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**29 November 2017**

Dear Barry,

**Statutory consultation on estimated annual costs for domestic consumers**

This submission was prepared by Citizens Advice. Citizens Advice has statutory responsibilities to represent the interests of energy consumers in Great Britain. This document is entirely non-confidential and may be published on your website. If you would like to discuss any matter raised in more detail please do not hesitate to get in contact.

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**Question 1: Do you agree with the changes we propose to make to the Estimated Annual Cost requirements?**

Informed choices are essential for consumers to make good decisions in the market, and consumers having accurate estimates of costs are an important component of this. Given the complexity of energy pricing, consumers generally rely on estimates of total cost, rather than the actual tariff price, when choosing a tariff.

Ofgem's recent consumer engagement survey found that financial risks - either costs going up or not saving as much as expected - are the main risks that consumers perceive with switching.<sup>1</sup> It is vital that consumers receive accurate Estimated Annual Costs (EACs), in order to have the confidence to switch. The EAC also allows consumers to plan for their energy costs, and is used as the basis for important prompts to engage, such as the cheapest tariff message.

We recognise that recent changes to tariff rules, and the emergence of innovative tariffs, mean there is a need to change the current EAC methodology. However, the removal of a single, prescribed methodology carries a number of risks. As set out in the consultation, there was some poor practice in this area by suppliers, price comparison websites (PCWs) and others prior to the introduction of the current

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<sup>1</sup> <https://www.ofgem.gov.uk/publications-and-updates/consumer-engagement-survey-2017>

prescriptive rules. We would not want to see a return to consumers receiving poor quality/misleading quotes as a result of these changes.

We agree that Ofgem's proposed narrow principles will mitigate these risks. In particular, the requirement for estimates to be based on actual consumption data (including their half hourly usage where necessary) should protect consumers from suppliers making assumptions about how they may behave on the new tariff. We set out further views on this in response to question 2.

We also support removing the requirement for estimates to be forward-looking. This approach can be confusing to some consumers, and result in misunderstandings about the savings that can materialise in some circumstances. This is also a pragmatic change, given the changing rules on default tariffs.

The proposed changes will mean that EACs vary according to supplier or PCW, despite the tariff and consumption data being the same. This could increase confusion for consumers. We set out our view on this risk in response to question 3.

While we consider that a mixed methodology - with a prescribed methodology for simple tariffs, and narrow principles for all other tariffs - could have been practicable, we agree that narrow principles are likely to be a more enduring regulatory framework. However, we don't see any cause for methodologies for traditional, single unit rate tariffs to diverge considerably, given their simplicity, and would be concerned if this transpires. Ofgem should monitor the variability of EACs following these changes, and take action if alternative sources are substantially different.

**Question 2: Do you agree that we should require that the Estimated Annual Cost is always based, as a default, on actual historic consumption where this is available? Please provide supporting reasons for your answer.**

Yes. Using actual, historic consumption data will generally enable a more accurate estimate of the upcoming year's costs, rather than using information on characteristics such as property type and number of occupants to determine probable consumption. The rollout of DCC-enrolled smart meters and the midata programme mean that historic consumption data will be more easily available to consumers when using PCWs and other comparison services. As such, there should be fewer instances where consumers rely on estimates based only on their characteristics.

Where historic data is not available, we agree that suppliers and PCWs should be able to provide estimates based on reasonable assumptions of actual consumption.

We would consider that 'actual consumption' means current, rather than expected future consumption, and therefore should not assume any particular behaviour change. For example, where a consumer is considering a time of use tariff, we would expect assumptions of behaviour change in response to the tariff to be included in a supplementary estimate, rather than the primary EAC.

Similarly, we support the exclusion of contingent discounts and bundled charges, which also require the consumer to take particular actions in future. The potential value of contingent discounts can also be communicated in supplementary cost estimates.

Where there has been a significant change in circumstances - such as a member of the household becoming unemployed, or major improvements to energy efficiency in the home - historic consumption data may not provide an accurate EAC. We support the proposal to allow suppliers to not use historical data in exceptional circumstances. The consultation does not set out what 'exceptional circumstances' may or not include. Ofgem should provide more detailed thoughts in its decision document.

**Question 3: Do you agree that we should aim to deliver within-channel consistency of results rather than full cross-market consistency? Please provide supporting reasons for your answer.**

We recognise that without a single prescribed methodology it is not practicable to achieve full cross-market consistency. Given this, we agree that it is preferable to achieve 'vertical consistency' within channels, rather than 'horizontal consistency' between channels.

This aligns with the existing informed choices principles, which require suppliers to provide information, tools and services that enable consumers to easily compare and select a tariff. Allowing suppliers or PCWs to vary their EAC methodology for different tariffs would make comparisons misleading and more difficult for consumers to understand.

However, the loss of horizontal consistency will introduce some new confusion for consumers. Consumers are encouraged to use multiple PCWs in order to get the best deal<sup>2</sup>, and Ofgem's consumer engagement survey found that around 60% of PCW users had used two or more sites in their search. If estimated costs for the same tariff vary widely between sites, consumers may not understand that the

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<sup>2</sup><https://www.gov.uk/government/publications/digital-comparison-tools-summary-of-final-report/digital-comparison-tools-summary-of-final-report>

underlying unit price of the product is in fact the same. Even if consumers do not use multiple PCWs they may be presented with a different EAC if they have to complete the switch with the suppliers, or may be given a different EAC when they receive welcome documents from their supplier.

There may also be a risk that PCWs intentionally design methodologies which overstate likely savings. Furthermore, given their commercial relationships with suppliers, PCWs may use methodologies which favour those suppliers who pay them higher rates of commission. We have previously identified the risks of commercial relationships affecting search results.<sup>3</sup> We note that the CMA has recently opened an investigation into hotel booking sites, including how commission payments affect the rankings of search results.<sup>4</sup>

The CMA has recognised these issues, and set out its view that they could lead to consumer trust in the market being undermined.<sup>5</sup> It is our view that there are two key mitigations to these issues:

- Transparency - it should be clear to customers how their results have been calculated by PCWs. Consumer protection regulations also place requirements on businesses to disclose commercial relationships, where that information is material to the consumer's decision.<sup>6</sup> The CMA's recent report on Digital Comparison Tools reiterated that PCWs must clear about how they make money and rank search results.<sup>7</sup> We therefore support Ofgem's proposals to require PCWs and suppliers to have clear messaging about the EAC methodology, including any assumptions. This complements existing Confidence Code requirements for prominent commission arrangements messaging.<sup>8</sup> We would also expect suppliers to have clear and timely messaging as to why the EAC they provide differs to that shown on a PCW, following a switch completed on one of these sites. This will enable consumers to use their cooling off rights if they feel the suppliers EAC is not acceptable.

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<sup>3</sup><https://www.citizensadvice.org.uk/about-us/policy/policy-research-topics/consumer-policy-research/consumer-policy-research/price-comparison-websites/> - see research report 'The Real Deal'

<sup>4</sup><https://www.gov.uk/government/news/cma-launches-consumer-law-investigation-into-hotel-booking-sites>

<sup>5</sup><https://assets.publishing.service.gov.uk/media/57f370fbe5274a0eba000025/cma-response-to-ofgem-confidence-code-review-consultation.pdf>, see paras 42-54.

<sup>6</sup> OFT (2012). Price Comparison Websites. Trust, Choice and Consumer Empowerment in Online Markets, p.15.

<sup>7</sup><https://www.gov.uk/government/publications/digital-comparison-tools-summary-of-final-report/digital-comparison-tools-summary-of-final-report>

<sup>8</sup>Confidence Code Requirement 1, sections G-J

- Monitoring - Ofgem should actively monitor the impact of these changes, and the range of methodologies employed by suppliers and PCWs. We do not see a reason why methodologies should diverge significantly for simple tariffs. Ofgem should monitor both the methodologies which are used, and compliance with transparency requirements. We will also monitor contacts to our service for evidence that consumers are being intentionally misled or confused following the changes.

White label arrangements are not mentioned in the consultation, but we would consider that suppliers should use a single methodology across all brands. Ofgem should make clear in its decision document how it expects suppliers with white label arrangements to implement these changes.

### **Issues not addressed in the consultation**

Ofgem is currently running a series of engagement trials in preparation to deliver the CMA disengaged customer database. The original design of this remedy would allow multiple suppliers to send personalised communications to disengaged consumers. These letters will need to be clear that the EACs in these separate letters may not be directly comparable, and that a single channel, such as a PCW, may provide a fairer comparison.

Ofgem has also trialled a Cheapest Market Offer Letter (CMOL), which lists the best deals in the market in a single communication, with both Ofgem and supplier letters tested.<sup>9</sup> If this approach is taken forward in future then Ofgem may be required to select an appropriate EAC methodology. A supplier branded letter approach would require Ofgem to ensure that the EAC methodology used by the relevant supplier fairly represented the cost of other supplier tariff offerings.

Citizens Advice runs a non-transactional PCW, which has been designated as a backstop whole of market comparison site by the CMA. We will work with the service provider of our site to select an appropriate methodology for calculating EACs.

Both Citizens Advice and Ofgem will need to consider these issues carefully, as the EAC methodology selected could impact the choices that consumers make, and have commercial implications for energy suppliers.

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<sup>9</sup><https://www.ofgem.gov.uk/publications-and-updates/results-cheaper-market-offers-letter-trial>

If you would like to discuss any aspect of this response further please let me know.

Yours Sincerely,

Alex Belsham-Harris

Senior Policy Researcher