Wright: I have to think carefully. You are putting quite a high hurdle, "absolutely convinced". There is no evidence to say there is anything untoward happening. What companies do on trading is straightforward. That does not necessarily mean it is possible to get a complete assurance that nothing untoward is happening, but there is no evidence to suggest that there is. This is one of the things that we are looking at as a part of the review of transparency. We have talked about this a lot on this Committee and we have agreed to take it away and look at it again. Some of the companies, SSE and Centrica, who have predominantly focused on UK activities, have been quite transparent about their trading profits. I think SSE talked about a £6 million loss in 2012 and Centrica talked about a £20 million profit; forgive me if the numbers are slightly wrong. That is consistent with the sort of figures that they report in their group accounts, which are largely focused on UK activity.

When you go to other companies, EDF, RWE, E.ON, these are large multinational companies who operate their trading books on a pan-European basis. The UK activities, although not a small part of their business, are not the largest part. Although you can see what profits they make out of trading on a group level, how much of that is attributable to the UK remains to be seen. The evidence we have suggests to us that there is nothing untoward going on, but getting the level of scrutiny of those international trading businesses to be absolutely certain is difficult and expensive. That was the crux of the dilemma that led us to reject that BDO recommendation. The solution is not easy. We are looking at it again, but finding a proportionate solution to that is not easy.

Q314 Ian Lavery: As the regulator, do you believe that it is possible some of these companies are trading with themselves, buying off themselves at above the wholesale price and passing that extra cost on to the consumer? Is this just a myth or do you think this is quite possible?

Andrew Wright: There is no evidence to suggest that is happening, and I think you would see quite a big difference between the prices that they sell power at and in the generation arms that they buy. There are external checks and balances on this that can give you some assurance that, if that is happening, it is not happening in a way that is enabling these companies to take billions out of the UK business into an international trading arm. To give you absolute assurance, I would need to see everything that was going on over their pan-European business. It is not even certain that we would have the power or authority to do that.

What I would say is I urge the companies to do as much as they can to reassure you and the general public that is not happening. There is no evidence that it is happening, but if they could do more to reassure people, that would be the quickest and easiest way, rather than us trying to find ways of trying to understand what is happening in their Düsseldorf trading arm, for example.

Q315 Ian Lavery: Do the companies have an obligation to report their trading figures to Ofgem?

Andrew Wright: No, they do not.

Q316 Ian Lavery: Is there a reason why that is the case?

Andrew Wright: It is something we considered as a part of the transparency. As I say, this is the issue that we have discussed at great length regarding whether or not we should put an obligation on companies to publish their trading profits. We took the view that did not provide value for money for consumers. The extra information it would provide would be too expensive to get and that would end up potentially leading to higher prices for customers. We are revisiting that—at least in part—as a result of the representations made by this Committee. That is the project we are looking at at the moment. If we can find a way of doing that that does not put an unnecessary burden on consumers' bills, then we will try to find a way of doing it. For the point that has been made, it is probably necessary in the current environment to go the extra mile to rebuild trust and transparency in this market.

Q317 Chair: I would not want this session to end with National Grid thinking they were being particularly targeted by me. I have similar concerns about the distribution networks, who also offer a monopoly effectively, perform a monopoly function in the areas for which they are responsible. UK Power Networks, which is a foreign-owned company, has a monopoly in my constituency. Can you tell us anything reassuring about Ofgem's scrutiny of the charges made by the Power Networks?

Andrew Wright: Yes. First of all, I can repeat what I said about the long-term track record here, which I think is second to none as far as delivering value for money for consumers from these networks. The benefit of the regulation over the last 25 years has been huge, both in terms of improved performance and reduced costs. Bills would be a lot higher were it not for that delivery of improved performance from those networks.

In terms of what we are doing at the moment, we are in the middle of the price control review of the electricity distribution companies. Just on Monday, we announced that one of the companies had put forward a business plan that we thought delivered good value for money for consumers. The incentive-based process that we have is key to this. Us sitting on top of these companies trying to manage these businesses on their behalf would not deliver the value that is delivered by giving the companies the incentives to go away, reduce costs, and deliver improved outputs for consumers, because they potentially can benefit from that. That incentive-based framework is absolutely critical to this. In some respects it is an innovation brought forward by UK regulators—Stephen Littlechild, among others—and has been adopted around the world as a model for efficient regulation of electricity networks.

Q318 Chair: It is easy to understand why transmission is a monopoly business and you made that point very strongly earlier on. Do you think that the local distribution also has to be a monopoly or are there a lot more opportunities for introducing competition?

Andrew Wright: There are more opportunities for introducing competition and we do have a number of independent distribution network operators and gas distribution networks, IDNOs, as they are called. It is difficult to introduce competition because the pricing and charging structure is an artificial one to some extent. It is quite difficult to create the appropriate revenue line for independent operators in that market and you have to ensure that the network operates as a coherent whole. But there have been independent developers of things like housing developments and business parks where independent network operators have taken some market share from the monopolies. But inevitably, given it is a natural monopoly, such competition is likely to be at the fringes, generally speaking.

The other developments there, metering of course used to be a part of distribution network activities and now that is part of a competitive market as well. We are also seeking to open up competition. We have opened up competition in the connections market as well and are seeking to try to make that competition more effective.

Q319 Chair: Is there any comfort you could offer to an SME in my constituency that wanted to connect two classrooms that were being built for training purposes, and were quoted a charge of £55,000 by UK Power Networks for making a connection that was only a few metres away from existing lines?

Andrew Wright: Once again, all I can say is there are appeal processes for determining any disagreement between the network companies and the customers about connection charges, and we are introducing competition or competition has been introduced into that market. Whether or not it is fully effective is another question. All I can say is that there are mechanisms whereby, if people are unhappy with connection offers, then they can do something about it.

Q320 Sir Robert Smith: Just returning to the other place where there is no competition is in the Dynamic Teleswitching, Total Heating Total Control-type markets. What are you doing to keep monitoring that? I think some of your reassurances are based on your past assessment, but there have been fairly hefty price rises in this latest round.

Andrew Wright: We will continue to monitor that situation. If there is any evidence that companies are abusing the lack of competition in that market for those customers, then we will clearly seek to take action there. If you have any evidence that is happening, then we would obviously like to hear about it.

The other thing, we are not resting there. We are working with the industry to try to establish both short-term and longer-term solutions to the issue. A longer-term solution once again is obviously smart metering—

Q321 Sir Robert Smith: But that is a while away.

Andrew Wright: It could be a while away, but one thing we might be able to do is—and it is probably worth exploring—whether or not these customers could be prioritised in the rollout of smart metering, if that can provide a solution sooner rather than later. You can rest assured that, although it is proving a difficult issue to address, we are not sitting back and just accepting the situation as is. We do want to see more competition in that market and we want to make sure that in the meantime those customers are not treated unfairly.

Chair: Thank you very much. We have covered quite a wide range of issues this morning. We are very grateful for your time.