HOUSE OF COMMONS

Business, Energy and Industrial Strategy Committee

Oral evidence: CMA's investigation of the UK Energy Market, HC 982

Wednesday 22 February 2017

Ordered by the House of Commons to be published on 24 February 2017.

Watch the meeting

Members present: Mr Iain Wright (Chair); Albert Owen; Michelle Thomson; Anna Turley; Chris White.

Questions 102–168

Witnesses

I: Lawrence Slade, Chief Executive, Energy UK, Audrey Gallacher, Director of Retail Energy Supply, Energy UK, Dermot Nolan, Chief Executive, Ofgem, and Rachel Fletcher, Senior Partner, Consumers and Competition, Ofgem

Examination of Witnesses

Witnesses: Lawrence Slade, Audrey Gallacher, Dermot Nolan and Rachel Fletcher.

Q102 **Chair:** Good morning. Thank you for coming to the Select Committee. We know you, but, just for the purposes of the record, could you introduce yourselves and say which organisation you are representing?

Lawrence Slade: I am Lawrence Slade, Chief Executive of Energy UK, the trade association looking after lots of generators, and independent and major suppliers.

Audrey Gallacher: I am Audrey Gallacher, Director of Energy at Energy UK, and I look after retail supply.

Dermot Nolan: I am Dermot Nolan, CEO of Ofgem, the independent energy regulator.

Rachel Fletcher: I am Rachel Fletcher, the Senior Partner for Consumers and Competition at Ofgem.

Chair: Thank you. Dermot, may I start with you?

Dermot Nolan: My apologies, Chair. I just appear to have thrown water all over my desk. My apologies.

Q103 **Chair:** That is okay. If I continue to start with you, in the recent price increase by npower, Ofgem are quoted as saying, "We do not see any case for significant price increases where suppliers have bought energy well in advance. Npower must therefore justify the decision to its customers". Is there justification for any price increase by any energy company at this time?

Dermot Nolan: Chair, first of all, I am happy to be here—me throwing water around notwithstanding. On that, there can be explanations for price increases by specific companies, in the sense that one thing we have seen in the market over the last year or two—we have seen some evidence of this in the range of prices or lack of changes in prices so far—is certain companies have adopted different strategies vis-à-vis their efficiency, perhaps in the way they have hedged and bought electricity. That can account for different price movements.

Of the four larger companies, we have seen one increase prices by close to 10%, while another announced a price freeze for another six months. To me, that is some evidence that companies have made different decisions about efficiencies and have different actual costs, which in some sense is a symptom of a market that one would hope is showing some level of competition. In that sense, I can see a situation where it is entirely possible that a particular company, which may be less efficient than another, may have raised prices simply because its own costs have risen.

What I was doing when I spoke more generally, perhaps, in January was saying that I did not see an obvious case for significant price rises across the market. I was looking on average across what we would call the range of standard variable tariffs. Based on the information we had on that time, we did not see a case for a significant rise by most firms.

Q104 **Chair:** What is significant in 2017? Is there a justification for any price increases at the moment, and what would those be? What would be reasonable in respect of being fair to customers and then allowing energy companies to cover their costs? Is any price increase reasonable at all?

Dermot Nolan: I realise I did use the word "significant". In one sense, given the essential nature of the service of energy, any price rise can be described as significant. As I said, at the time we were commenting, in mid-January, what we were seeing was the wholesale cost of energy, which is an important constituent of it, had risen considerably over the last year. It had risen by roughly 15%, mainly because of rises in the prices of gas and fossil fuels. In that sense, we saw those costs rising.

However, the overall cost of energy, including electricity and gas together, was still approximately the same and in fact marginally below what it had been three years ago. That is looking at nearly every aspect of cost; there are certain not covered, which I will come to. In that sense, three years ago we thought the average level of cost was similar. Therefore, it does not seem compelling to us that, in fact, there should be a significant price rise at this point.

I will make two further caveats on that, if I may, Chair, however. One is that the comments were made at that time. Those were comments made in January about figures we had seen from December. Regardless of what was said then, future costs will undoubtedly at some point have an effect on future prices. If costs rise or continue to rise, then it is likely there will be a case for a change in prices. Alternatively, if costs fall, you would expect prices not to rise anymore and perhaps start to fall again. It will depend upon the future movements of costs. Ultimately, I would say costs are the main driver of prices.

My second caveat is that we have focused—understandably, because in my view it is the biggest problem in the market—on standard variable tariffs, which roughly about 65% of British residential energy customers are on. Obviously, that is where the movements were announced. Roughly, the remaining amount of customers tend to be on fixed tariffs, one-year deals or sometimes two-year deals, which over the last few years have been somewhat lower in price than the standard variable tariffs. In some sense, those prices started to rise in the second half of last year in any case.

If you look back to, say, June 2016, if you look at the top five cheapest deals in the market for a one-year dual fuel bill, you would have found something for £720 or £730 for the following year. As wholesale costs started to rise in the second half of 2016, that changed. Now, the cheapest deal is around £840 or £850.

Q105 **Chair:** You see a direct correlation there. The cheapest deals have moved upwards in respect of wholesale energy costs.

Dermot Nolan: Yes.

Q106 **Chair:** Where does hedging come into that?

Dermot Nolan: Hedging strategies are ultimately choices for firms. If I may paraphrase—I hope I am paraphrasing correctly—the firms have generally said to both the regulator and to the competition authority that typically, particularly for their standard variable tariff customers, they hedge well in advance: 18 months or perhaps two years in advance.

In particular, when wholesale costs started to fall in 2014-15, at the time a number of firms said, "It will take time for this to be reflected in price falls, because we have hedged sufficiently far in advance. It will take time". The CMA investigation broadly supported that many firms tended to hedge a lot in advance. It varied, but in that sense our feeling then was that if, indeed, it took prices a while to react to the fall in wholesale costs, that must be true on the upside as well. If wholesale costs are rising, then retail prices for SVTs should also be smoothed out.

Chair: That is very helpful. I have a flurry of Members wanting to come in.

Q107 **Chris White:** Good morning. I just have a quick point on something you said about prices going up and down and "showing some level of competition". That does not sound a terribly positive statement. Is the competition not where you would like to see it?

Dermot Nolan: It is not where we would like to see it, although it has also improved somewhat. I would go back to the CMA report, which was finally published last June. I think I can paraphrase it: it broadly said that it was a two-tier market within the retail energy sector. Certain aspects of fixed deals were working well, but there had been a large amount of entry into the market. We now have many new suppliers offering quite competitive fixed deals.

They also said, as I said, that nearly two-thirds of the people in the UK are on standard variable tariffs, where, on the whole, they are not getting good deals and where the level of engagement is relatively low.

Q108 **Chris White:** I want to bring you back to the point. I am sorry. You said "showing some level of competition". By extension, are you saying that these organisations are working together and not being competitive?

Dermot Nolan: No, I am absolutely not saying that. I am saying that within a segment of the market characterised by standard variable tariffs, the CMA's own analysis suggested that they had something akin to market power; because of the lack of engagement of many of their customers, they had the ability to raise prices above a competitive level. The measures the CMA has recommended and we are putting in place would ultimately reduce that power, allow them to become more engaged and ultimately lead to lower prices.

That is very much the course we were set on. I was not in any sense saying that there was any co-operative behaviour between the firms.

Q109 **Albert Owen:** I have a couple of questions. First, I have a question for Ofgem and Dermot, but it is also for Energy UK. One of the reasons for the move that npower gave in their statement—I am quoting here—was "the cost of delivering on Government policies". I assume that applies to every company, whether they are the big six or the independents.

Can we expect that to be a driving force in putting prices up in the near future? What are those costs? Again, I am quoting from memory here, but they mentioned smart metering and, also, possibly, the green levies. That is what they were talking about. Do you have a comment on that? Certainly, does Energy UK have a comment? The reason we are annoyed with npower is because they were sitting where you are when we were questioning EDF, who were putting their prices up. They did not say a bloody word to us—excuse my French—and within days they put the prices up. As a Committee, we deserve a bit more respect than that.

Dermot Nolan: I will do my best to answer the question about costs. As I said, we published something we now call the supplier cost index. The main purpose of that is to try to bring some understanding as to what is driving costs in the market on an ongoing basis. It is not a perfect index. There is no one perfect index that captures the entire energy market in one number, but we hope it will bring some value and understanding.

What that suggested to us over the last year was, as I think I said to the Chair earlier, that there had been a 15% rise in costs at the end of 2016 compared with last year. Of that 15%, 12.5% was essentially fossil-fuel price rises. The rise in the straight wholesale price was predominantly driven by increases in the price of gas, coal, oil, et cetera. Roughly about 2.8% was Government costs.

Albert Owen: It was less than 3%.

Dermot Nolan: Yes, it was less than 3% of that 15%.

Q110 **Chair:** This is an important point, Dermot. On that point, they have justified their price increases of something like 14% based upon Government policy. That is disingenuous, is it not?

Dermot Nolan: Can I make one further explanatory comment, Chair, and then I will come back to that point? I am afraid it comes back to my comments about no index being perfect. I was not here at the time, but I certainly look back to 2013, when there was a very significant set of price increases. I am probably woefully mischaracterising it, but there was a sense that prices were rising considerably. Firms were pressured, and we were told they were profiteering. The firms—not all, but often—reacted by saying it was a Government policy issue.

One of the reasons we are trying to bring this index forward and trying to have some trust and confidence in it is to try to bring some sort of clarity to that. I would say that, over the last year, yes, any increases in cost have been predominantly fossil-fuel based, not based on Government policy.

However, my caveat is the following. I said the index is not perfect. What it does not cover—because we cannot expect to measure the supply costs of every particular firm every three months, which is the period we are committed to—is the actual supply and retail costs to firms, and nor does it attempt to measure smart-metering costs. Now, there are some general measures on that. The Government has done a cost-benefit analysis on the costs of smart metering, but our index by itself does not cover smart metering.

There were comments from a number of the firms where they said, "Well, it might be due to Government policies or it might be due to smart metering". The argument about Government policies is not particularly valid on this point. Smart metering is not covered by the index; I accept that. In terms of my own view—looking at what we have seen, having talked to the firms, and looking the Government's cost-benefit analysis—smart metering by itself will not be driving significant increases in cost.

Q111 **Albert Owen:** Can I come back to the Chair's point? What you are saying is that the other companies are either absorbing these costs or they basically do not exist.

Rachel Fletcher: Perhaps I could come in at this point. It picks up on the point about whether we feel there is a competitive market. In a vigorously competitive market, if there were cost pressures coming externally you would expect companies to be taking every step they possibly can to offset those cost pressures through making internal efficiencies. There are some signs some energy suppliers are doing just that. This goes right back to Dermot's initial point. We are now seeing very different pricing strategies for standard variable customers in the market, with a difference of around £140 between the largest suppliers.

That is some indication that some companies are being more effective than others at absorbing those external cost pressures and becoming more efficient themselves.

Q112 **Chair:** Dermot, I have a question. Then Lawrence obviously wants to come in. I just want to take you back to the comment you made when npower put their prices up. "Npower must therefore justify the decision to its customers". Based about what it has said about the wholesale prices and about Government policies, have they justified that price increase?

Dermot Nolan: It is hard for me to judge whether they have justified it. I have two points. I will try to answer you directly. One is that npower's costs may well be higher—I find it a little awkward to talk about a specific company—than those of many other companies. A number of companies, including the big ones, have had significant IT problems—that is, cost issues in the last three or four years when they have put in IT systems. As a result, their costs may now be higher than those of other companies. Frankly, without criticising people, they may not have dealt with the situation very efficiently.

If you look, every year we publish profitability figures for the preceding year for the major supply companies: npower was not profitable last year. I suspect, for various reasons, its costs are higher than many of the other companies, at least for now. They have not been able to reduce those costs and, consequently, they have tried to raise their prices as a result. In a market where we hope to see effective competition, the question is whether that price rise will potentially be profitable. Frankly, the hope would be that it is not. If indeed they raise their prices more than other companies and lose a significant amount of customers, the price rise will not have been profitable. Then there will be some evidence the competitive market is working.

Q113 **Chair:** But that does not tend to happen. When we had them before us, they basically admitted to us that something like 55% of their customer base are on standard variable tariffs, which are the most expensive tariffs. They feel complacent in being able to put up their prices by an astonishing amount, 14%, and thinking people will not switch as a result of that. The market is not working for customers. What can Ofgem do to make sure it does work?

Dermot Nolan: I have two points. I agree, Chair: the market is not working effectively—certainly for all customers. That was the result of the CMA's inquiry. As Rachel and I have indicated, it said it is a two-tier market. There must be a situation in which a company cannot raise its prices and expect people to be sticky, if you like, and stay with them.

In that sense, the focus of the CMA remedies was on trying to make people much more engaged within the market. There are a variety of potential remedies in place. One is to trial various types of ways of becoming more engaged with the market. There are a number of trials we are now starting to run with companies, which Rachel could speak to.

Another was the admittedly somewhat questioned database, which we are trialling in a different way to try to bring, over time, that sort of engagement to the market. We want to bring that sense that customers cannot be taken for granted, and that if a company raises its prices unreasonably, the customer will find it easier to switch.

Q114 **Chair:** I want to bring Chris in, but I really need to push you on this, Dermot, if I may, in terms of the second sentence in that remark: "Npower must therefore justify the decision to its customers". I would expect Ofgem to determine whether justification is appropriate and reasonable and, if not, what will you do about it?

Dermot Nolan: If not, all we would do about it was say we did not think it had been justified. I should stress that we do not have the power to tell Ofgem to tell npower or any company to change its prices.

If I may, we can speak in public about it. We rarely speak about specific companies, but in this case we thought we should. We can say, "This seems unjustified to us". We can say, as we did, that the best response is for customers to engage and switch. We can put in place various measures that will make it much easier to do that. But we have no direct power to say to npower or any company, "You must change your pricing".

Chair: We will come on to powers that Ofgem can and possibly should have in a moment.

Q115 **Chris White:** I have a quick point. Do you know another market where you can buy identical products and where one of the main companies can increase their product price by 14%? Is there an element of complacency? Are the entry barriers so high that npower knows it effectively can get away with its price increases?

Dermot Nolan: I have a couple of points. Electricity is, in some sense, as you say, a relatively rare consumer market. Products really are identical. There is customer quality, which is quite important, and we want to bring more details out about that, but they are essentially, if I might use this phrase, homogenous products. But they are also products that are bought without an obvious prompt for future engagement. Certainly, the model for some companies has been to buy someone on a cheap deal and then let that deal go up over time and hope the customer is not engaged and hope the customer does not react.

One thing I will say is that I do not think that issue is unique to energy. Without necessarily casting the net widely, if you look at products such as insurance, home insurance or motor insurance, you see similar kinds of levels of price changes, simply because the customer has engaged. The Financial Conduct Authority did a study of the home insurance market just over a year ago, which suggested that people who had not changed their insurance provider in three years would be paying 35% more than a new customer and in five years would be paying 70% more than a new customer.

These problems are not unique to the energy market. The problem, to me, intrinsically seems to be partly barriers to entry. But that is not the biggest issue, because we have seen a lot of new entry in the last period of time. It is the sticky customer—the customer who is on a deal, who does not feel confident, engaged or secure, and does not find it easy enough to switch away. That is the core of the problem the CMA wants us to attack.

Q116 **Chris White:** I just have one last, brief question. Thank you for that answer. I do not understand the insurance market at all, but I would imagine there are a lot more players in the insurance market than there are in the energy market. We are talking about the big six. If you were in front of this Committee again in a year's time, five years' time, 10 years' time, will we stop talking about the big six because of behaviour like npower's? Will it be the big 20 or will it be the big two?

Dermot Nolan: I do not know, but I will speculate. I really do not know, and predicting the future is dangerous. There is some sense that the idea of the big six is changing. At least two firms who have entered in the last three years are beginning to rise in terms of residential customer numbers to something close to the smaller of the big six firms. We are not quite seeing the big eight or nine, but we are getting there. We have also seen a lot of new entry into the market, sometimes regional, sometimes not. We currently have over 40 suppliers.

Having said that, the share of what we traditionally call the big six is still 84% of the residential market. Certainly, I would like to see change in that over the next five or 10 years—significant change.

Rachel Fletcher: Perhaps I could add that over the last year we saw a reduction in the shift of consumers away from the largest six energy companies compared with the previous year. There is not a clear picture of exodus from the large energy companies to the smaller ones.

Q117 **Chris White:** Can you explain that? Do you know why that reduction is happening?

Rachel Fletcher: Quite a lot of it is that the larger companies are fighting back with very competitive deals for the more active customers. That part of the market, frankly, does not concern us. There are real signs of vibrant competition. What deeply concerns us, and where all of our focus as a regulator is, is trying to break the complacency, as you say, for the market for standard variable tariff customers.

Q118 **Chair:** I am going to bring Anna in, but, Lawrence, you have been very quiet. Do you see any justification for any price increases at this time?

Lawrence Slade: First and foremost, Chair, thank you and your Committee members for inviting us along. I will give you all the respect you are due. I would agree a lot with what Dermot and Rachel have been saying. The publication of their index recently is a good step forward towards bringing more transparency into the market and showing how the market operates. It is plain that we have seen increases in wholesale prices over the last 12 months or so—and indeed we can see, going out into the future, it certainly looks like there are continuing pressures there.

I would not underplay the issue relating to policy costs. They are forming an increasing percentage of the bill as we go forward. We are looking at somewhere in the region of £120 to £140 being added to the average customer bill next year, and we are seeing that rise, using public information, out to the 2020s. It is an important aspect that any company—that is any of the companies operating in the market—are going to have to be looking at when they are making their pricing decisions.

Q119 **Chair:** How is it that some companies absorb those costs, as we have heard from Ofgem, and others cannot? Are some of your members quite poor companies in the sense that they are not very efficient or not very customer focused? What is the range of members you have? You have successful, innovative companies who can control their costs, who hedge the prices in a successful way, and then you have failing companies, have you not?

Lawrence Slade: I would not go quite so far as to say we have failing companies at all, but you are certainly right to point to the fact that we have a very good cross-section of the market in our membership. I am very proud of the fact we have seen so many new entrants come into the market. You cannot stereotype one company across the whole scene. Each company has a very different strategy and they will be looking at how they are doing that.

I would pick up on Rachel’s point that we are starting to see much more competition coming into the market. We have seen exponential growth—I use that word appropriately, I feel—over the last 12 months, for example, in the number of people switching. We have seen recent research published that points to a much higher percentage of new customers entering the market. We would point to voluntary work or voluntary actions the industry has taken, for example, in introducing an energy-switch guarantee to give customers that confidence.

What we see is a market that is much more competitive and a market where companies are starting to have competitive pressures really exerted on them. If you do not fight for those customers, they will go. That is why we are seeing market share drift; that is why we are seeing new entrants come into the market and growing their market shares; that is why you are seeing this shift in attitudes from customers.

What Dermot and Rachel are perfectly right on is saying that more has to be done to reach out to those customers who have not engaged in the market yet. That is where our efforts need to be focused: to make sure that, as we move forward, as we roll out smart meters, as we invest in digitalising this industry, we also make sure we are not leaving any customers behind. In this process of starting to put customers in control of their energy, we have to make sure we are reaching out and making sure that everyone can do that. That is a really important point that we must not underestimate.

Q120 **Chair:** Is a 14% increase in the bill acceptable?

Lawrence Slade: I cannot comment on that from an individual perspective, but I can point to the fact that, if I look at the market overall, as I say, there are wholesale price rises and there are increasing cost pressures on the bill. For example, if I look at the cost of buying energy today for March delivery, it is 100% higher compared with last year for gas and 69% higher for electricity. That is in the month-ahead market, which is one of the different markets that are available.

What that says to me is that companies are taking different strategies and there are different strategies at play in this market. Yes, some are going to be better at it than others. That is a market, as Dermot said.

Q121 **Anna Turley:** I want to come back in a minute to the link between costs and prices again, because that is really important and there is more to explore there. Just picking up on the last point you were making about getting more people engaged in the market and getting more people active, I am sorry to ask a real sort of layperson's question here but why should people have to keep changing their bills, keep looking at their energy prices, and feel like they are being ripped off and have to try to protect themselves against being ripped off?

Surely this is the wrong way around. Surely people should be able to trust the company they are with, know they are getting a good deal and just be able to get on with their lives—and all the other issues. Why are we putting this onus on people all the time to play the market, when the majority of people are just trying to go about their business and want to pay for a fundamental utility to support their life?

Lawrence Slade: There are a couple of points in response to that. First and foremost, we are spending quite a lot of money and time making it as easy as possible for people to engage. That includes voluntary initiatives to reduce the time it takes to switch. It includes, as I said earlier, things like the switch guarantee. There is a commitment to work with Ofgem to speed up switching even more. The actual time it takes an individual, if you went online now and you had your recent bill to hand, to switch supplier is only about 15 minutes.

Let us not get carried away. We need to understand that the actual action is not very intensive. That is the first point: we are doing as much as we can to make it as easy as possible. We need to work with Ofgem as an industry to make sure the trials, happening either at the level of the individual companies or at an industry level with Ofgem, are as effective as possible and that we learn from those how best to engage with customers. Wherever we can, we should be sharing best practice to make sure we are getting to people in the best and most efficient way.

Furthermore, to go on from that, you are also seeing the competition element come in, which, as I say, is also helping drive prices down. We are doing all of those. We need to be more transparent and clear about how we are regaining trust with those customers.

Q122 **Anna Turley:** I am still struggling with the idea that getting people to switch is the main driver of driving down energy costs. It just seems to me that that is an irresponsible deflection of responsibility.

Lawrence Slade: You are right to point this out. It is not just getting people to switch supplier; it is getting people to engage with their current supplier. Not all customers are alike. Not surprisingly, I am quite happy engaging with my energy company. I manage my account entirely online. I do not have any paper documents. I pay by variable direct debit every month. That means I get the best tariff I possibly can on the market. Not everyone is in the position to do that. Not everyone can manage their account online or wants to manage their account online.

That is where engagement is absolutely key. It is about making sure we are reaching out to our customers, we understand what they want and we are getting them on to the best deal for their circumstances. I know it is tempting to think there is one size that fits all. Six years ago, when I joined the industry, that was my view—but it does not work like that. What that does mean is we have to be better, as an industry, at understanding customer needs. Again, that is happening.

We do see this sea change. It is certainly something I and my colleague Audrey challenge businesses on all the time: "How are you engaging? What are you looking at? How are you looking after your customers?" I think we are seeing that change. I would probably agree that probably has not happened fast enough and we have not been good enough in the past. Is the industry committed to it? Yes, I think they are.

Q123 **Chris White:** Can I follow up very quickly on that point? The word "complacency" has been used a couple of times in this Committee. You said that to switch takes 15 minutes. Do you want to expand on that statement for the whole of society, the people who may not have online access or who may not be aware of their bills? Would you like to go a bit further on what those 15 minutes would contain?

Lawrence Slade: Thank you, Mr White. You are quite right to bring that up. That is for someone who has access to the internet and who has all the relevant information in front of them. We did a test run in the office yesterday, so that is what I was referring to.

What we are trying to do is make the process as easy and as straightforward as possible for everyone. As I said to Ms Turley's comment, we need to make sure the facilities are in place so we are not leaving any customers behind. Equally, that applies if you are switching within your own company—that is, you are ringing up your supplier at the end of a fixed term deal and saying, "I note from your recent invoice and statement that my fixed deal is coming up. Have you got a better deal for me? How can I bring that on?"

It is not just about switching. It is about how easy we are making it for everyone in society to engage with the industry.

Q124 **Chris White:** I do not want you to answer this, but I just would suggest to you that if you were starting from a premise that this is going to take 15 minutes, the industry has got quite a long way to go.

Lawrence Slade: I agree we are not there yet. I would not disagree.

Q125 **Chair:** Lawrence, for you the key to having a more dynamic market that serves customers, which we currently do not have, is greater switching.

Lawrence Slade: It is greater engagement, Chair.

Q126 **Chair:** Okay. Is it unacceptable that, essentially, many energy companies' business models involve having a sizable proportion of their customer base on the most expensive price they provide and having stickiness because they do not engage? That is unacceptable.

Lawrence Slade: That is a picture of the past; it is certainly not a picture I see going forward, Chair. I see a picture going forward where we are working to further engage customers and to make sure we do not have that situation.

I would also just make the point quickly that we have to bear in mind that this is not one single market. There are different suppliers out there. Some suppliers only offer SVT models. We need to understand that you have to look across the scene at the volume of different suppliers who are offering different pricing models.

Q127 **Chair:** I am sorry, Lawrence. That just simply defies credibility. About a month ago, we had npower sitting there and they said they were going to try to engage in loyalty schemes and engage with customers. Forty-eight hours later, they hiked up their bills by 9.8%. As for the notion this is somehow in the past, we have seen for ourselves, vividly, how that is simply not the case. How are your members really going to change?

Lawrence Slade: As I say, if you look across the scene, across the market, not at one individual company, you are seeing how different companies are doing exactly as you say—how they are engaging and how they are challenging the status quo. That is where I want to look. That is where my concentration is: in making the market work better for all customers.

Q128 **Chair:** The idea is a business model whereby a sizeable proportion of customers are on SVTs, which are, in the main, the most expensive tariffs. These are the current figures: British Gas, proportion of customers on SVT, 74%; EDF Energy, 56%; E.ON, 73%; npower, 59%, ScottishPower, 50%; SSE, 91%. That is still the case. That is not in the past; that is now.

Lawrence Slade: I know. I recognise those numbers. Audrey?

Audrey Gallacher: Those numbers are from March 2016. We anticipate that those numbers will be lower. We are waiting to see the latest ones. Companies have reported individually that they have made some inroads, but those are not going to be the inroads we would want to see under any circumstances. I fully appreciate that.

Lawrence Slade: Also, Chair, if you look at the actions that have been undertaken, some of which Dermot and Rachel have outlined in comments already, I do expect to see those numbers coming down. If a company is not looking at how it is managing its customer base and how it is looking after loyalty, they can expect to be challenged by other entrants into the market. That is the benefit of having 45 to 50 different players in this market. If you are complacent, you will get caught.

Q129 **Michelle Thomson:** Just following on from this thread, I am also not yet even remotely convinced that we are anywhere near where we want to be. I anticipate that figures may come down in terms of those who are on SVT tariffs—but nowhere near quick enough.

How do you feel specifically the trust issue around the industry generally is with consumers? All the hard work—I appreciate that will be the case behind the scenes—that gets done is continually and regularly blown away by minor or more major scandals from a consumer perspective. This is a corrosive, "drip, drip, drip" effect. Some of the evidence we are already hearing today is just not going to help that.

In terms of the trust factor with consumers and measures—this is a question for all of you—any of you take, where is that at present? Where do you anticipate it will end up, given the current model? Frankly, to me, the model does not look like it is working.

Audrey Gallacher: Trust has been a major issue in the past. That has been one of the things that has contributed to the lack of consumer engagement. Often, when we ask people why they are not switching, they are telling us, "Because all companies are the same. Why should I bother?" It is a big challenge for us to address that.

Q130 **Michelle Thomson:** How are you addressing it, then?

Audrey Gallacher: To talk about numbers, BEIS runs a kind of tracker on consumer research. The waves of that tracker—they are on wave 20, which they put out recently—show an increase in trust.

Michelle Thomson: Of what to what?

Audrey Gallacher: It is a funny measure of trust. It is around trust you get an accurate bill and trust you are getting charged the right price. It is up at about 70% just now, but there is a whole range of different measures out there. Which? publishes some figures around customer satisfaction, so we can make sure we get that information to you.

We know we are on an upward trajectory; we know complaint numbers are coming down. But there is still a lot more to do, and the key for engagement is going to be trying to reassure people. That is why Lawrence has already mentioned the energy switch guarantee. That was about us understanding what issues prevent people from getting engaged. What are they worried about? How can we address this? Can we do some myth-busting? Can we raise consumer confidence that this is an easy, simple and safe process? That is really what we are trying to do.

I do appreciate your point that it is not happening fast enough, and I can wholly appreciate the frustration that has been mentioned around people sitting in front of you and then price rises. I can only say that we are committed to doing this, and there is a lot of work already under way.

Lawrence Slade: To add on to Audrey's points, for a long time now we have been trying to increase the level of transparency around the market. That is why every month we publish wholesale market prices. They are actually published today; they are available on our website, so everyone can see gas and electricity prices that are available in the market and where they are going out into the future. I support Ofgem looking at more scrutiny and providing their supplier cost index.

All of that, if it is handled in the right way, can help trust. What I have also been promoting—and you have probably heard me say this in one-to-one conversations with BEIS as well—is that we need to have an open and honest debate in public around the cost and money we are spending every year doing what we need to do—and I must stress that this has to happen—to clean and reinvest in our energy infrastructure.

There is a price associated with that. As I pointed out earlier, it is carried in bills. We need to look at that and we need to make sure people understand why we are doing it—and, ultimately, the benefits it brings if we spend money on making sure your house is working more efficiently and on making sure we are using less carbon to generate our electricity. These are all important debates that are part of the bill that everybody pays. We really need to make sure of this.

You cannot just have trust without understanding the billions and billions of pounds that are being invested into this market every year and how that is recouped from customers' invoices or monthly bills.

Q131 **Michelle Thomson:** Ordinarily, though, if you think of other sectors, it is a standard business practice to meet the required level of capital investment to position a business for the future or make various improvements, whether it is IT or whatever. Many other businesses in many other sectors manage to do that without educating the consumer: "You have to understand that we, uniquely, have to do this". Why would energy be so different that consumers are required to understand that?

Lawrence Slade: For example, I could be running a supply business and have absolutely no generation interests whatsoever. I am only interested in supplying electricity and gas to you. There are a number of costs I have to pass through to you that are completely outside of my control. It is probably something around about 50% of the bill that I can compete on. The rest of those costs are direct pass-through costs I have no control over whatsoever.

If there were an increase in those costs, I have to make a decision as a board, as a company, whether I absorb that cost, because I want to undercut others in the market, or I pass that cost through. That is why I am saying we need a better conversation in public around the structure of a company's bill they are passing to a customer. There is a bit I can compete on, and I can compete openly and hard. We are seeing new entrants in the market do exactly that. They are fleeter of foot; they are challenging and they are pushing the other companies to be more efficient.

But there is a large chunk that I do not have any control over—and that is the bit we need to be clear about with the general public. There is a bit I, as a supplier, can fight on. I can be more efficient: I can buy more effectively; I can run my business more effectively. But there is another big chunk I have no control over.

Q132 **Michelle Thomson:** I have to say, to be honest, I remain unconvinced about that as well. That does not strike me as a spectacularly unusual business model: a business in a supply chain that has variable costs that it cannot control. There are many other sectors where that also applies, and I have never heard any of them say, "We need to make the consumer understand why ours, uniquely, is so complex", to be honest.

I fully accept Anna's point and also the Chair's. To me, this sounds like a broken model if the consumer needs to bear responsibility for continually switching when we have these kinds of percentages remaining on SVTs. So far I am not convinced, to be honest.

Lawrence Slade: It is not all about the consumer. It is about us being more effective in how we are engaging with the consumer and how we are helping to put them in control of their energy consumption. Take smart metering, for example. That is the enabler that will start opening a lot of doors and help people get more control over their energy and make sure they are using energy more efficiently.

The point I am just trying to make is—I do not know about other industries—the Government-policy related issues and regulatory issues we have to pass-through are different, I think, from those in other industries.

Q133 **Anna Turley:** Particularly on that point, I wanted to talk about transparency. I am really glad you raised that, because that is key to a lot of this. Dermot, in your comments you talked about cost being the ultimate driver of prices, but of course we have seen Which? analysis that says when prices drop that is not passed on to consumers. That obviously completely demolishes trust people have in the industry, because they cannot believe you that this is the main driver if they do not see the alternative benefit.

You have mentioned low-carbon policies as being a key driver of prices, but, according to Ofgem, they are only 7% of a dual-fuel bill. We have differing reports talking about the costs of low-carbon generation.

First Utility say costs are going to rise £134 per customer from April, and then Cornwall Energy said that their costs dropped by 14% this month. How are we supposed to understand what the drivers are? How are we supposed to have this trust? What are you as the industry doing to improve that transparency? Would you like more powers or more enforcement to enable you to make companies do this and show their costs?

Dermot Nolan: I suppose I will try to answer this. One of the reasons we published some of the material we published in the last few months was about transparency on a variety of issues. We published material before Christmas on the difference between standard variable tariff and the cheapest tariffs for each of the bigger companies to try to bring some awareness of it. We brought in the supplier cost index, which we have referred to a couple of times now, after Christmas to try to bring in what we hope will be a degree of authority—maybe that is a naive hope—to what is shaping the costs.

As I said, it is not perfect. You get different estimates of costs. What we are trying to do ourselves, using public information, is to look forward a year and say what we think is driving different costs. We are trying to do so, I hope, as a neutral independent regulator, in that sense.

On Government costs, there was a big—and "unhelpful" is the wrong word—debate about this in 2013, as to what was driving price increases. Over the next one to three years, we would like to regularly publish data that suggests our best estimate of what Government-imposed costs will be. I am sure other entities will publish this information, too—and I respect that. But we are going to put significant resources into trying to give a good average estimate.

I will say—I hope I am not overcomplicating things—that in itself is going to get quite messy and difficult to do. I do want to make one point to the Committee, because it is quite an important point. Traditionally, Government costs imposed, sometimes for decarbonisation, have been an extra add to the bill, as it were. Specifically, there was money paid to, say, renewable generators. The nature of the way we give money to renewable generators is now going to change in the next two, three or four years—and certainly over the next 10 years. We are using what we call contracts for differences. I know it is some years away, but, for instance, the Hinkley Point power plant is paid for via contract for difference at a particular price. That will relate to the wholesale price.

Essentially, it will specify a price of X. I am sorry: "X" is never a good thing to use in a Select Committee. It will specify a particular price and it will then say, "If the wholesale price is much less than that, the particular generator is paid significant amounts of money to top up the difference. If the wholesale price is in fact exactly the same as the price that is guaranteed, then the generator gets paid nothing". That will make that more difficult and more complex.

In 10 years' time, if average wholesale prices, which will still mainly be influenced by gas, coal, et cetera, are high, then other forms of generation will look cheap and will look as if they are not getting any subsidy. If in 10 years' time, wholesale prices are low, then it will look as if it is very expensive. It will be difficult to try to get the public, insomuch as they are interested, to a clear understanding of what is driving these costs. But it is important to try to do so and to try to explain it as candidly as possible.

If I can take up one or two of the other points, if I might, I said we are trying to bring transparency to the market. I finished with the point about switching you have both made. We are trying to bring transparency to the market. Doing something, as Energy UK are promising to do, on customer switching and guarantees about that, giving customers more confidence to engage in the market, is key. In terms of trust complaints, that is clearly an issue. In the last five to six years, a number of the bigger companies across the sector, frankly, had very difficult IT transitions. Some—not all—made a mess of their IT systems and their billings systems. As a result, they incurred significant costs. They were fined by the regulator significant amounts, but that led to a real spike in complaints, which damaged public trust again.

There are some signs—I do not want to overstate this—of that changing. In 2015, there were just over 5 million complaints to energy suppliers. That has fallen by 12.5% in 2016. That is only one year's data, but I would very much want that trend to continue. That would give us the sense that companies are getting fewer complaints and responding to them much better. We have the ombudsman services as well in that regard.

As a regulator, I would say we have put a very clear, we hope, signal to companies that they have to uphold a general licence condition—most of the supply companies have licences—that we call a standard of conduct: they must treat customers fairly. Given that we are trying to make competition easier, given that we are trying to make engagement easier, the other strand of that must be that if an energy company, in what is admittedly an essential service, treats customers badly, does not bill them properly and just treats them inadequately, we will be there to fine them, if necessary.

I have a final comment about trust, costs and switching. Should people have to switch? That probably goes beyond my policy mandate, in the sense that we were set up by and large predominantly to further the interests of customers via competition. That was, in some sense, the framework set up for energy for telecoms, et cetera. I get the switching thing. I get the question, "Why should I have to switch?" One of the best responses to that is that companies would start doing things more for customers who do not switch.

To change the entire switching framework is a policy decision. I am not saying it is the wrong one, but in that sense it is a policy decision. People switch all the time in respect of, say, supermarkets, if you do not like something. It is a little more different, because you do not engage naturally with telecom and insurance, but by and large switching, or at least the threat of switching, is one of the things that drive the energy market. Changing that would be a fairly significant policy change and really a matter for Government.

Rachel Fletcher: If I could just add to that, the vision we have of a well-functioning market is one where people who choose not to switch are still protected by market pressures. We will not be satisfied until we get there.

Q134 **Anna Turley:** That is the really important point. I take your point about the supermarket comparison, but I know, pretty much, when I go to the supermarket, what the cost of a pint of milk is. I do not want to go tomorrow and find out there is an extra 40p and then the following day it is back again. I cannot trust a supermarket that does that. I know what I am going to buy.

Whereas with the energy market, you feel totally blind, as a consumer, as to what is happening, what the pressures are or what your bill is going to be from one month to the next. I find the phrase "engaging with the energy market" strange. I do not engage with my supermarket. I go and have a transaction. It is really important that the industry looks at it from the consumer perspective.

There are those of us who just want to get home, turn the lights on and put the heating on. That is the way most people function. We are not going to have a functioning market if you are relying on people to be looking at their bills every week, looking around the market and spending time online choosing the best deal. It is just not going to happen.

Dermot Nolan: I appreciate that, but I have two comments. We have not talked about a lot of the technical change that will happen in the sector. As Rachel said, if we have a vision—and we do have a vision, I hope—for a few years' time, it would be that, literally, there will be an app on your phone. Maybe you would not want to, but you could be walking down the street, hit the app and just say, "Right, find the cheapest deal".

Another thing even in the last year or two years is that we have seen services—I will not name specific ones, and there are issues with this as well—that are offering, for a relatively small yearly fee, a switching service. They are saying, "We will do it for your energy bill and your telecoms bill, et cetera. We will guarantee that we will keep you on one of the cheapest deals. We will take the hassle out of it". That is not an unreasonable model.

I am sure there will be issues at some point about whether those companies are behaving reasonably—and there will need to be some protections put in place—but there are models developing that say, "If you pay us a small amount of money, we will guarantee, over time, to try to ensure you are on the cheapest deal". They take away that issue of when you come home and you think, "The last thing I want to do is search on a website to switch".

Anna Turley: For me, it is fine. I can use an app and so on. But I knock on a door and there is an old lady who is in her coat. I think she is leaving the house, but she is not. She has got her coat on because she cannot afford her fuel bills. She is not online. These are the people we have to protect, and I look to the industry not to take them for granted.

Q135 **Chris White:** The impression I get from the panel is that this is a unique sector operating under unique circumstances, and the relationships between them and their customers are also unique. Five million complaints is a shocking number, is it not? Do you, as Ofgem, take any responsibility for letting that spike happen?

Dermot Nolan: I suppose in some sense we do. We feel it should not have happened. It did happen on our watch, so I regret that. We have taken significant action against the companies. In the last few years, we have fined companies about £210 million for basically poor customer service. I am glad, as I said, that it has gone down from 5 million to nearly 3.5 million.

Yes, it should not have happened. We have put considerable resources into making sure it will not happen again, and we will enforce strongly against companies that do treat their customers poorly.

Q136 **Chris White:** You fined them £200 million. Is that what you said?

Dermot Nolan: About £216 million, I think.

Q137 **Chris White:** Presumably, they will just recoup that penalty through their customers.

Dermot Nolan: I do not believe they will. First, some companies have not been fined; others have. Some have been fined significantly. To be quite candid, the damage from the fine is probably less than the overall negative effect on the company, because there is considerable negative publicity attending that. One of the companies we fined most significantly was a company we have discussed already today. They lost customers last year.

Q138 **Chris White:** For the record, can you say which one that was?

Dermot Nolan: That was npower.

Albert Owen: They are recouping through their customers.

Dermot Nolan: They are raising their prices, but as I said, the key point is that I would hope that is not necessarily a profitable strategy for them.

In a better functioning market, it certainly would not be—and I am also hopeful it will not be in this market.

Given the fining powers, though, we need to use them actively. It is a power we have, and it is still an effective deterrent. We have seen significant reductions in complaints. Obviously, it is a major target for us to make sure that continues.

Q139 **Chris White:** If you had to do a bar chart on complaints, not the companies that caused the complaints, what would be the top two or three issues?

Rachel Fletcher: It would be billing. The accuracy of bills is always top of the complaints. This is partly to do with the fact we do not yet have smart meters. One of the things smart meters will do is remove a really big bugbear for consumers, which is that they get a bill in the quarter and it may not bear any resemblance to the actual amount of energy they have used.

Q140 **Chair:** I am going to bring Albert in on an important point about powers of Ofgem, but can I indulge in two questions to you, Dermot?

You mentioned transparency, and some of the information you provide is fantastic in terms of really being transparent and exposing how some companies are trying to do their best and some are not. I have some things in front of me now in terms of the difference between the SVT and the average of the cheapest tariffs from the 10 cheapest suppliers. The numbers there, the money that could be saved, is striking.

The difference for British Gas is £166; for Co-operative Energy, it is £244; EDF Energy is £192; Extra Energy is £252; First Utility is £193; Scottish Power is £203. This is great, transparent information that can really aid the customer, but I do not think anybody knows about it.

It is really a case of two questions to you in regard to this. Are you seeing customers, through this information, changing their behaviour, that is, switching and what have you? Given that this is great information but my perception is that no one knows about it, how are you going to communicate and promote this further?

Dermot Nolan: We published that particular piece of data for the first time in December. We are committed to publishing it roughly every three months. We will be publishing something again at the end of March. It got a fair amount of attention at the time, but perhaps not enough. We will try to give it attention every time we publish it. We have committed to doing it regularly every three months.

In terms of whether it has had an impact, it would be naive to say it has had a significant impact by itself over time. Rachel and I have talked about the urge to get customers engaged, subject to what was discussed earlier. That will take time. There are various other measures and remedies coming out of the CMA that we think will assist. In that sense, it has not yet had a significant effect. I would not claim that. But bringing it out constantly and giving it some attention will help.

Though it is only one fact, I would also note that switching has risen in the last year. It rose significantly during late 2015 and 2016 to about 16%. Switching is only one aspect of competition in the market. We have seen some increased switching compared with two or three years ago.

Q141 **Chair:** That brings me on to my second question. You say that switching is only one part of increasing competition, but it seems to the Committee to be the be-all and end-all. People who are not switching, who possibly are not engaging and do not want to be engaged, for the quite reasonable reasons that Anna suggested, are frankly being fleeced.

It is a case of how we keep it fair for every customer, not just the IT-savvy customer who may switch on a regular basis. What do we need to be doing to ensure that, if you are on an SVT and you are paying the expensive tariff, you are automatically switched to a cheaper one? How do we get it fair for everybody?

Dermot Nolan: I have two points. First, I will say that there are specific measures—I could come back in writing on this, but perhaps I will speak a little bit about them now—to protect those who are vulnerable, which is always an important thing and it is very much part of a regulator's duty, very sensibly, in my view.

On the first point, I cannot promise a magic bullet. I can say this was the CMA's core finding. The market is not working well for people on SVTs. It is just not. Its response was to say, "Make it easier to engage". By doing so, as Rachel referred to earlier, we want to get a situation where people who still do not engage are protected, but over time we have more competition in the market and force the dispersion levels down.

Certainly, the scenario one would hope for in 2021 is that by that particular point in time you would still have markets where, probably, there were increased levels of switching, but also markets where the levels of dispersion between those on what we call standard variable tariffs now and those on other types of deals were much lower.

Being candid, I talked—I do not think he would have any problem in me saying this—to the head of the CMA panel. They did a large study that suggested people would only switch for £200. I would like to see, in 2010, significant evidence of less dispersion of prices and people, if they were asked that question again, saying, "If I was going to switch, it is so easy to do it that I will switch for £20".

Chair: You are tasked with producing a fair market, and we are very keen to find out whether you have sufficient powers to be able to do that. That is a key part of what the Committee wants to look at. Albert, could you talk about that?

Q142 **Albert Owen:** Before I do that, I do accept there is greater transparency now. I have been on Energy and Climate Change Committee since 2010. The thought, Lawrence, that this is voluntary from the companies is absurd, because they have been dragged screaming and kicking.

Lawrence Slade: No one told us to do it, Mr Owen. We did do it ourselves. No one told us to.

Q143 **Albert Owen:** No, with the greatest respect, it has been consumer pressure; it has been the regulator.

Lawrence Slade: I do not disagree with that.

Q144 **Albert Owen:** It has been Select Committees like this. The companies were in denial that there was an issue. All of a sudden, now they are saying, "It was our idea after all". I would like you to comment on that.

Lawrence Slade: As I say, we certainly have pushed, as Energy UK, to put more data into the market. We did it because—and I agree with you—we felt it was needed, after hearing what customers were saying. That is why we started publishing the switching numbers.

Q145 **Albert Owen:** You have been exposed.

Lawrence Slade: I would not call it being exposed, no. We took a decision, as a trade association, that we had a responsibility to put more information into the market.

Albert Owen: That is good.

Lawrence Slade: That sits next to Ofgem and their responsibility. I take that fair and square.

Q146 **Albert Owen:** You said you wanted an honest debate. I have heard this before—it is déjà vu—from the big six, in particular: "We want an honest debate". I regret not asking npower whether they were going to put their prices up when they were sitting there with EDF, so I am not going to lose this opportunity. Do you envisage prices going up over the next 12 months?

Lawrence Slade: Please bear in mind that I have no knowledge whatsoever of any company's pricing decisions.

Q147 **Albert Owen:** Yes, but you said you wanted an honest debate. You are a trade body.

Lawrence Slade: The honest answer, Mr Owen, is, as I said at the start of this session, we have seen increasing price pressures on the bill, but it is up to each individual company as to how they deal with that. That is an honest answer.

Q148 **Albert Owen:** That is your honest answer, but the consumer is sitting there now, thinking that we are going to have honesty in this and that there are going to be the external costs you have mentioned. How is that going to filter through, in your honest opinion, to the consumer?

Lawrence Slade: The only way of answering that accurately is to get the chief executives of the 50 energy companies in here and say—

Q149 **Albert Owen:** Do you not represent them?

Lawrence Slade: I represent them, but I cannot talk about pricing issues, because I do not know how they are going to handle their own pricing issues.

Q150 **Chair:** Before you go on, Albert, following up on that, based upon what we have heard today from Dermot and you—that successful companies have been able to hedge, innovate and control costs—do you anticipate that successful companies will not have to put up energy bills for customers?

Lawrence Slade: You are describing a market that is not homogenous. You are describing a situation we have, where we have had some increases. One company has decreased their gas tariff. Other companies have frozen or extended their tariffs. We have other examples over the last week of companies that are investing millions of pounds in new services for their most loyal customers.

What you are seeing is a market that is responding in a competitive way, where you have boards saying, "Okay, what is our risk? What can we take? How can we ensure we are looking after our customers? What programmes are we looking at bringing in there?" You have new disruptors coming into the market that are challenging the established companies and challenging the status quo.

To me, that all points to a market that has not done enough in the past but is moving forward and is investing in new technology like smart meters to make things better for customers and, as I have said on the record before, to make this a market that works for everyone.

Q151 **Albert Owen:** We have had a number of reports, and the CMA review was the latest, if you like. Part of its remedies was a transitional price control for the most vulnerable customers, predominately—the 4 million households on prepaid meters. I have a question here to Ofgem. Given that you have very quickly implemented a price cap for this transitional period, why did you not do this yourselves? Why did you have to wait for the CMA review? You knew these kinds of customers were being ripped off—I will use that term. Now, the CMA has had this very in-depth review, and you are going to put a cap on that. Why did you not do it before?

Dermot Nolan: I do not know if I can give you a very good answer. In some ways, I regret doing that. There was some evidence we had in the past that households on pre-payment meters were not being allowed to engage in the market. In many ways, I regret doing that.

We sent the entire market to the CMA for study. We very much endorse this PPM issue. As the study went forward, it became clearer to us that they had weaker options in the market than anybody else. In some ways, the differences between PPMs and other forms of technology became greater. We obviously implemented it. It is a very good idea. I suppose I do regret not having acted sooner.

Q152 **Albert Owen:** That is a good honest answer, but what you are saying is that you did have the powers to do it; it is just that you did not act.

Dermot Nolan: We have the powers to do it. I should be clear about this. We have powers to put in place licence conditions, which are then, perhaps ironically or otherwise, substantively appealable to the CMA. Once we had referred the entire market to the CMA, if we then initiated a move to put a backstop tariff in, that would, in my view, have resulted in a substantive appeal to the CMA, which would have, in itself, taken a very significant period of time. That is the statutory framework.

It could then have been appealed further on, but perhaps not. The CMA has different kinds of powers that allow it to make—without sounding like a lawyer, which I am not—what is called an order, which is only appealable to the court.

Q153 **Albert Owen:** But, on that, again Iain used the term that people on certain tariffs were being "fleeced". Do you have the powers now to put a cap on the standard variable tariff? It might be subject to an appeal, but do you have to obtain a licence? Can you explain that to the Committee? Do you have the powers? Will there be circumstances where that cap could be introduced?

Dermot Nolan: In theory, we have the powers. As I said, there are licence conditions. In theory, we have the powers to amend any sort of licence condition we see fit.

Given the statutory framework we have operated in, we have never sought to put a price cap or a backstop tariff in, partially because we assumed—correctly, in my view—two issues. One is that it would almost certainly be appealed to the CMA and, secondly, it would constitute a major policy change to the framework that is set up.

Tracing that back, the CMA obviously thought long and hard about whether or not to put in a backstop tariff for SVTs. The interim conclusion suggested that they should. They thought long and hard, and I do know personally they all spent a lot of time thinking about it. In the end, they decided not to. Four of them decided that it was not proportionate at this point in time but that there should be remedies to encourage people to get off SVTs and to ultimately talk about getting to the market we have just suggested.

But there was a minority report saying the level of harm is sufficient now as to suggest a backstop tariff for SVTs would be useful. They split, and they are perfectly reasonable, honest decisions on both parts. Given we had referred the market to the CMA and said we would accept its conclusions, we are now trying to get on with the remedies.

Q154 **Albert Owen:** I just want to push you on this. I want to link the hike we have just seen from npower with claims that smart metering is one of the issues that caused them to put up their price. Smart metering is the issue for which the CMA said they would have a transitional period of four years. This is your personal opinion here. There are many people and families who are just about managing on their tariffs now. As their champion, are you suggesting that there is a cap or the ability for you to make companies put them on to the cheapest tariff? I am linking the two there deliberately.

Dermot Nolan: Genuinely, that kind of decision strikes me as a decision that has pros and cons. The CMA agonised about it, but that decision is really a policy decision.

Q155 **Albert Owen:** It is, but if there is evidence coming through now of rises at this stage and they are blatantly saying it is due to this external pressure of smart metering, is there a different case to be put to the CMA?

Dermot Nolan: I am not trying to use this as an excuse, Mr Owen, but legally I do not think we can go back to the CMA and refer again. They did their analysis. As I said, they came to a finely balanced decision.

Q156 **Albert Owen:** But we might be able to. You are here to give evidence, with respect. The Government have been left off the hook here today; they should be in front of us, as well, because the Prime Minister has said she is going to deal with energy companies. This is one way of dealing with them.

Really, what I am asking you is, do you have enough powers? Do the Government help you and back you? One of the remedies as well—I am not digressing here—from the CMA was for recalibrating the relationship between the Department and you as the regulator and for you to become more independent and have greater co-ordination. If circumstances change, do you need more powers or does there need to be a reference back to the CMA?

Dermot Nolan: If Government and Parliament wish to give powers to put in place a backstop tariff, that is something Government and Parliament should do. If they did, we as the regulator would implement it to the very best of our ability.

Q157 **Albert Owen:** Good. The other thing in the CMA report that was very important—you have touched on it, to your credit—was loyalty bonuses. In the past, you have said, "We cannot do it. We are restricted from doing it". Now, the CMA suggests that you can do it. I am sure you will watch this very closely. How will that work? Will people who are threatening to leave be told, "You can have a sweetener and stay with us for a period of time"? Will it be—you mentioned supermarkets—that people have vouchers and are able to reduce their bills significantly by staying with the same company?

Dermot Nolan: There was an announcement from one firm this morning—

Albert Owen: I have been busy this morning. Tell us.

Dermot Nolan: That was just one example. It was Sky, and it related to getting a broadband thing or something like that. There were different kinds of things that were presumably of value to customers. That often makes things difficult to compare. There will be a challenge in that sense, if loyalty bonuses are given in non-cash ways, for people to value them—even though it is likely they will be there.

It would be difficult for me to say exactly what kinds of loyalty bonuses might arise. Some companies might not offer them. I would prefer it if it were something that was tangible that a customer could value in some fashion.

Q158 **Albert Owen:** Do you have any ideas from your perspective?

Audrey Gallacher: There are quite a lot of initiatives going on. The one that was mentioned today was around a package.

Albert Owen: A package of what, sorry?

Audrey Gallacher: Sky TV—

Albert Owen: Well, let us stick to energy.

Audrey Gallacher: There are also initiatives to make better contact with customers to make sure they are on the best deal for them. There is a whole range of different tariff options. Another one of the things from today was discounts, which is basically free energy days. We are going to see more and more of that coming. We have already looked at some of the indicators that are showing the market is—

Q159 **Albert Owen:** I am going to press you on this. As a trade body, should you be recommending to your members that this is a way that will increase further trust with the consumer?

Audrey Gallacher: We are continually making recommendations to our members.

Albert Owen: You are.

Audrey Gallacher: Yes. We are continually recommending that they take actions to improve their service to ensure they are treating their customers fairly and come out with things the customers actually want.

Q160 **Albert Owen:** Is a loyalty bonus a good idea?

Lawrence Slade: Time will tell. As I said to Ms Turley, it is the case that different things will work with different customers. What is important is that the industry puts the effort into understanding what each customer needs and how they respond to that.

Q161 **Albert Owen:** I do not think it is. The example Anna gave was a very good one. She was talking about ordinary people who are suffering because their energy prices are going up. What we are saying is that they have no trust—Michelle raised this point as well—in the companies. What I am asking you quite directly—this is your opportunity—is: will a loyalty bonus help those people in those circumstances?

Lawrence Slade: In the circumstances you paint there, Mr Owen, what we need to do is make sure we are getting assistance to those people as effectively as possible.

Q162 **Albert Owen:** Calling them sticky customers is not good enough, is it?

Lawrence Slade: I do not call them sticky customers.

Albert Owen: No, but that is the general—

Lawrence Slade: There are various services that provide help and make assistance available to customers in vulnerable circumstances. There is the Digital Economy Bill going through Parliament at the moment. One of the things that will come out of that is better data-matching powers. One of the benefits of that is that we can get services to people faster and more effectively.

Q163 **Albert Owen:** Again, that is the responsibility of society, Government or the regulator to impose.

Lawrence Slade: It is the responsibility of all of us to deliver that.

Q164 **Albert Owen:** Exactly, yes. I am asking you a question. Should the companies you represent be more proactive in doing loyalty bonuses? It is a very simple question.

Lawrence Slade: They should be proactive in doing both: be proactive for people who that works for, and be proactive in making sure we are using everything in our ammunition pack, if you like, to make sure we can get measures to those people who need them. We have to do it in the most effective way.

Q165 **Albert Owen:** I have one final question for Ofgem. One of the CMA review remedies was also—I think they were critical of you here—that you had restricted the companies to the four tariffs. Was that an error? Will loosening that help?

Dermot Nolan: When it was put in place, which I think was back in 2013, it was always envisaged as—

Albert Owen: It was a reaction to the situation then.

Dermot Nolan: It was a short to medium-run measure in any case. The CMA said they thought it had probably done more harm than good, so we did remove it. Dealing with it going forward, the key point is that we are putting in place a principle, which is enforceable as a licence condition, on companies not to confuse their customers.

There will be more tariffs. There is a balance to be struck. More tariffs is good; more choice for consumers is good. But we also want to try to ensure that consumers are not consciously confused by their companies. That is quite an important thing we need to enforce.

Q166 **Chair:** I have two final questions: one to Lawrence, one to Dermot. Lawrence, does Energy UK and your members think Ofgem is too strong as a regulator?

Lawrence Slade: There is a very simple answer to that: we support having a very strong regulator. It is an integral part—

Chair: Do we have that?

Lawrence Slade: Yes, we have.

Q167 **Chair:** Okay, thank you. Dermot, forgive my ignorance, but I want to clarify this in my own head. Were you saying earlier that Ofgem has the power, through the licensing regime, to cap SVTs?

Dermot Nolan: Yes, it would have the power to introduce such a condition.

Chair: But you choose not to.

Dermot Nolan: We have never done so. We thought that would be changing the policy framework we were set up in.

Q168 **Chair:** But, that being the case, you say on your website, "Our principal objective when carrying out our functions is to protect the interests of existing and future electricity and gas consumers". We have been talking about every customer, not just those who switch. If you have the power to cap SVTs and you choose not to, you are failing as a regulator for customers, are you not?

Dermot Nolan: I am not sure we are, Chair. This may sound like we passed the issue to the CMA, and to some extent we did, but that was one of the strongest powers we had—to ask the CMA to look at whether there was a major issue in the industry that required substantive structural change.

At the time, there were issues about whether or not the companies might be broken up either vertically or horizontally and, ultimately, a choice on whether or not to put in a price control on SVTs. On balance, the CMA said not to. It was a finely balanced decision, but on balance they said not to.

At the start, we said to the CMA—as I think I said in front of the Energy and Climate Change Committee at various points—we would accept whatever the CMA came out and recommended. We know it was a finely balanced choice, but there are pros and cons to all forms of price caps. I can understand the idea that it would protect those who do not switch. It can have other effects in terms of price controls. We did not choose to second-guess the CMA report.

We were also conscious of the idea that, if there is a desire for a policy shift in this, it would be a fundamental change to a regulator that has been set up to achieve these kinds of aims through competition. That is very much a matter for Government, though it is potentially a very understandable decision. If Government do choose to go down that road, we will support that in every possible way and implement such a cap, if it comes in.

Chair: Thank you very much. It has been very helpful. I have no doubt we will be seeing you again very soon—but thank you for your time.