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20 September 2017

Dear Barry,

Response to consultation on default tariffs for domestic customers at the end of fixed-term contracts

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We welcome the opportunity to respond to Ofgem's proposals on default tariffs. We agree that these changes could result in positive outcomes for consumers, in the form of potentially lower energy costs and price security over the period of the default tariff. The new freedom is an opportunity for suppliers to consider how they treat their customers at the end of the fixed term period - and to justify why they continue to roll customers onto the SVT should they choose to do so.

However, there are also some risks for consumers from these changes, which Ofgem's proposed controls seek to mitigate. In some areas we think these should go further, to ensure that consumers benefit from these changes.

Consumer engagement

One risk of the change is that consumers rolled onto a fixed term default tariff become less likely to engage in the market. There is currently a lot of interest in the impact of the renaming of tariffs on customer behaviour and engagement. We are concerned that names related to 'fixed tariffs' may lead consumers to think they are unable to switch supplier/tariff, or that they need to pay exit fees to do so, even though this would not be the case. This could be exacerbated because in recent years messages from consumer groups, the media and others have often used the SVT as a shorthand for default tariffs.

Ofgem itself recently highlighted the naming of default tariffs as an area of interest that should be trialled by suppliers.[1] Ofgem should ensure that any learning from trials is shared and applied to all default tariffs, not just SVTs.

Ofgem should also monitor the impact of the changes carefully, including differences in consumer engagement between those who default onto fixed, rather than variable, tariffs. It should also adapt its reporting on non-prepayment account types[2] to separate out default fixed tariffs. If this evidence shows that engagement by these consumers is reduced then further action, in the form of extra prompts or other communications to consumers, may be required.

There is also a risk that customers who repeatedly roll over onto default fixed contracts may experience small annual increases that decrease their propensity to engage, but with the cumulative impact that they pay significantly more than if they had switched. This has been a feature of the insurance market, where pricing is much more personalised.[3] Companies can become adept at pricing products according to their assessment of a customer's particular price sensitivity.

Ofgem's new 'informed choices' principles require a supplier's tariffs to be easily distinguishable from each other,[4] with the stated aim that this should prevent tariff proliferation.[5] This principle should help prevent this sort of pricing behaviour in energy, by limiting the choice of tariffs available to a supplier to use as default tariffs. Despite this, the principle was not mentioned in the 'related initiatives' section of the consultation. Ofgem should make clear in its decision that tariffs chosen as the default are also covered by the informed choices principles, despite them not being actively chosen by the consumer.

Price and type of default tariff

We support Ofgem's proposal that suppliers must take account of the consumers characteristics and preferences when deciding on a rollover contract, and that this tariff must be the same, or cheaper than, the SVT.

[1] https://www.ofgem.gov.uk/publications-and-updates/open-letter-finding-ways-unlock-consumer-engagement-through-supplier-trials
[2] Available under the 'Prices and profits' tab at https://www.ofgem.gov.uk/data-portal/retail-market-indicators
[3] https://www.fca.org.uk/publications/increasing-transparency-and-engagement-renewal-general-insurance-markets-ps16-21
[4] See Standard Licence Condition 25.2 https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions
[5] https://www.ofgem.gov.uk/system/files/docs/2017/01/statutory_consultation_informed_choices.pdf

It is not possible to comment on in detail how the policy outcome will be achieved because there is no draft version of the proposed defined term, “Relevant Fixed Term Default Tariff” included in the consultation. Our preference would be that this contains the same specific requirements as the Relevant Cheapest Evergreen Tariff definition (ie current payment method, same Relevant Meter Type and same Account Management Arrangement required) with an additional requirement to consider the consumer’s characteristics and preferences. If the definition relies on ‘characteristics and preferences’ alone we would be concerned that consumers rolling onto a fixed term contract may receive fewer protections than those rolling onto the SVT.

The proposals are not clear about whether the price of the default tariff should be amongst the factors a supplier considers when taking account of a consumer’s characteristics and preferences. If price is included, then where there are multiple tariffs available which meet the other criteria (tariff type, payment method, account management, lack of exit fees etc) we would expect the supplier to choose the cheapest available.

We agree with Ofgem that the change is likely to mean that, where suppliers choose to use these tariffs, the majority of consumers will roll from a one year, fixed deal onto another. These consumers may benefit from price certainty across the fixed period, and a lower cost (should the supplier choose a tariff that is cheaper than the SVT). They could lose out if the SVT price subsequently falls, but the risk of the SVT and fixed rate deviating widely across the year seems relatively small, as set out in the consultation.

We think that the risks are increased for consumers rolling off a longer fixed deal - for example a three year fix. Given the time that has elapsed since their last choice of tariff, it is more likely that the characteristics and preferences of the consumer could have changed. Suppliers will need to ensure that they have a good understanding of these before they default the consumer onto another long term fixed contract.

There may also be a higher risk that the SVT price could diverge widely from the fixed price across the period of the tariff, with the consumer paying much more than they would under the current arrangements. This can be demonstrated by looking at Ofgem’s data on the changing value of the SVT from 2014 to 2017.[6] Had the proposed new rules been in effect in 2014, a customer rolling onto a three year

[6] Average SVT (Big 6) for typical domestic dual fuel customer paying by direct debit. See chart titled ‘Retail price comparison by company and tariff type: Domestic (GB)’ at https://www.ofgem.gov.uk/data-portal/retail-market-indicators

fixed deal set at the price of the average SVT would have been paying £84.78 a year more than the average SVT by the time their default tariff ended.

Date	Annual cost (SVT, Big 6)	Three year fixed deal	Difference
January 2014	£1145.84	£1145.84	-
January 2015	£1124.33	£1145.84	£21.51
January 2016	£1098.03	£1145.84	£47.81
January 2017	£1061.06	£1145.84	£84.78

Table 1. Average Big 6 SVT compared to the cost of a three year fixed deal

Of course these customers could engage with the market, but may also be less likely than those on a shorter fix to do so, as it will be a significant period since they last did so. These customers will receive the Cheapest Tariff Message - but, as the consultation sets out, this is less likely to be effective than an end of fixed term notice, which they will not receive until the end of the fix. They may also receive prompts from the database remedy - but while this is still being tested it is not possible for us to comment on the likely effectiveness of this intervention for these customers.

We therefore consider that it would be a sensible and proportionate for Ofgem to require suppliers rolling consumers onto longer fixed deals to check annually that the consumer is not paying more than they would on the SVT - and to change them onto a different tariff if this is the case. We do not think that this would be onerous for suppliers, as they would only need to do this assessment if the SVT had fallen in the previous year, which may often not be the case. If this control had been in place in the example set out above then the consumer would have saved around £70.

<u>Implementation of the proposals</u>

It is not clear from the consultation (para 2.33) how Ofgem expect suppliers to implement these changes through their contracts; in particular whether they will apply to new contracts only or if suppliers are likely to amend existing contracts.

If suppliers make amendments to existing fixed term contracts, either unilaterally or by mutual variation, they will need to do so in line with SLC 23 and 23A. The licence in particular requires that consumers should be informed about unilateral contract variations that are disadvantageous. We consider that these changes cannot be assumed to be advantageous over the period of the fixed deal, due to the lack of price protections in the current proposals. Therefore consumers should be informed of the unilateral contract change, and given the opportunity to switch away.

If existing contracts are likely to be amended the proposed timeline for the decision would mean consumers begin rolling onto these default tariffs late this year or early in 2017. If this approach is expected we would recommend Ofgem consider a longer period between the decision and implementation, to enable advice providers and other consumer bodies to ensure that the information they provide will be accurate and relevant for customers on non-SVT default contracts.

If you would like to discuss the content of this consultation response further please let me know.

Yours sincerely,

Alexander Belsham-Harris

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