Dear Lesley,

Re: Consultation on the Third Price Control for Phoenix Supply Ltd (PSL)

The Consumer Council is a Non-Departmental Public Body set up in legislation to safeguard the interests of all consumers, and particularly the vulnerable and disadvantaged. The Consumer Council is an independent organisation which operates to promote and protect the consumer interest.

We welcome the opportunity to respond to this consultation on the Third Price Control for Phoenix Supply Ltd (PSL).

The Third Price Control for PSL is very significant for the future of the gas market in the Greater Belfast and Larne area. With rising levels of fuel poverty in Northern Ireland, it is increasingly important that consumers know that they are getting a fair deal for the energy they purchase, and that they receive the best possible levels of service. This includes ensuring that bills are correct, meter reading occurs in a timely manner and debt management procedures are put in place.

The competitive landscape has changed since the last Price Control was determined. Firmus have entered the domestic customer market, and although customer switching has yet to take place in significant numbers there is a possibility that with the recent PSL price increase this could change. It is
therefore very important that this Price Control provides the gas consumer that chooses to remain on the regulated tariff with the price protection they require.

The consultation refers to ‘effective’ competition. The Consumer Council’s believes that in order for gas competition in Greater Belfast and Larne to be effective it must improve the customer experience for all consumers, and it will only do this by:

- Providing lower prices to the consumer;
- Providing better customer service;
- Being available to all types of consumers, and;
- Providing increased and targeted protection to vulnerable consumers;

At present, the Consumer Council believes that there is no comprehensive evidence to suggest that competition will deliver consumers all these benefits. As this consultation document states, “Competition in the GB market has brought increased profit margins, a confusing array of tariffs to make comparison difficult and little variation between standard tariffs”. It is therefore the Council’s view that competition should not be pursued at any cost. The Consumer Council therefore welcomes the Utility Regulators announcement that it will undertake a project that will consider the future regulatory approach to the retail market and looks forward to working with the Regulator on this.

### Consultation questions

1. **What are respondent’s views on the scope of this control?**

   The Consumer Council would strongly agree that it is too early in the development of competition in the Greater Belfast area to consider removing the price control mechanism from customers using less than 25,000 therms.

   However, we urge the Regulator to monitor this market closely, and set out its vision for a competitive natural gas market in Northern Ireland with a roadmap clearly setting out the milestones on how this will be achieved.

   The Consumer Council recognise that if a large number of consumers decide to switch, possibly as result of the recent Phoenix Supply price increase and/or if a new competitor enters the market, it may be necessary to alter the scope of the price control.

   Furthermore, we believe that it is prudent to wait until the review of competition in the market for customers using more than 25,000 therms is complete to consider whether a price control is required in this sector.

2. **What do respondents consider to be an appropriate timeframe for this price control?**

   The market for domestic and SME gas customers in Greater Belfast is at the early stages of competition. It is too early to say how effective competition in
this consumer segment will be. The timeframe for the price control must reflect the competitive conditions, whilst providing certainty to PSL and consumers. A five year period provides a reasonable period of regulatory certainty, but the Price Control must be capable of adapting to meet new market conditions. It would seem prudent to have in place a mechanism to review the price control annually to see if it is continuing to act in the interests of consumers. It would not be in the interests of consumers if in 18 months time the price control was seen to be a barrier to the entry of new competitors.

3. What are the respondents’ views on the trigger mechanism?

The Consumer Council agree that the figure of five per cent for the trigger to a tariff review is reasonable. We also agree that this figure should work both to increase and decrease the tariff. Whilst the price control remains the Regulator should also retain the flexibility to initiate a review at any time.

4. What are respondent’s views on the tariff structure?

The Consumer Council welcome the initiative shown by the Regulator to ensure that the tariff structure is cost effective and that no class of customer is paying above the maximum average.

Until the hopeful advent of Social Tariffs, it is the Consumer Council’s view that all regulated gas customers should pay the same price irrespective of the amount of gas they use and that there should be no standing charge. PSL gas customers who are in fuel poverty can be best helped by having lower tariffs and other social benefits such as free energy efficiency measures specifically targeted at them.

5. What are respondents’ views on k factor?

The Consumer Council recognise that the k-factor is incompatible with a fully competitive retail energy market. It distorts a competitive market and reduces the purchasing risk for the incumbent, relative to that of other suppliers.

However, the k-factor, if operated in a closely regulated manner can provide some level of protection to the consumer. The stability it provides for the incumbent supplier allows for a relatively low margin to be set. In addition it provides an element of risk-smoothing for consumers, and is compatible with annual tariff setting. This will involve the Utility Regulator, in partnership with PSL actively monitoring the k-factor to ensure that it does not grow to unwieldy levels.

As competition matures those customers that switch supplier will no longer be paying for an under recovery or receiving the benefit of an over recovery despite having made payments that created it. To some extent this is inevitable in a competitive environment. However, minimising the k-factor that is carried into the next tariff period will help allocate costs and benefits fairly between consumers. Therefore the Consumer Council believe the Utility
Regulator must review the size of the k-factor on a regular basis and take action if and when required to keep it to a minimum.

6. What are respondent’s views on bad debt?

The Consumer Council agree that the methods available to PSL to control customer debt do mean that it has a low risk in this area. The consultation states that PSL was given time in the current Price Control to review its policies on reducing customer debt. The Regulator also gave PSL an amount in the 2009-11 Price Control to improve their bad debt processes. To our knowledge PSL have made no improvement in their customer debt processes and we would like to see a report from the Regulator on how PSL have performed in this area.

Increased meter reading will reduce bad debt by improving the accuracy of billing. Despite committing to increase the number of meter reads for Direct Debit customers PSL have failed to do so. This commitment could have been funded from the amount given to PSL in the current Price Control. Therefore, it should not now require additional funding in the new Price Control.

The new Price Control must explicitly insist that PSL increase the number of meter reads for Direct Debit customers, and actively monitor and identify consumers who are struggling with their bills to proactively provide budgeting support to consumers in difficulty.

7. What are respondent’s views on efficiency factor?

It is important that the Price Control is used to provide an incentive to PSL to increase the efficiency of the business and reduce the price to the end user.

The end price consumers pay for gas is dependent upon, among other things, the efficiency which PSL exercises when purchasing gas. Currently the Regulator is not prescriptive and only monitors the strategy which PSL uses to purchase gas. While the Consumer Council appreciate PSL seek independent advice when devising their strategy, we believe that it is in the interests of consumers for PSL to be given an incentive to purchase efficiently and for them to incur penalties if they fail to purchase economically.

Incentives can keep costs down, and that is for the benefit of supply companies and consumers. To draw a parallel in the Northern Ireland context, NIE Energy has a licence requirement to purchase electricity economically, (the Economic Purchasing Obligation). Urgent consideration should be given to creating a mechanism that can be enforced against PSL if need be.

Research commissioned by the Utility Regulator and undertaken in 2010, showed that gas suppliers scored less well than the electricity supplier over a range of customer contact indicators, for customers with debt problems\(^1\). We

believe that the Price Control should include incentives and penalties covering the performance of PSL in its customer service role.

The Energy Act 2011 has introduced standards of performance that includes compensating customers when standards are not reached. The Consumer Council believe that any such payments must come from the profits of the gas suppliers or they will fail to provide an incentive for PSL to improve its performance.

8. **What are respondent’s views on supply margin?**

We agree that the pass though of costs to consumers means that PSL should be able to recover all their costs from consumers and therefore the risk to PSL is assessed by the Regulator as low.

The margin of 1.5 per cent that was determined for the current Price Control included the impact of competition and the risk of working capital. However until regulation and the pass through mechanism is removed, the risk in fact lies with the consumer. If the customer base decreases because of switching to a competitor or the cost of working capital increases, it is the customer that will pay for this. The supply margin should ultimately reflect the risk to the supplier of providing a regulated tariff, in which the costs are passed through to the consumer. We therefore see no reason to increase the margin from its current 1.5 per cent.

Furthermore, it follows that if the total costs increase the final overall cash figure derived from the 1.5 per cent margin will also increase. The Consumer Council believes that steps must also be taken to reduce the overall costs involved as currently there is an incentive to increase costs.

**Corporate Social Responsibility**

We appreciate that the issue of Corporate Social Responsibility (CSR) was not consulted on as part of the PSL Price Control. However, this is an area which we believe is important for consumers and should be given urgent consideration.

It is the position of the Consumer Council that Energy Companies that make a profit from generating, distributing and selling fuel and power have a corporate social responsibility to their customers to provide support and care schemes to households that are struggling to heat their homes to adequate levels.

It is often argued that the main domestic energy suppliers are tightly regulated and financially have no leeway to invest or develop social tariffs for those in fuel poverty. The Consumer Council believe that there is a real opportunity to examine the whole supply chain within the energy market as a whole, which would include suppliers, importers, generators and transmission and distribution companies.
EU Third Internal Energy Package (IME3)

The provisions of the IME3 contain a range of measures that will increase consumer protection. The Consumer Council welcome these enhanced measures. It is important in preparing the new Price Control that consideration be given now to the resources that may be required by PSL to implement these measures. It is important to identify and take account of these measures as early as possible so that costs are not required unnecessarily and to ensure the maximum benefit to the consumer.

Conclusion

The Consumer Council believes that we need to ensure that regulation works in consumers’ best interests in both the long and short term, and with growing levels of fuel poverty provides adequate protection for the most vulnerable consumers in our society.

Therefore we believe this process should be conducted in a manner that will focus on the final consumers needs and ensure that the pass through risks that the consumer faces are accurately reflected in energy companies margins, purchasing decisions, and levels of service provided.

Yours Sincerely,

Richard Williams
Senior Consumer affairs Officer