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By email to: CDconsultations@ofgem.gov.uk

Non-confidential version – redactions marked

Dear Meghna

Draft Consumer Vulnerability Strategy 2025

This is the Centrica response to Ofgem's Draft Consumer Vulnerability Strategy (CVS) 2025 consultation and it may be published on Ofgem's website.

We welcome the opportunity to respond to this consultation and to help shape Ofgem's CVS. As Ofgem will be aware, we have a very long and proud tradition of providing additional help and support to vulnerable customers. We are regularly cited and recognised by leading consumer groups and charities as consistently demonstrating industry best practice for the work that we undertake to help vulnerable customers. Over many years, we have invested a significant amount of resource into helping those consumers who are most in need, not only financial help, but also in terms of staff training, charity and Non-Government Organisation (NGO) partnerships and local community investment programmes. A lot of the additional support we offer is discretionary and becomes increasingly less tenable to sustain until the issue of funding has been fully addressed by Ofgem.

The CVS consultation makes passing reference to the Default Tariff Price Cap (DTC), the Competition and Markets Authority's (CMA) Prepayment Charge Restriction (PCR) and the possibility of enduring price protection for vulnerable customers. However, it does not explicitly consider how (potentially substantial) additional costs that may result from Ofgem's proposals will be funded in the context of the DTC or any successor price cap (or, indeed, in the absence of any further cap). This is a serious omission which must be rectified before the CVS is finalised.

Executive summary

- We broadly agree with the five priority themes that Ofgem has set out in its draft consultation paper. However, we will need to see concrete detail behind each theme. Where there are specific proposals, there will need to be an accompanying Impact Assessment for each, before we can respond more fully. Where Ofgem has been vague or ambiguous around "better" outcomes, Ofgem must be clearer in its next consultation as to what exactly is being asked of suppliers, which in turn will inform the costs and operational impacts of what Ofgem is proposing.

- We understand Ofgem's rationale for not reopening its definition of vulnerability. However, society is changing and concepts of vulnerability and vulnerable customers are themselves fluid. Groups previously flagged as 'vulnerable' may not always be the case. For example, the need for any specific priority action or treatment to protect a healthy, well-off, digitally-savvy 70-year-old is far less clear today than when the regulations were originally drafted. We recommend there should be a full review by Ofgem as to whether it should remove the more prescriptive definitions within the licence conditions, as these are already covered within the existing overarching vulnerability principle.

- Ofgem should consider whether loading new obligations on to suppliers which carry a disproportionate volume of certain categories of vulnerable consumers, risks creating a bifurcated market. This could lead to an overall reduction in the intensity of competition, with a number of suppliers unable to compete effectively. We are pleased that BEIS and Ofgem have recently recognised that there is an imbalance in higher cost to serve customers in their consultation on Flexible and Responsive Retail Markets[1]. Ofgem should not exacerbate this issue as part of its CVS.

- We broadly agree with Ofgem's proposals for its first-year priorities. However, Ofgem must produce clear guidelines on the specific definitions that it intends to apply to the concepts of 'self-disconnection' and 'self-rationing', not least to ensure that a consistent approach to this issue is taken by all suppliers.

- We agree there is a need for Government to take the lead on affordability, with Ofgem and other regulators playing a supporting role. However, improvements will only be truly and fully delivered for vulnerable consumers if all the parties which participate in the energy sector commit to making changes.

- We also believe that all support must be paid for and delivered in a way that is proportionate across all suppliers. This will ensure that there are no disproportionate burdens on suppliers or that there is an uneven distribution of benefits to consumers. This is not the case, for example, with the Warm Home Discount (WHD) scheme.

- It would be more efficient, and effective, if Ofgem and the ICO worked together to produce a consistent, coherent and joined up plan in relation to the use of 'smart data' (with each body setting out clear guidance for suppliers to follow, with accompanying privacy and regulatory impact assessments). This should be undertaken in conjunction with BEIS, to ensure that there is a consistency of approach across different sectors. Ofgem must also be clear what it means by 'smart data'.

- The recent Independent Commission of Customers in Vulnerable Circumstances [2] (CCVC) Final Report, highlighted a number of specific recommendations for Ofgem to consider and implement. Ofgem's next iteration of its draft CVS paper should explicitly reference each of these recommendations, outlining how Ofgem will or has addressed or implemented each recommendation.

- We have long called for Ofgem to work with the Department for Work and Pensions (DWP) to review the process (and obligations on suppliers) in relation to Third Party Deductions (Fuel Direct). This call has also been taken up, on more than one occasion, by Citizens Advice; most recently in its report on people who fall behind on their bills entitled, 'Supply and Demand'[3]. It is time for Ofgem to act.

- We note that Ofgem has not seen any compelling evidence to expand the scope of the vulnerability definition to include microbusinesses nor has it received any comments following its open letter on this matter. Therefore, we agree with the decision not to expand the definition into this market.

- Before any new obligations for vulnerable customers are expanded or re-defined by Ofgem, the issue of funding must be properly addressed. Additionally, against a backdrop of vigorous competition and direct regulatory intervention to cap prices, suppliers are having to review all discretionary / non - mandatory activities and financial spend in an attempt to replicate the low-cost base Ofgem has modelled to set cap allowances. Discretionary activity that supports vulnerable customers is not immune from this pressure, which will be exacerbated by overlaying additional mandatory cost obligations unless cap allowances are revised upwards to accommodate.

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[1] BEIS & Ofgem consultation on flexible and responsive markets :https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/819624/flexible-responsive-energy-retail-markets-consultation.pdf

[2] Independent Commission of Customers in Vulnerable Circumstances Report: https://www.energy-uk.org.uk/publication.html?task=file.download&id=7140

[3] Citizens Advice Supply and Demand report: https://www.citizensadvice.org.uk/Global/CitizensAdvice/Energy/Supply%20and%20final%20demand.pdf

The Default Tariff Price Cap – implications for supporting vulnerable customers in the future

We have demonstrated that, beyond Q1 2019, ✂, the price cap is set at least £39 below the costs of an efficient supplier which has, like British Gas, a cost base that contains above the proportions of customers that are higher cost-to-serve that are assumed in the benchmark (see attached Annex 1 Centrica Default Tariff Cap summary table 121018 for further details). This shortfall places an intense and unreasonable pressure to reduce costs. Such pressures are not in the interests of customers, particularly vulnerable customers.

As we have said to Ofgem previously, of the £39 shortfall in the cap, the uncertainty component of headroom is already at least £18 per customer too low to meet the requirements of the Tariff Cap Act, before taking into account other material unforeseen costs such as the £58.6m industry Renewable Obligations (RO) mutualisation costs[4]. In its DTC Decision, Ofgem suggested that the headroom allowance should be sufficient to cover the costs of regulatory changes that were not envisaged at the time the price cap was set; this is incorrect.

In the draft CVS, Ofgem has mooted a series of potential additional measures to protect vulnerable customers, most if not all of which will increase costs. If Ofgem wishes any of these additional protections to be implemented, it must carefully define their costs, explain how they will be recovered under the price cap and make explicit provision in the price cap if necessary. In addition, Ofgem must fully consult and equip itself (and industry) as to any implications that the proposed changes may have before adopting them.

The full details of the DTC implications of Ofgem's CVS are set out in Annex 2 of our response. However, the implications of the DTC for Ofgem's proposed vulnerability initiatives are stark. Either Ofgem needs to increase the cap to facilitate specific funding of each and every of the measures suggested to the extent that they entail extra costs, or it must specify and facilitate equivalent spending or savings elsewhere that are already built into the cap.

Detailed analysis, with a full supporting evidence base, is required in any event to address the Regulatory Policy Committee (RPC's) reservations about the adequacy of the Impact Assessment underpinning the DTC. The RPC made clear that it required further detail on assumptions and calculations for the period 2021-2023 in the event that the DTC is extended beyond 2020.[5]

In conclusion:

- Calls for suppliers to 'do more' to support vulnerable customers within the current regulatory framework are not provided for within the current caps. Similarly, there is no provision for additional regulatory obligations in support of Ofgem's CVS within current caps.

- Any proposed new obligations must be justified on their own merits through rigorous impact assessment that explicitly considers funding, having regard to Ofgem's statutory duties to ensure that suppliers (and new market entrants) can finance their regulatory obligations.

- In the short term while the DTC is in force, this will require Ofgem to weigh customer benefits it expects to result from new initiatives with the additional costs that will ultimately fall to customers to bear through higher cap allowances. However, the need for rigorous cost-benefit analysis does not stop when the (temporary) DTC comes to an end, especially where Ofgem is considering the possibility of enduring price protection beyond the life of the DTC.

- In an effectively competitive market not subject to a general DTC, higher costs of serving vulnerable customers would need to be recoverable from those customers as cross-subsidy via 'socialisation' will not be commercially sustainable.

[4] See https://www.ofgem.gov.uk/system/files/docs/2019/02/centrica_cm_response.pdf, https://www.ofgem.gov.uk/system/files/docs/2018/10/centrica_-_response_2_-_appendices_2-10.pdf and Annex 1 Centrica Default Tariff Cap summary table 121018

[5] https://www.ofgem.gov.uk/system/files/docs/2019/07/rpc-43581-beis-ofgem_domestic_gas_and_elctricity_default_tariff_cap_-_iaf_-_opinion.pdf

- Without an explicit external funding stream, maintaining artificially low pricing for high cost to serve vulnerable customers where suppliers cannot recover their costs would result in a clear disincentive to serve such (loss-making) customers. This would not serve the long-term interests of vulnerable customers.

We have also included a separate paper from Frontier Economics at Annex 3, which outlines the framework Ofgem will be required to follow in terms of undertaking the Impact Assessments for any proposed actions to support its CVS.

Coherent and consistent regulation

From a Government and public policy perspective, as the energy market transitions through significant and complex changes, and to avoid unintended consequences, all of the proposed policy interventions should comply with the following recommended principles:

- Consistent with competition and retaining customer agency - any policies to support vulnerable customers should continue to encourage customers to engage as much as they can.

- Aligned with continuing decarbonisation - the vulnerability strategy needs to reflect the need to decarbonise over the next few years and how vulnerable customers will be supported through this.

- Simplified and cost effective - dealing with consumer vulnerability is key. However, there are a plethora of vulnerability and consumer reviews and consultations sitting across a number of Regulators and Government Departments. At face value, these appear to be similar in nature to or overlapping with Ofgem's CVS. As energy suppliers, we need clarity on roles and responsibilities between Regulators and Government Departments, i.e. making clear which body leads on each policy area and how these interact with each other.

- Data enabled - BEIS is currently undertaking the smart data consultation. Consumer vulnerability forms a key consideration in this. We agree that vulnerable customers stand to gain from increased data sharing and data portability, but careful thought needs to be given to ensure frameworks are future proofed and cost-effective. Ofgem must also be clear when referring to 'smart data' – as to whether it means data sharing or data portability. The two are very different matters. Ofgem should also be clear if it is specifically referring to data from smart meters, 'smart meter data' or data and information from other sources.

Social Policy considerations for the CVS

We have been highly commended for our work on proactively identifying those customers who are at risk of self-disconnection and for offering support to those customers who have self-disconnected. We were the first energy supplier in the UK to attain the BSI Accreditation for Inclusive Services. We currently have a large number of charity, health and financial referral partnerships, including with CLIC Sargent, Carers UK, StepChange, the Alzheimer's Society, Macmillan Cancer Support, The Stroke Association and Christians Against Poverty – to name just a few. We also utilise Sign Video within our Operational Units and have rolled out a highly successful Dementia Friends Awareness Programme across our UK office, covering thousands of our employees.

To improve the experience of all energy consumers (not just those who are in vulnerable circumstances), it will require all of the parties which participate in the energy sector to take action. This includes not only energy suppliers, but also Government, Consumer Groups and the Regulators too.

It is therefore disappointing to note that the Ofgem CVS paper made so little explicit reference to the recent Independent Commission of Customers in Vulnerable Circumstances Report– which set out a number of important actions for Ofgem itself to consider and implement.

Equally, neither does Ofgem's CVS paper fully address the proposals made by Citizens Advice in its Supply and Demand report. Specifically, Citizens Advice called on Ofgem to commit to working with the DWP to review the guidance and application process for Third Party Deductions (Fuel Direct). We have long called for Ofgem to start this dialogue, as the current obligations within the Supply Licence Conditions (SLCs) do not work for either the consumer or the supplier – and more concerningly, conflict with the rules laid down by the DWP.

Ofgem's key themes and first-year priorities

We are broadly in agreement with Ofgem's key five themes and the first-year priorities as set out in the draft CVS paper. However, these themes are currently (as proposed) very high level and we will need to see concrete detail with impact assessments before responding more fully. And, as noted above, more clarity will be required around what Ofgem considers to be 'self-disconnection' and 'self-rationing'.

For ease of reference, we have set out below our comments on each of the outcomes for the five themes in Annex 4 and have provided answers to the four specific consultation questions in Annex 5.

We hope that you find this response useful. Please do not hesitate to contact me if you would like to discuss any aspect of this response further.

Yours sincerely

N. Howard.

Nigel Howard
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Centrica, Legal and Regulatory

Annex 1 – Centrica default tariff cap summary table 121018

Annex 2 - Price cap and cross-subsidy implications of Ofgem's draft customer vulnerability strategy

Ofgem's draft CVS is focused on five areas where Ofgem seeks to "drive strong improvements for consumers in vulnerable situations"

- Improving identification of vulnerability and smart use of data
- Supporting those struggling with their bills
- Driving significant improvements in customer service for vulnerable groups
- Encouraging positive and inclusive innovation
- Working with partners to tackle issues that cut across multiple sectors

The draft CVS sets out a variety of desired outcomes that Ofgem wishes to see, summarised at Appendix 2 of the CVS consultation document. In general, it appears that Ofgem envisages that these outcomes will result from various requirements for suppliers to 'do more' whether through reinterpretation and more vigorous enforcement of existing licence conditions or the introduction of new regulatory obligations.

Whilst the CVS consultation makes passing reference to the default tariff price cap (DTC), the CMA's prepayment charge restriction (PCR) and the possibility of enduring price protection for vulnerable customers, it does not explicitly consider how potentially substantial additional costs that may result from its proposals will be funded in the context of the DTC or any successor price cap (or, indeed, in the absence of any further cap).

This is a serious omission which must be rectified before the CVS is finalised. We note that such analysis, with full supporting evidence base, is required in any event to address the Regulatory Policy Committee (RPC)'s reservations about the adequacy of the impact assessment underpinning the DTC. The RPC made clear that it required further detail on assumptions and calculations for the period 2021-2023 in the event that the DTC is extended beyond 2020.

Below we explain in further detail why Ofgem cannot further develop its CVS in a vacuum that takes no account of the unavoidable interaction with the DTC. Put simply, in the short term, if Ofgem wishes to impose extra costs on suppliers it will need to increase cap allowances accordingly. However, Ofgem should also look beyond the horizon of the DTC and reflect carefully on the likely unintended consequences of costly new interventions that make vulnerable customers uneconomic for suppliers to serve. There is a very real risk that well-intended interventions to protect vulnerable customers have the reverse effect in the long term.

Ofgem has a statutory duty to ensure licensed suppliers can meet their regulatory obligations

It has long been part of the statutory framework that Ofgem must have regard to the ability of suppliers to finance their licensed activities and meet their regulatory obligations. This longstanding requirement is further reinforced by the Domestic Gas and Electricity (Tariff Cap) Act 2018 (the Act) which specifically identifies *"the need to ensure that holders of supply licences who operate efficiently are able to finance activities authorised by the licence".*[6]

Ofgem maintains that whilst this and other statutory needs referred to in Section 1(6) of the Act are desirable in principle, it does not consider that the Act requires it to achieve them. It does, however, acknowledge that it must give them very serious consideration and states that it has sought to do so "carefully, rigorously and conscientiously".[7]

This is not simply a legal formality, however. It is a basic regulatory (and business) principle: it is plainly not sustainable to impose regulatory obligations that efficient suppliers are unable to finance. Therefore, before Ofgem extends regulatory obligations that stand to impose costs on suppliers, it must consider how such costs can be recovered under any prevailing price cap.

[6] https://www.legislation.gov.uk/ukpga/2018/21/section/1/enacted
[7] See for example https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_2_-_cap_level_analysis_and_headroom.pdf at paragraphs 2.8-2.10

There is no 'slack' in current cap allowances

The need to consider how any new or enhanced regulatory costs can be funded is further reinforced by the fact that the ability to recover efficiently incurred costs under current caps is already in substantial doubt.

Ofgem has acknowledged that there may be differences between suppliers that are not related to their efficiency, but which drive significant differences in their costs. Most significantly, some suppliers have a customer base that is more expensive to serve than others, for example more customers on the Priority Services Register, or fewer dual fuel accounts.[8][9]

Despite this, Ofgem has explicitly adopted a lower quartile benchmark that does not allow full recovery of efficiently incurred costs by suppliers whose efficient costs are 'high' relative to its chosen benchmark. Ofgem has sought to defend this approach by stating that setting an allowance that reflected such higher efficient costs would not, in its view, provide sufficient price protection for consumers. It has then arbitrarily reduced the operating cost allowance within the DTC by £5 per dual fuel customer (£3 per gas account; £2 per electricity account).

We have previously demonstrated how failure to control for differences in efficient cost between efficient large suppliers due to customer mix, results in a very substantial shortfall in allowance, amounting to £15 per dual fuel customer in Q1 2019 compared with Ofgem's adjusted benchmark.[10]

Ofgem has accepted that the allowance it has set may not take full account of cost differences due to payment type and does not allow suppliers with WHD customers to recover costs where their customers pay by standard credit[11] (due to Ofgem's decision to require suppliers to apply Direct Debit rates to WHD customers irrespective of payment type). But Ofgem has not adjusted cap allowances to accommodate these known additional costs.

Notional headroom provides no 'buffer' to accommodate additional costs

Ofgem maintains that it still 'expects' suppliers with a range of different customer bases to be able to finance their activities. But this expectation evidently relies on the availability of additional headroom over and above the adjusted benchmark cost allowance.[12]

However, as noted previously in response to Ofgem's September consultation on the default tariff cap[13] and in our subsequent response on capacity market allowance[14], in our view, the uncertainty component of headroom is already at least £18 per customer too low to meet the requirements of the Tariff Cap Act, before taking into account other material unforeseen costs such as the £58.6m industry RO mutualisation costs.[15]

The notional £10 headroom in the DTC is plainly insufficient to accommodate known variation in efficient costs, let alone cater for residual cost uncertainty. The combination of conscious decisions not to allow full cost recovery for suppliers with high efficient costs (e.g. due to disproportionate numbers of high cost to serve customers) and mounting evidence of failure to make adequate provision for other costs (such as mutualisation due to failing suppliers, escalating costs of policy driven industry change programmes, and Unidentified Gas (UIG)) mean even that small margin is illusory.

[8] https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_2_-_cap_level_analysis_and_headroom.pdf at paragraph 3.38
[9] Ofgem reports the median additional cost to serve PSR customers was around £10 per account and while the median additional cost to serve single fuel customers was around £9 per account in 2017. See https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_6_-_operating_costs.pdf at 2.18
[10] See for example https://www.ofgem.gov.uk/system/files/docs/2018/10/centrica_-_response_1_-_summary.pdf
[11] https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_2_-_cap_level_analysis_and_headroom.pdf paragraphs 3.93-3.94
[12] https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_6_-_operating_costs.pdf paragraph 3.17
[13] https://www.ofgem.gov.uk/system/files/docs/2018/10/centrica_-_response_2_-_appendices_2-10.pdf
[14] https://www.ofgem.gov.uk/system/files/docs/2019/02/centrica_cm_response.pdf
[15] https://www.ofgem.gov.uk/publications-and-updates/ofgem-takes-action-over-payment-shortfall

In these circumstances, Ofgem cannot credibly appeal to 'incentives to efficiency' caused by a cap intentionally set below the benchmark level of efficient cost for a fully obligated supplier as a source of funding. Ofgem itself has recognised that:

> *"A cap that is set too low could risk unintended consequences in incentivising suppliers to improve their efficiency, such as by cutting costs in a manner detrimental to customers. This would not be consistent with meeting the objective of providing protection to standard and default tariff customers."*[16]

The CMA makes a similar point in its provisional decision on the PCR.

> *"the PCR is no longer effective in meeting all of its aims, due to underestimating the costs incurred by efficient suppliers . . . . . . we note that, where the PCR was set too low, this would present the risk that suppliers reduce service levels to prepayment customers, competition is materially reduced, and suppliers may be forced to exit the market"*[17]

'Incentives to efficiency' are in practice imperatives to curb discretionary expenditure wherever possible *even where this has adverse consequences for levels of customer support*.

Price caps may be temporary, but financing requirements are enduring

The points made above focus on the immediate situation under the current DTC. The DTC itself is set to end at the end of 2020, although it may be extended up to 2023 depending on the outcome of future Ofgem reviews and decision by the Secretary of State.[18] Ofgem is presently consulting on how it should go about the first of these reviews into conditions for effective competition.

In addition to reviewing the conditions for effective competition under Section 7 of the Act, Ofgem is also required to consider whether to provide continuing protection for particular categories of domestic customers on default tariffs, including vulnerable customers, under Section 9 of the Act.[19]

The outcome of such future reviews is, of course, unknown at this stage, although Ofgem has previously indicated that it considers there may be a case for some kind of enduring price protection for vulnerable customers beyond the temporary life of the DTC.

If Ofgem should decide to pursue an enduring price cap for vulnerable customers, it will need to ensure that any such cap is consistent with its statutory duty to ensure that suppliers can finance their licensed activities, including their regulatory obligations in respect of vulnerable customers.

As Ofgem notes in passing in the CVS consultation, there are open questions about how far it is appropriate for a sectoral regulator such as Ofgem to make policy decisions with large distributional consequences, such as those that would be implied if the cost of subsidised prices for vulnerable customers were to be borne by other consumers.[20]

Cross-subsidy absent adequate provision and a level playing-field is not a sustainable funding model for vulnerable customers

Ofgem cannot safely assume that the cost of supporting artificially low prices for any particular group of customers (i.e. prices that do not allow the full cost of serving that group of customers to be recovered through the charges they themselves face) can be 'socialised' across other customers without further specific regulatory intervention to require and support this.

In a competitive market, suppliers who attempt to recover subsidies for one group of customers from other customers will find their prices are no longer competitive, making cross-subsidy commercially self-defeating over time. The commercial incentive will be to avoid the need for cross-subsidy by avoiding loss-making

[16] https://www.ofgem.gov.uk/system/files/docs/2018/11/appendix_2_-_cap_level_analysis_and_headroom.pdf paragraph 3.8
[17] https://assets.publishing.service.gov.uk/media/5cf7cd9b40f0b663f62506af/Finalised_Provisional_Decision.pdf summary paragraph 5
[18] https://www.legislation.gov.uk/ukpga/2018/21/section/7/enacted
[19] https://www.legislation.gov.uk/ukpga/2018/21/section/9/enacted
[20] https://www.ofgem.gov.uk/system/files/docs/2019/06/draft_consumer_vulnerability_strategy_2025_0.pdf page 42

customers wherever possible, which would not be a good outcome for high cost-to-serve vulnerable customers.

There is a clear tension between creating new regulatory obligations that impose additional costs to serve vulnerable customers and a wish to provide price protection to that same group of customers if such price protection requires suppliers to serve vulnerable customers at a loss. The conflict is one that Ofgem will have to confront if it chooses to pursue enduring price protection. However, the need to avoid imposing excessive costs through regulatory obligations is one that applies in any event assuming that even without a formal cap, Ofgem remains concerned to limit the costs that vulnerable customers themselves may end up bearing.

Conclusions:

1. Calls for suppliers to 'do more' to support vulnerable customers within the current regulatory framework are not provided for within current caps. Similarly, there is no provision for additional new regulatory obligations in support of Ofgem's CVS within current caps.

2. Any proposed new obligations must be justified on their own merits through rigorous impact assessment that explicitly considers funding, having regard to Ofgem's statutory duties to ensure that suppliers can finance their regulatory obligations.

3. In the short term while the DTC is in force, this will require Ofgem to weigh customer benefits it expects to result from new initiatives with the additional costs that will ultimately fall to customers to bear through higher cap allowances. However, the need for rigorous cost-benefit analysis does not stop when the (temporary) DTC comes to an end, especially where Ofgem is considering the possibility of enduring price protection beyond the life of the DTC.

4. In an effectively competitive market not subject to a general DTC, higher costs of serving vulnerable customers would need to be recoverable from those customers as cross-subsidy via 'socialisation' will not be commercially sustainable.

5. Without an explicit external funding stream, maintaining artificially low pricing for high cost to serve vulnerable customers that suppliers cannot recover would result in a clear disincentive to serve such (loss-making) customers. This would not serve the long-term interests of vulnerable customers.

6 August 2019

FRAMEWORK FOR ASSESSING ACTIONS TO SUPPORT OFGEM'S VULNERABILITY STRATEGY

1 The purpose of this Annex is to provide a framework for evaluating alternative options that Ofgem may propose to deliver its vulnerable customer strategy.

2 The role of appraisal is to provide objective analysis to support decision making. The HM Treasury Green Book, the CMA's Competition Impact Assessment Guidance and the Better Regulation Framework all provide guidance for how to undertake such appraisals. Ofgem also has its own Impact Assessment Guidance. The framework that we propose is based on these documents, and considers their specific application to the types of intervention that Ofgem may consider to deliver its vulnerability strategy. This requires the analysis to properly reflect the particular challenges that these policy choices are likely to raise.

- **The policy choice will be wide.** There are likely to be many different option choices to deliver a particular policy objective. These may span different actors in the energy sector and may also include options for delivery outside of the sector.[21]
- **The options may involve distributional choices**. Policies that require additional interventions to be in place, or outcomes to be achieved, for particular customer groups may incur additional costs. These will need to be funded either from those customers themselves or from implicit or explicit cross-subsidies from other customer groups.
- **Interventions may impact competition.** If the interventions are made in the retail energy sector, the interventions are likely to impact on competition, requiring that additional considerations are taken into account in the appraisal. In particular, the uneven way that consumers in vulnerable situations are distributed across suppliers means that many potential policy interventions risk raising costs for one group of suppliers versus another. This can be expected to have a detrimental impact on competition and consumer outcomes.[22]
- **Interactions with existing price caps must be factored in.** Whether the interventions are made at the network or retail level, they will also be impacted by the presence of price caps. The need for enquiry is particularly compelling in a scenario where a price cap is in place given that Ofgem will have already made a judgement about its view of the efficient cost base and the activities that this covers during the price cap setting process. Therefore the need to understand costs of any new policy intervention accordingly becomes more important. This will raise further issues that will need to be considered as part of the evaluation.

[21] The recent NAO report on "Vulnerable consumers in regulated industries" (NAO), 2017 commented on the need for better cross-sector working in this area.

[22] Indeed this is something that BEIS and Ofgem have recognised in a recent consultation: "Flexible and responsive energy retail markets", BEIS, Ofgem (2019).

3 What follows is a set of requirements that need to be followed to enable robust appraisal of any policy options. Such guidance is there to enable policy makers to "develop transparent, objective and evidence-based advice for decision making".[23] Failure to follow it can therefore be expected to have serious consequences.

4 We would also suggest that Ofgem engages with stakeholders at an early opportunity to improve the information that it will need to make these assessments. This is the case for assessment of the benefits of any option, as well as the costs. Reliance on largely qualitative assessments are unlikely to be adequate. Instead, quantification that stands up to scrutiny will be essential to inform an understanding of the full economic impact of any policy decision and its impact on customers.

Requirement 1: Clear articulation of the rationale for intervention and the objectives that it is seeking to meet

5 It is standard practice that at the outset of the appraisal process a clear identification of why change is necessary must be made and SMART[24] objectives set.

6 In the case of policies that are being designed to meet the strategic objectives of Ofgem's vulnerability strategy, it will be important to ensure the following.

- **The outcome is articulated sufficiently broadly.** The risk in being very specific is that it will automatically narrow down the options for delivery. For example, a broad outcome that may be sought would be to enable a particular customer group to make a more confident choice of energy provider. In contrast, a narrow one would be to identify an outcome where this could only be met by a single intervention, such as an objective to introduce a helpline service. The aim is not to constrain how the outcome can best be met before considering the long list of potential options to meet it, both in terms of how it may be delivered and who may be best placed to deliver it.
- **The beneficiaries of the action must be precisely defined and capable of identification.** As is well known, there are particular challenges with the identification of vulnerable customers given the fluid concept and its many different facets. This means that customers may only be vulnerable for a transient period of time and, depending on the issue, may or may not display vulnerable characteristics. There is also often no good identification proxy for the type of customer that the policy is trying to target.[25] It will therefore be important to think about, and address, the following questions at an early stage of policy development:
  - Is it possible to identify the customers who the policy is aimed at?
  - If not, what group of customers will be targeted by the best available proxy and what are the implications of this, particularly in terms of the cost of the policy and its ongoing viability?

  Once a policy is put in place that benefits a group of customers, it becomes very hard to remove it. This is even if it has limited ongoing justification and/or there becomes a better way of identifying those that really require it.[26]

7 Once the objective for the intervention has been clearly defined, it will then become easier to consider and evaluate the alternative options for achieving that objective.

23 HM Treasury (2018) para 1.5.
24 Specific, Measurable, Achievable, Realistic and Time-limited.
25 In addition, even if a proxy is a good measure for certain policy aims, it may be a poor one for others. For example, PSR may be a good way to identify customers who may be in need of additional help in the event of a powercut, but a poor one for identifying those requiring financial help because they are fuel poor.
26 These issues have been at the forefront of recent discussions about reforms to the funding of free TV licences to the over 75s.

Requirement 2: Identify a long list of options for meeting the objective

8 The benefit of defining the objective with reference to a broad outcome is that is should enable identification of a large range of options for achieving the aim. This is important as there may well be multiple ways to deliver an outcome when looking at policies to assist vulnerable customers.

9 To do this it helps to follow the guidance included in the Green Book to construct the alternative options around the five facets in its "Strategic Options Framework Filter", as set out in Figure 1.

Figure 1 Choices in the Strategic Options Framework Filter

Option Choices – broad description	
1. Scope	Coverage of the service to be delivered
2. Solution	How this may be done
3. Delivery	Who is best placed to do this
4. Implementation	When and in what form can it be implemented
5. Funding	What this will cost and how it shall be paid for

Source: HM Treasury Green Book

10 Using this framework, a wide variety of options for meeting the policy objectives should be tested.

- **Options in other sectors.** If the objective is to target the barriers that vulnerable customers may face, it may be that the best policy intervention lies outside of the energy sector. For example, barriers to engagement in the energy sector due to digital exclusion may best be dealt with through interventions in the communications sector.
- **Cross-sectoral approaches.** Vulnerability is very much a cross-sectoral issue and if an energy customer is vulnerable, that increases the likelihood of them also being vulnerable in other sectors. This means that options that take a cross-sectoral approach to delivery may have greater benefits than ones solely targeted in energy.[27]
- **Options within the energy sector.** There is a range of players in the energy sector and it is important that consideration should be given to which entities are best placed to fund and deliver any particular policy outcome. It is likely always to be worth exploring different options for delivery by both network companies and retailers, given the different features of the markets where intervention would be made. This is in line with Ofgem's recent strategic narrative and with the BEIS/Ofgem retail market review consultation.[28]

11 It will be particularly important to ensure a range of policy options is considered in the event that there is a risk that one of the favoured options can be expected to have an adverse impact on competition. As the CMA notes in its Guidance, "Ideally, alternative policy proposals should be identified that have a less adverse effect on competition but still enable policy objectives to be achieved."[29] We discuss this further below.

12 Given the choices to be made, it will be important not to reduce this long list too soon. Instead a robust evaluation should be taken of all options that provide a credible way of delivering the policy objective.

27 See NAO (2017)
28 See "Our strategic narrative for 2019-2023", Ofgem (2019) p17 and "Flexible and responsive energy retail markets", BEIS, Ofgem (2019) p27.
29 "Competition impact assessment – Part 1: overview", CMA (2015) para 2.11.

Requirement 3: Explicitly identify, and justify, distributional considerations

13 Policies that require additional interventions to be in place, or outcomes to be achieved, for particular customer groups may incur additional costs that will need to be funded either direct from those customers or from cross-subsidies from other customer groups.[30]

14 Ofgem has recently set out in its strategic narrative that its role is "to ensure fair prices that reflect the actual costs of providing energy to disengaged consumers and those with traditional prepayment meters" but, absent a change in Government policy, it is "not to implement social tariffs, or drive further cross-subsidy between consumer groups."[31] This implies that any new policy intervention will either be self-funded through cost reflective charges or will replace an existing policy where the cross-subsidy is already in place.

15 Because of this, we assume that there will be no need to make use of distributional analysis involving the application of welfare weights – such as that carried out to justify the Warm Home Discount[32] – to justify policy interventions.

16 We instead assume that any additional costs associated with new policies will either be capable of being funded direct from those customers that benefit, or will replace existing policies at lower cost. This should be made explicit within the appraisal process, assuming it is true. The information on which to undertake such analysis has often been lacking in the past. It is therefore good that Ofgem is seeking a better understanding of distributional impacts from its policy interventions and will be improving the information base it uses to do this.[33]

Requirement 4: Undertake a rigorous competition assessment

17 If the policy intervention will impact on a non-monopoly part of the energy market, it is imperative that a full assessment of any risks of distortions to this market arising from it is undertaken. This should be seen as being of at least equal importance to any static assessment of costs and benefits that an appraisal involves.

18 While the Green Book is not particularly instructive in the assessment of such factors, both the CMA's Competition Impact Assessment Guidance[34] and the OECD Competition Assessment Toolkit[35] set out how such assessments should be done. Ofgem will need to develop its thinking in this area, and also improve the information it has available to undertake such analysis. This has previously been highlighted as an issue by the Regulatory Policy Committee (RPC) when it voiced its reservations about the adequacy of the impact assessment underpinning the Default Tariff Cap.[36]

19 We would expect that any intervention that will have an impact on the energy retail market will require an "in-depth competition assessment", as defined by the CMA.[37] The CMA's guidance provides a framework for undertaking this. It begins with a requirement to identify the affected markets and identify a baseline. The focus of the assessment is then structured around assessing four questions about the policy's expected impact on the market.

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30 If the funding comes from a cross-subsidy between customer groups, good practice would dictate that this should be made explicit in any policy evaluation.
31 Ofgem (2019) p16.
32 "Warm Home Discount Scheme 2018/19 - Final Stage Impact Assessment", BEIS (2018).
33 "Draft Consumer Vulnerability Strategy", Ofgem (2019) p11.
34 https://www.gov.uk/government/publications/competition-impact-assessment-guidelines-for-policymakers
35 https://www.oecd.org/competition/assessment-toolkit.htm
36 The RPC made clear that it required further detail on assumptions and calculations for the period 2021-2023 in the event that the DTC is extended beyond 2020 https://www.ofgem.gov.uk/system/files/docs/2019/07/rpc-43581-beis-ofgem_domestic_gas_and_elctricity_default_tariff_cap_-_iaf_-_opinion.pdf
37 As defined in "Competition impact assessment: Overview" CMA (2015).

- Will the measures directly, or indirectly, limit the number or range of suppliers?
- Will the measures limit the ability of suppliers to compete?
- Will the measure limit suppliers' incentives to compete vigorously?
- Will the measure limit the choices and information available to consumers?

20 Consideration of all of these questions will be required when assessing a policy intervention that will impact in the retail sector. However, perhaps the most important consideration falls under the first of these questions and involves an assessment of whether the policy risks "raising the costs of some suppliers relative to other suppliers".[38]

21 This is likely to be a central part of any investigation given that suppliers have different numbers of customers with vulnerable characteristics. Therefore, if the policy intervention has a cost associated with it that is related to the number of vulnerable customers, this will have the effect of raising the costs of some suppliers relative to others. This is a particular issue if suppliers are then unable to set cost reflective prices to these customers. It is also the case if a policy is only applicable when there are exclusions to participation based on the size of the supplier. A policy intervention that increases the costs of suppliers with a disproportionate number of vulnerable customers is likely to distort competition and lead to consumer detriment.

22 The importance of this issue has recently been highlighted as part of the BEIS/Ofgem review of the retail market, which considers the "risk that the uneven way that high cost-to-serve consumers are distributed across suppliers could lead to further distortions" in the retail market.[39] These high cost-to-serve consumers are "particularly consumers in vulnerable situations with higher customer service needs and/or customers at a higher risk of indebtedness".[40] As well as the impact on supplier's ability to compete for customers and the risk of efficient suppliers being unable to compete, it also creates incentives for suppliers to avoid attracting these customers that have a higher cost-to-serve. This is unlikely to be in those customers long-term interests. The seriousness of the distortion seems to have been recognised and it concludes "any future scheme proposing additional obligations on the supply market should be designed with an understanding of the retail market impact in mind".[41]

23 Given its importance, we would expect any appraisal to look quantitatively at the impact on competition of the policy change. As the CMA notes, quantitative analysis requires less need for judgement and provides estimates of the numerical impact of the measure. It also requires data, the technical skills to undertake the analysis and more time,[42] all of which should be available to Ofgem.

24 In this context, quantification could come from a predictive economic study of the policy proposal's impact. Such analysis should estimate the impact on price, cost, quality of service and also make an assessment of the impact on innovation in the affected markets. The results can then be compared with the impact of other similar policies.

25 Given the recent work that has been done by BEIS and Ofgem to look at the impact of policy delivery in the retail sector, there will be evidence available with which to compare the expected outcomes. It would be helpful for Ofgem to set this out in advance of its policy development phase, so it can help inform the choice of options. The OECD Competition Impact Assessment Toolkit also has an assessment of average price impacts from different types of restriction that provides

38 CMA guidance p9
39 "Flexible and responsive energy retail markets", BEIS, Ofgem (2019) p27.
40 BEIS, Ofgem (2019) p27.
41 BEIS, Ofgem (2019) p27.
42 Competition impact assessment – Part 2: guidelines",CMA (2015) p47.

a 'rule of thumb' to estimate the price effect of introducing a regulatory restriction and there are circumstances when these may be useful.[43] Estimates of consumer harm can then be calculated.

26 When considering competitive effects in the energy retail space, it will also be important to consider the following issues.

- Any comparison of policy costs should be undertaken with reference to the direct operating costs of suppliers, rather than using revenue as a proxy, given the nature of the retail function and the level of pass-through costs.
- Given the expectation that the retail sector will be subject to further disruptive change, undertaking a specific assessment of the impact of the policy on innovation will be of particular importance. This should recognise that the innovation may be necessary to meet other public policy objectives and if these might be constrained by the policy intervention, they will need to form part of the evaluation.
- Consideration will need to be given to any demand-side impacts of the policy that could impact on switching (positively or negatively). For example, will the policy make customers think that there is a risk that they will lose the support if they change supplier?
- There needs to be the capability for sufficient oversight of the policy to ensure that all suppliers meet the requirements. Without this, the appraisal must take account of the additional distortion that this failure will create.
- The energy retail sector has had a history of policy exemptions for retailers with less than a certain number of customers. This is something that is one of the aspects of the market that BEIS/Ofgem are looking to potentially reform. In the event that it is not reformed, any assessment of competition effects from lowering barriers to entry through such exemptions must take account of the number of suppliers already operating in the sector.

27 We also note that, at least until the end of 2020, this review will also need to understand the impact of the policy on competition while the price cap is in place. We consider this further in the next section.

Requirement 5: Consider the impact of the price cap

28 Given that there are price caps in place on both retail and network companies, Ofgem will need to consider the impact of them from any policy obligations. As part of the price cap setting process, Ofgem will have already made a judgement about its view of the efficient cost base and the activities that this covers. Therefore the need to understand costs of any new policy intervention accordingly becomes more important. To the extent that there is a cost associated with delivering a new policy, consideration of how this will be treated in the cap will be required.

29 In the case of the retail price cap, it will not be possible to assume that any additional activity can be financed through headroom or margin. There are therefore two basic options for how any cost will need to be dealt with in the cap:

- the cap can be increased to cover the cost; or
- trade-offs will need to be made such that activities that would have been financed under the cap will instead have to be discontinued.

30 If the second of these options is taken, the appraisal will need to consider the activity (or activities) that will no longer be carried out. The baseline against which the policy is measured will then need to include the costs and benefits of the existing activities, while the appraisal of the policy

43 This is available on their website: https://www.oecd.org/competition/assessment-toolkit.htm

option will need to include the change to costs and benefits associated with those existing activities no longer being undertaken.

31 Any such evaluation will also need to take account of the impact the change in activities will have on distributional outcomes, to check that those are in line with Ofgem's strategic intent not to drive further cross-subsidies.

Requirement 6: Undertake cost benefit assessment with an appropriate counterfactual and a data set that is fit for purpose

32 The Green Book provides clear guidance for policy makers in how to undertake a static cost benefit assessment. There are two main factors that can compromise the quality of an appraisal that follows it.

33 The first is an inappropriately specified counterfactual. When evaluating a policy, it is important to compare it with the appropriate counterfactual. This may need to take account of the fact that, even absent the policy intervention, there may be changes to the current landscape that need to be taken into account.

34 The second is inadequate data. Ofgem should undertake work now to get a better data set with which to undertake the evaluation of policy interventions to help vulnerable customers. It has already expressed its intent to improve the distributional impact tools it uses in its assessments.[44] It should go further and also consider the wider information base it will need for such assessments.

- On the cost side Ofgem has a good basis on which to start to do this from both the cost assessment undertaken as part of the price cap setting process and the work it is undertaking jointly with BEIS on retail market reform. It should put these sources together and then consult with stakeholders about its adequacy and whether there are options for improving it ahead of the need to use it for a particular appraisal.
- On the benefit side, estimation risks being largely qualitative and potentially subjective if Ofgem does not act now. It should share its current evidence base for making such assessments so that it can be improved with stakeholder input. In the event that certain benefits are particularly difficult to quantify, this will need to be explicitly acknowledged, and greater use made of sensitivity analysis to assess how dependent the case for that option is on those assumptions.

44 Ofgem (2019) p11.

Annex 4 – Ofgem's preferred outcomes

1. Improving identification of vulnerability and smart use of data

Outcome 1A: We want energy companies to act swiftly to provide support to the people who need it. To ensure they can do this, we want them to regularly maintain and proactively update the data they hold on their customers, including their Priority Services Register data.

As the supplier with the largest Priority Services Register (PSR) in the industry, we recognise the importance of effectively identifying these customers.

Moving forward, as we have more access to a wider range of smart meter data, we will continue to seek out new and innovative ways of proactively supporting our customers.

Whilst we agree that the PSR is an important part of supporting vulnerable customers, it is not, however, a good proxy for more specific aspects of vulnerability. As Ofgem repeatedly notes, vulnerability is neither a simple nor a single issue and different aspects of vulnerability will require different approaches. Therefore, simply maintaining all-purpose vulnerability flags will not always be helpful or indeed, relevant.

The proposed measure to monitor this outcome is by "reporting PSR data trends through Social Obligations Reporting (SOR) including assessing the consumer experience of some of these measures". The CVS consultation does not expand on how Ofgem intends to assess the consumer experience nor does it propose what measures will be used to gather this level of detail. Likewise, there is currently no metric in the existing SOR for this, or the revised metrics Ofgem consulted on last year, so we would expect there to be a full consultation on any additional changes to the SOR proposed metrics.

Outcome 1B: We want to see evidence that there has been an improvement to support consumers to self-identify, for example through best practice guides that are easy to access and understand.

Whilst we agree that customers do not always self-identify as needing support, further insight is needed on what it is that customers with poor mental health require from suppliers. Whilst it is the intention of Citizens Advice to carry out some research in this area, there are no guarantees it will provide simple solutions on how customers will feel more comfortable about disclosing their circumstances to suppliers. Neither is it clear from the consultation how providing, for example best practice guides, will help these customers to self-identify.

Ofgem must be clear as to:

- the evidence that it is seeking in terms of there being an improvement in self-identification,
- the base data and metrics which will be used to establish an improvement, and
- what the level of expected improvement looks like.

For example, to help drive more customers to self-identify and assess whether they are eligible for the PSR, we are currently exploring a self-serve option on our website. This will enable customers to record and join the PSR via our website and engage with an agent from our specialised team via webchat or telephone.

Additionally, through our sales process and the switching sites, customers can self-identify online and join the PSR. All our agents are trained to recognise vulnerable situations and we also have our specialist Priority Services Team, which offers additional support and care to customers.

However, even by suppliers innovating in these areas, Ofgem must recognise that this is a very difficult area as many customers simply do not want to self-identify (for a number of perfectly understandable reasons).

Outcome 1C: We want to see better use of data across regulated sectors to enable more holistic and targeted support for consumers in vulnerable situations.

It is not clear from the consultation how Ofgem expects to achieve the better use of data across regulated sectors.

Ofgem should also be clear if it is specifically referring to data from smart meters ‘smart meter data’ or data and information from other sources. There are benefits to be gained from the use of smart meter data, particularly for vulnerable customers. However, for these to be fully realised, there needs to be a joined-up approach from Government and the Regulators, and specifically including the involvement of the ICO. There also needs to be completion of Privacy and Regulatory Impact Assessments on the use of smart data.

We believe that the biggest benefit to data usage in the energy industry would be for all stakeholders to review and input into an overall strategy on data, i.e. one that provides a clear direction on what is trying to be achieved. This will avoid the potential pitfall of numerous activities being carried that, though well intentioned, do not complement one another. Consideration needs to be given to not only how data can benefit consumers right now, but also what it should look like in the future.

A number of the data proposals will involve both cost and resource to implement. With numerous initiatives being considered, as set out above and particularly in a price cap constrained environment, Ofgem will need to be very clear about how these activities are to be financed.

To make the most of any learnings from the proposed data sharing with the water sector, it would make sense to wait until this process has been implemented and evaluated before further data sharing options are introduced.

2. **Supporting those struggling with their bills**

Outcome 2A: We want consumers to have access to affordable energy

We agree that consumers should have access to affordable energy and that ongoing compliance with the price cap should be monitored.

In paragraph 2.4 of the CVS, reference is made to the Energy UK Commission for Customers in Vulnerable Circumstances, that recommended that Ofgem “revisit the provision of social tariffs”. The consultation states that Ofgem would take on the role only when and if, the government were to revisit its programme for financial assistance with energy costs.

Ofgem should be clear as to what it sees as the difference between a social tariff and a price cap for customers in vulnerable situations. If a social tariff is introduced, then Ofgem, or specifically BEIS, would need to consider:

(i) how this will be funded, ensuring a level playing field between suppliers;
(ii) how will the definition of which group of customers who would be eligible be reached; and
(iii) how to ensure support goes to the right customers (i.e. those who struggle to pay, as opposed to those who choose not to pay).

The upcoming review of the Fuel Poverty Strategy and the Future Retail Energy Market review are probably the best places for that discussion, as decisions with re-distributional consequences must be for elected representatives to make, rather than Ofgem.

We understand that affordability is an issue for some of our vulnerable customers and for over 30 years we have worked with National Energy Action, the leading charity for fighting fuel poverty. It is essential to consider that low incomes reflect wider poverty. Whilst energy efficiency improvements can help address affordability as well as decarbonisation, in some cases, they are not cost effective, and in others, measures are insufficient on their own.

The DWP should take the lead on identifying which individuals and families receive support, including support on energy bills. For energy, such support could in principle take the form of a capped tariff or a cash rebate, subject to appropriate funding. However, we think the rationale for preferring a cash rebate to a social tariff or price cap remains valid (i.e. as the Government decided and implemented the WHD). We will provide more thoughts on these matters in our response to Ofgem’s Flexible and Responsive Retail

Markets consultation. We also draw Ofgem's attention to Centrica's paper, 'Levelling the playing field[45]' which gives our view that there should be no supplier exemptions to the WHD in a competitive energy market.

Outcome 2B: We want to see better support for consumers who are at risk of self-disconnecting and a decrease in the number of self-disconnections

Self-disconnection should be an area where support is provided.

Paragraph 4.17 of the CVS states that Ofgem's data shows one in ten prepayment meter customers temporarily disconnected from their supply in 2017 and Ofgem intends to gather better insight into this area, through the revisions to the Social Obligations Reporting.

As we set out in our response to the SOR consultation, dated 22 January 2019, we would like the opportunity to discuss further the inclusion of the proposed new indicator on the number of smart meter customers who have self-disconnected. With the changes to the industry infrastructure for smart meters, suppliers do not yet fully know what alerts will be available for reporting. This will need to be considered by Ofgem in due course, as will how Ofgem intends to use the output from this metric. Our offer to discuss with Ofgem in more detail still stands.

Also, as set out in our letter of 21 February 2019 in response to Ofgem's RFI on Self-Disconnection, the reasons for a customer self-disconnecting cover many situations, including change of tenancy, moving out and seasonality where the customer consciously chooses to self-disconnect as a means of budgeting. Without clear guidelines as to the specific definition and criteria that constitutes self-disconnection, it would be (i) impossible to compare one supplier against another as the reasons for self-disconnection vary significantly; and (ii) evaluate if the self-disconnection is causing a risk of detriment. Not all temporary self-disconnections cause a detriment to the customer. For example, when a property is empty, not having to top up would be a customer choice where the customer suffers no detriment.

Likewise, it is extremely difficult and in fact almost impossible to accurately identify those customers who are self-rationing, without clear parameters as to what constitutes "very low energy consumption". This was the definition Ofgem set out in the Request for Information: Self-disconnection and self-rationing, published on 17 January 2019. Low energy consumption is a very subjective measure, as some households may only need to use a smaller amount of energy (for a number of very good reasons).

Self-rationing does not just affect prepayment meter customers. Customers on other payment methods, through a credit meter, may also decide to, or experience limiting their energy consumption. This may range from a customer simply turning the thermostat down slightly (for whatever reason), through to a customer not putting their heating on at all. Again, it must be recognised that a customer may actively choose not to put their heating on, so this is not necessarily an accurate gauge of any detriment.

With Smart Meter data, suppliers should find it easier to analyse consumption patterns to help identify if there is a change in customer behaviour. This, of course, would be subject to the customer giving their consent for their data to be used in this way, or for the data sharing regime for Smart Meters to be changed. There may however, be costs associated to implement a process. A change of consumption behaviour is not always an indication of detriment. There could be reasons as we have outlined above, where there is a change in consumption but no detriment to the customer.

Outcome 2C: We want consumers in payment difficulty to be proactively supported, including by being put on an affordable payment plan. We want to see more consumers become debt-free for their energy debt as a consequence, and the levels of debt to come down overall.

We agree with this outcome and with the proposed monitoring of this outcome through the existing Social Obligations Report.

Paragraph 4.23 considers whether it is necessary to strengthen the Ability to Pay (ATP) rules. Does this relate to the proposal to include the ATP principles into the SLCs, or does this refer to both inclusion and

[45] https://www.centrica.com/sites/default/files/levelling_the_playing_field.pdf

also changes to the principles? It would be helpful to understand the areas where Ofgem feels the principles need strengthening.

We are surprised that the impending introduction of HMT’s Breathing Space initiative, to provide consumers who are in problem debt with protection from credit action, was not referenced more fully in the consultation. This is another example of where well-intentioned policy or activity (which we support in principle) is being introduced without due consideration to how it interacts with both existing efforts to support those in debt and how it fits into the future policy landscape. Specifically, the lack of provision in the price cap for any new vulnerability initiative.

Citizens Advice’s Report *Supply and Demand* has asked that Ofgem publish the lessons learned from the recent review of suppliers’ procedures and communications with customers in payment difficulty which showed inconsistencies in repayment rates and weaknesses in assessing consumers’ circumstances. It would be useful to add these findings into the “Poor outcomes for customers in debt” theme to help suppliers identify areas of best practice.

Outcome 2D: We want new gas connections for fuel poor consumers who are not on the gas grid to be better targeted, to make sure those who need it most can benefit from the scheme and save on their heating bills.

We support the RIIO-2 proposals to extend the Fuel Poor Network Extension Scheme (FPNES). This includes the requirement for Gas Distributions Networks to submit targets for the number of FPNES connections in their Business Plans, and for these to be assessed by Ofgem and challenged by Consumer Engagement Groups. We also support the inclusion of a re-opener mechanism to deal with any changes in government policy.

3. **Driving significant improvements in customer service for vulnerable groups**

Outcome 3A: We want energy companies to have a corporate culture that focuses their efforts to identify and support consumers in vulnerable situations.

We agree with this and over many years have invested a significant amount of resource into helping those consumers who are most in need, not only financial help, but also in terms of staff training, charity and NGO partnerships and local community investment programmes.

Our culture is to offer support and ways to identify customers in vulnerable situations; something that all our agents are trained to do. In 2018, we referred over 4,100 people to StepChange Debt charity, which helps people who are having difficulties paying their bills and need advice on how to manage their finances.

We also work with a number of organisations, such as Macmillan Cancer Support, housing charity Shelter, Islington Council and CLIC Sargent, the leading children’s cancer charity.

In 2017 we won the Dementia Friendly Organisation of the Year award recognising our success in creating over 21,000 Dementia Friends and becoming dementia-friendly. Also, in February 2018, the Dementia Friendly Utility Guide was launched; we led the industry’s steering group and co-authored the guide with the Alzheimer’s Society.

However, as we have noted throughout this response, if Ofgem is keen to see energy companies embed a corporate culture that focuses their efforts to identify and support consumers in vulnerable situations, Ofgem will need to provide a clear analysis on how it believes that this can be achieved and funded.

Outcome 3B: We want industry to have systems to better target and to tailor their customer service to consumers with specific needs.

We already take a number of effective steps to understand our customer needs, both through customer engagement and through our internal processes and systems, to ensure customers receive appropriate support.

We are comfortable with the proposed guaranteed standards for gas distribution companies, and the proposal to introduce a licence obligation on how gas distribution companies treat consumers in vulnerable situations. We would expect a similar licence obligation to be introduced for electricity distribution in due course.

Outcome 3C: We want new companies entering the market to be able to provide an adequate level of customer service to consumers in vulnerable situations.

We agree with this outcome, although this does need to reflect the theme that existing smaller suppliers as well as new companies entering the market must provide adequate customer service.

Ofgem has a very important role to play here in providing clear rules for smaller suppliers and these new entrants. Recent blogs from a number of organisations have called on Ofgem to include the review of customer service arrangements as part of approving licences for new suppliers.

Citizens Advice has noted[46] how the current supplier licensing regime has "allowed insufficiently prepared suppliers to enter the market and resulted in acute customer service issues".

We agree with Citizens Advice's view and we feel that it is for Ofgem, as part of its process when issuing new supply licences, to ensure that new entrants can provide evidence of credible customer service plans and can satisfy the provision for serving consumers in vulnerable situations. This will be in conjunction with meeting all the appropriate criteria as required for any new entrant.

Consumers can suffer from adverse selection in supply markets because they cannot effectively appraise whether suppliers are likely to suffer financial difficulty. Regulators may face a similar problem when approving licenses for new suppliers. In these cases, "risky" suppliers, which follow a strategy of offering low prices and compelling switching offers to new customers, may initially outcompete "good" suppliers, who offer prices that can be maintained regardless of customer growth. This may result in a large proportion of "risky" types entering and operating in the market.

Both moral hazard and adverse selection increase the chances of suppliers failing and offers incentives for suppliers to enter the market without a full understanding of their obligations to their consumers. Both factors are likely to leave customers worse off, including those customers that may be vulnerable.

Centrica supports Ofgem's supplier licensing review decision[47] to introduce tougher market entry requirements and we further propose a new licence condition[48] to prevent the mutualisation of costs should a supplier fail.

Outcome 3D: We want consumers to be effectively identified as eligible for priority services: and for them to receive consistent and high-quality priority services in a timely way.

We understand Ofgem's rationale for not reopening its definition of vulnerability. However, society is changing, and concepts of vulnerability and vulnerable customers are themselves fluid. Groups previously flagged as 'vulnerable' may not always be the case. For example, the need for any specific priority action or treatment to protect a healthy, well-off, digitally-savvy 70-year-old is far less clear today than when the regulations were originally drafted. We recommend there should be a full review by Ofgem as to whether it should remove the more prescriptive definitions within the licence conditions, as these are already covered within the existing overarching vulnerability principle. This will enable suppliers to effectively identify which eligible customers would benefit from priority services.

Through the training and processes we have in place we feel that we effectively identify when the right support is needed.

However, if Ofgem feels that other suppliers are not offering this standard, as set out in the SLCs, then this should be addressed directly with the relevant suppliers.

Outcome 3E: We want consumers to have easy access to relevant information on how well energy suppliers support consumer needs. This will allow them to take this into account when switching.

46 Citizens Advice's response to Ofgem's supplier licensing review:
https://www.citizensadvice.org.uk/Global/CitizensAdvice/Energy/Energy%20Consultation%20responses/Citizens%20Advice%20response%20to%20supplier%20licensing%20review.pdf

47 Ofgem's final proposals on entry requirements: https://www.ofgem.gov.uk/publications-and-updates/supplier-licensing-review-final-proposals-entry-requirements

48 Centrica's response to Ofgem's supplier licensing review: https://www.ofgem.gov.uk/system/files/docs/2019/04/centrica_response.pdf

We don't necessarily agree there is a lack of information around how well customer needs are supported. We do a significant amount to provide information on the support available to help consumers in vulnerable situations, as noted throughout this response.

We are supportive of Ofgem working with Citizens Advice on its work plan to develop an easy to understand vulnerability supplier indicator that will show how well each supplier is treating consumers in vulnerable situations.

4. Encouraging positive and inclusive innovation.

Outcome 4A: We want all consumers (particularly those in vulnerable situations) to have access to affordable energy and suitable services. We want products and services to be designed to meet the needs of a wide range of consumers (including the most vulnerable).

As noted above in Section 3, we are supportive of all customers having access to affordable energy and suitable services, (for example, Time of Use tariffs).

The recent former GB energy regulators paper[49] responding to Ofgem's Discussion Paper on the proposed framework for assessing effective competition in fact argues that all consumers are benefiting from competition and the main things damaging competition are the prepayment meter and default tariff price caps.

We are fully supportive of Ofgem's regulatory sandbox approach to innovation. However, Ofgem must continue to demonstrate a flexible approach in considering suppliers' requests for derogations and show a more open and supportive approach when assessing requests to undertake trials.

Outcome 4B: We expect suppliers and networks to demonstrate innovative measures to support consumers in vulnerable situations.

As previously flagged throughout this response, the price cap constrains investment for suppliers, including investment in innovation.

However, we support the proposed changes to RIIO-2, which allow innovation spending on projects which address consumer vulnerability, and the introduction of a use-it-or-lose-it allowance for initiatives that address consumer vulnerability and CO safety.

5. Working with partners to tackle issues that cut across multiple sectors

Outcome 5A: We want to achieve greater understanding and consistency across essential services markets for more joined up action to improve the experience of consumers in vulnerable situations.

The consultation mentions UKRN and the pilot PSR data sharing project between water and electricity; however, there is no reference to other regulators in terms of best practice. To better understand consistency across essential services, we would expect Ofgem to engage with regulators like CMA, FCA, Ofwat and Ofcom.

There must be a joined-up approach from Regulators and Government to identify the common ground on vulnerability, what they are trying to achieve and what the current differences are. To provide a joined-up approach and reduce unnecessary costs (and regulatory burden), future market developments need to be considered holistically rather than multiple "singular" strategies from numerous sources.

It is, also, disappointing that there is no reference within the consultation for Ofgem and the DWP to align their policies on Third Party Deductions ('Fuel Direct'). This is an area where we have repeatedly offered our support to work with both Ofgem and DWP to look at improvements to the current processes and licence obligations. The current Ofgem Supply Licence Condition relating to Third Party Deductions is at odds with the guidance set out by the DWP. This anomaly must be addressed and corrected.

[49] Former GB energy regulators paper: https://www.eprg.group.cam.ac.uk/tag/s-littlechild/

We have noticed that the impact of the DWP transition to Universal Credit (UC) is causing difficulties for customers, as they can go several weeks without receiving benefits or other support. This delay in payments is detrimental to the customer and impacts on suppliers which are seeing the problems every day across their front line, as customers are more likely to self-disconnect or self-ration when faced with this scenario.

Outcome 5B: We want to further improve our information sharing approach with the third sector, which will help target our policy, compliance and enforcement actions and support organisations who provide advice to energy consumers.

Whilst we agree that improvements to Ofgem's information sharing approach could help organisations who provide energy advice to consumers, this should not be based on single or limited examples. Paragraph 7.5 refers to one successful example provided by the Extra Help Unit, on evidence of issues faced by consumers in vulnerable situations. We would hope that a single case is not the barometer for wider issues, as this could result in a biased view of the potential issues these consumers face.

Outcome 5C: Through E-Serve, we will continue to improve the operations and effectiveness of the government social programmes.

Outcome 5D: We will work with government on common consumer challenges to complement its social policy measures.

We agree with these outcomes.

As we've previously said in our response, we agree that the roles of Government and Ofgem needs to be more clearly defined. The starting point for this should be for Ofgem to evaluate and review where it wants to get the market to and then how we get there. This should take account of numerous other policy areas, including data strategy, vulnerable customers, and the supplier hub model.

Annex 5 – Ofgem's four specific questions

The comments set out in this Annex support the answers we have given above. Therefore, we have only provided comments which have not already been raised.

Question 1: Do you agree with the five priority themes and the outcomes we will aim for (as set out in Chapters 3 - 7 and Appendix 2)?

We broadly agree with the five priority themes and we have set out our thoughts and views on the preferred outcomes for each of these themes above (including where we do not agree).

Question 2: Do you agree with our approach on affordability? While we recognise this is a concern for many consumers in vulnerable situations, we think addressing wider affordability pressures is mainly a matter for government to address.

Yes, we agree that there is a need for Government to take the lead, with Ofgem and other Regulators playing a supporting role.

Question 3: What more could be done through energy regulation to assist consumers in vulnerable situations in the longer term? How should any such further measures be funded?

As we set out in our covering letter, and repeatedly throughout this response, the implications of the default tariff price cap for Ofgem's proposed vulnerability initiatives are stark: either Ofgem needs to increase the cap to facilitate specific funding of *each* of the measures being proposed, or it must specify and facilitate equivalent spending or savings elsewhere that are already built into the cap.

The cost of identifying and supporting customers in poverty (not just limited to fuel poverty) should not fall on suppliers, as wider support is needed. Ofgem must recognise that there are certain segments of customers who, as a result of their poverty, are unable to afford the energy they require for their homes and need support from the state, funded through general taxation. These customers should be identified through a method which uses existing government data (e.g. DWP data) or through specialist agencies such as Citizens Advice.

Question 4: Do you agree with our proposals for the first year of the strategy?

Proposal 1: Create an analytical framework to consistently assess the impact of our policies on particular groups of consumers in vulnerable situations. This will enable us to assess consumers groups at risk in a more targeted way and propose tailored mitigations.

It is not clear which groups of consumers in vulnerable situations will be targeted nor how the evidence will be gathered that will feed into the framework referred to. The assessment needs to consider whether this targeted approach has unintended consequences for any groups who sit outside of the particular group Ofgem has decided to target. Ofgem's resources are finite and so whilst it targets its work on specific groups it could be overlooking something else it should be looking at.

Proposal 2: We aim to strengthen protections for consumers in vulnerable situations who self-disconnect from their prepayment meters.

Please refer to our response to Outcome 2B in Annex 4.

Proposal 3: Consult on our proposals for the future energy retail market

We look forward to engaging with Ofgem on this.

Proposal 4: Consider formalising the Ability to Pay principles in our rulebook to provide targeted support to consumers facing payment difficulty

Please refer to our response to Outcome 2C in Annex 4.

Paragraph 8.13 of the CVS considers whether to strengthen the ATP rules. Ofgem should confirm if it is proposing to only copy the main headings of the ATP Principles into the SLCs or the full detail of the ATP Principles in their entirety.

Proposal 5: Propose a requirement on gas network companies to adhere to a vulnerability principle, similar to the obligation that we have placed on gas and electricity suppliers.

We support this in principle and expect similar arrangements to be introduced for electricity distribution in due course.