

# COMPETITION AND MARKETS AUTHORITY ENERGY MARKET INVESTIGATION



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**Response to Addendum to provisional findings**

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**13 January 2016**

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Redactions are indicated by [X] and reflect items omitted due to reasons of commercial confidentiality or due to the terms of our licensing agreements with third parties

## 1. Introduction and summary

- 1.1 This submission is made by EDF Energy plc ("EDF Energy") on behalf of EDF Group Companies. EDF Energy welcomes the opportunity to respond to the Competition and Markets Authority's ("CMA") Addendum to the provisional findings, published on 16 December 2015 ("Addendum"). This response should be read in conjunction with EDF Energy's response to the CMA's Second supplemental notice of possible remedies ("Second Supplemental Remedies Notice").
- 1.2 EDF Energy regards prepayment meter ("PPM") customers as an important and valued segment of our customer base. We currently serve approximately 760,000 PPM customer accounts [X]. This is equivalent to about 14% of our customer accounts and represents a wide demographic base. Many of our PPM customers value the ability to prepay as it provides them with both a sense of control and peace of mind, allowing them to budget effectively for their energy use and help avoid 'bill shock'.
- 1.3 EDF Energy is committed to working with the CMA to improve trust and consumer outcomes in the market, and welcomes this opportunity to consider how the market can be improved for PPM customers.
- 1.4 As noted in our response to the CMA's Notice of possible remedies ("Remedies Notice"), EDF Energy believes that the key feature negatively affecting consumer outcomes in the retail energy market is weak engagement. We have considered whether the Addendum illustrates issues for PPM customers separate from weak engagement. Our view is that large parts of the Addendum raise issues that are *complementary* to the issue of weak engagement, a factor important for considering the remedies package.
- 1.5 While we would not analyse all the issues in the same way as the CMA has, we believe that there is a feature, or combination of features, giving rise to an adverse effect on competition ("AEC") due to the technical constraints that currently exist with the PPM infrastructure that limit the ability of suppliers to make a wide range of offers to PPM customers. When weak customer engagement in switching and searching already exists, additional barriers or disincentives to switch, or otherwise engage, are problematic. The technical constraints that currently exist also impact on the ability of smaller suppliers to expand as investment in a new meter is at present more likely to be necessary if an innovative tariff is to be offered by such rivals.
- 1.6 These issues are likely to be addressed by the roll-out of the second generation of smart meters ("SMETS 2") from around late 2016 - *but not*, the CMA should note, *by the first generation smart meters ("SMETS 1")* as there is no clear timetable as to when these would be adopted by the Data Communications Company ("DCC"). Until these meters are adopted by the DCC they are likely to lose functionality on change of supplier, creating a barrier to switching. This is a critical factor for the CMA to be aware of.
- 1.7 We also agree that the failure by certain suppliers to adopt the Debt Assignment Protocol ("DAP") Point of Acquisition ("POA") model, is problematic in that a number of switch refusals under DAP may be unjustified. While the numbers switching are greater than identified by the CMA, in a market characterised by weak customer engagement, a mechanism that allows one or more suppliers to prevent switches without justification is problematic.
- 1.8 We welcome the fact that the CMA has not framed the AEC in the domestic prepayment sector ("PPS") in terms of suppliers exercising "unilateral market power" over an inactive customer base. As stated above, we consider that the issues that the CMA has identified in the Addendum relate closely to the broader issue of weak customer engagement.

1.9 Our summary views in relation to the CMA's provisional findings regarding the domestic PPS and PPM customers are contained in the following table:

<b>Relevant views / Features identified by CMA as giving rise to an adverse effect on competition ("AEC")</b>	<b>EDF Energy's initial response</b>
<p>A combination of features of the markets for domestic retail supply of gas and electricity in Great Britain, relating specifically to the PPS, give rise to an AEC. (Addendum, paragraph 77)</p>	<p>We agree that an AEC arises due to features specific to the PPS.</p> <p>Weak customer engagement remains the material feature giving rise to concern with respect to many PPM customers in the same way as it is for certain standard variable tariffs ("SVTs") customers. Customers on a PPM have historically not had many options outside of SVTs, and so may exhibit a different level of engagement to cash/cheque and direct debit ("DD") customers on SVTs (more particularly the latter). Having said that, EDF Energy notes that [3&lt;] % of its PPM customers are not in debt and so should be able to access the credit sector and corresponding tariffs if they so wish. While PPM customers may be more aware of their energy purchasing than non-PPM customers (due to the need to top up their key or check how much money is left on the meter), EDF Energy considers that the key AEC affecting these customers (as in the broader retail segment) is weak engagement.</p> <p>While not agreeing fully with the way the CMA has analysed all issues, we agree with the CMA's provisional finding that there are a number of features that may lead to <i>some</i> PPM customers (but not all) facing particular obstacles to market access that are beyond their effective control. This is especially important given that weak customer engagement already exists, and so additional barriers to switching are likely to be more problematic as a result. In particular:</p> <ul style="list-style-type: none"> <li>- To the extent that PPM customers with debt under £500 are facing obstacles to switching (whether to credit or other suppliers), there is an AEC. This results largely from the inconsistent way that suppliers currently apply the DAP procedure. Many suppliers have already taken the requisite steps to address this but others have not done so. We believe that this can be remedied by mandating adoption of POA for all suppliers. Industry has already started to make changes to allow this to happen (by adding the DAP to the Master Registration Agreement ("MRA")) and it is essential that this is completed. The CMA should support this change and ensure that this is passed and successfully implemented at the earliest opportunity.</li> <li>- To the extent that PPM customers carry debt over £500 and so are not eligible to switch to credit or would (justifiably) face additional procedural complexities changing supplier, it is questionable whether there is an AEC. In EDF Energy's view, such customers present significantly higher costs and risks and the tariffs in the PPS reflect these additional costs. We consider</li> </ul>

	<p>in more detail below the CMA's analysis of the cost-to-serve differential between the PPS and credit segment.</p>
<p>These features, in combination, reduce retail suppliers' incentives (and, for some, their ability) to compete to acquire PPM customers (in particular, customers with an outstanding debt or a poor credit history) and to innovate by offering tariff structures that meet customers' demand. (Addendum, paragraphs 78-79)</p>	<p>We do not analyse the issue of suppliers' incentives in the same way as the CMA. For example, we have a clear ambition to grow our customer base and provide competitive tariffs both to attract and retain customers across all segments, including the PPS, as evidenced by our fixed-term and fixed-price Blue+ Prepay tariff (first launched in July 2014) that comes with no exit fee.</p> <p>In respect of indebted customers specifically, EDF Energy does not differentiate between indebted and non-indebted PPM consumers when seeking to attract new customers.</p> <p>However, we do agree that technical constraints may impact on our ability to innovate and smaller suppliers' ability to compete, raising their cost to do so and hence lessening their incentives.</p>
<p>As a result, the tariffs available in the PPS are not competitively priced compared with the DD segment. (Addendum, paragraph 6)</p>	<p>EDF Energy agrees that tariffs in the PPS are on average currently higher than in the credit sector. We also agree that there are higher costs-to-serve PPM customers on average.</p> <p>The CMA's analysis of the issue relies on a number of assumptions that should be considered further and made more robust. EDF Energy also suggests that some of the language used be revisited as, for example, the definition of "competitive acquisition tariffs" does not match our day-to-day experience in the market and may easily confuse. We disagree that competitive tariffs do not exist in the PPS.</p>
<p>Those features are:</p>	
<p>Technical constraints that limit the ability of all suppliers, and in particular new entrants, to innovate by offering tariff structures that meet demand from PPM customers who do not have a smart meter. (Addendum, paragraphs 31 <i>et seq.</i>)</p>	<p>EDF Energy agrees that there are technical constraints relating to the current PPM infrastructure that limit the ability of most suppliers, but particularly smaller suppliers, to innovate by way of PPM tariffs.</p> <p>If EDF Energy were to offer a prepayment variant for all of its short-term fixed tariffs, then we would run out of tariff slots very quickly due to the technical constraints of the system. Slots would only become available as fixed-rate tariffs ended (with an approximate six month lag before each slot became available again to allow customers time to switch tariff). As recently highlighted to the CMA, if EDF Energy had offered a PPM version of each of our short-term fixed tariffs in 2014, we would have run out of slots by [X] 2014 and [X].</p> <p>These technical constraints have limited the tariffs that we have been able to offer PPM customers and also applies to many other suppliers (it appears Centrica is an exception).</p> <p>SMETS 1 meters are not themselves a solution to this problem, as these are not fully interoperable among suppliers unless and until adopted by the DCC, the timing of which is uncertain. Some PPM SMETS 1 customers are likely to lose smart services on change of supply (as the systems supporting these meters are bespoke to individual suppliers and not compatible with other</p>

	<p>suppliers' systems). There is a risk that some customers may in effect therefore be 'locked in' and thus potential switching levels could be reduced.</p> <p>Roll-out of SMETS 2 should alleviate these constraints. As detailed in our response to the Second supplemental remedies notice, SMETS 2 meters are likely to be available from Q4 2016 (DCC adoption), although high volume deliveries to support mass deployment is unlikely to be any earlier than Q1 2017.</p>
Softened incentives for all suppliers, and in particular new entrants, to compete to acquire PPM customers due to: (Addendum, paragraph 40 <i>et seq.</i> )	<p>It has not been EDF Energy's experience that our <i>incentives</i> to compete for PPM customers are softened although our <i>ability</i> to do so may be constrained. We have approximately 14% of our customer accounts on PPMs and we are always seeking to acquire new customers across all segments as outlined above. Our customer acquisition in the PPS is likely to have benefited from the fact that we have had the lowest SVT among the major suppliers for long periods of time but with the increasing number of fixed-rate PPM tariffs on the market, we are continuously monitoring our position to ensure that we also remain competitive in this area.</p> <p>Competition in the PPS is increasing and this has partly been driven by the proliferation of SMETS 1 meters. While we do not believe that expediting SMETS 1 roll-out is a cost-effective or proportionate solution across the market, it does give confidence that the roll-out of fully interoperable <i>second</i> generation (SMETS 2) smart meters will further increase competition.</p>
i) actual and perceived higher costs to engage with, and acquire, PPM customers compared with other customers; and	<p>It is the case that there are higher costs to serve PPM customers.</p> <p>Acquisition costs on a channel by channel basis are the same for PPM as for credit sector customers (e.g. suppliers pay the same commission to a price comparison website in respect of each) but PPM customers are generally harder to access and less responsive to approaches by suppliers and so cost more to acquire per account.</p>
ii) a low prospect of successfully completing the switch of indebted customers, who represent about 15% of PPM customers.	<p>We agree that there are problems with implementation of the DAP. In response to this, EDF Energy and nine other suppliers (from April 2015) have proactively taken steps to change their operation of the DAP (and were joined by an additional supplier in July 2015). The changes under the POA approach aim to make it easier and simpler for PPM customers who are repaying a debt of £500 or less per fuel to switch. However, the POA remains a voluntary commitment that has not been adopted by all suppliers (including a significant number of smaller parties) which has limited the effectiveness of the changes. We believe that all suppliers should be required to adopt this new process so that all customers benefit from the improved outcomes.</p>
Reduced innovation as a result of the simpler choices component of the Retail Market Review ("RMR"). (Addendum, paragraph 69 <i>et seq.</i> )	<p>We agree that regulation has been a contributing factor to limited tariff choice in the PPS (as across the retail segment generally).</p> <p>EDF Energy originally supported Ofgem's 'four-tariff rule' and the</p>

	<p>move to all tariffs consisting of a standing charge and unit rate. This is because we recognised that customers were finding both the number and structure of tariffs to be confusing, and this was inhibiting engagement. However, the evidence is that this is not the best way to encourage innovation and simplicity for customers going forward. We therefore support the removal of the 'simpler choices' component of the RMR rules in a sensible manner that retains customer protections. This will allow greater commercial flexibility and promote competition between suppliers to develop more innovative tariffs that are better suited to customers' needs, including those with PPMs.</p> <p>While we agree with the CMA that the simpler choices component of the RMR has played a role in discouraging suppliers from designing more PPM-specific tariffs, it is our view that the main issue has been the technical constraints described above.</p>
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## 2. Context for considering prepayment meter issues

2.1 In considering the potential features giving rise to an AEC with respect to PPM customers, we find it helpful to consider relevant issues against the following background:

- (a) Our data suggests that switching levels among PPM customers are comparable to credit sector cash and cheque customers (but slightly lower than direct debit ("DD") customers).<sup>1</sup> To the extent that customers in the PPS are disengaged, this will likely have been exacerbated by the historically more limited tariff availability.
- (b) A profiling of customers in this segment suggests that there is a subset of customers for whom the relevant feature or features gives rise to an AEC and where specific and tailored remedies are needed.
- (c) We would encourage the CMA to undertake analysis to try and identify and understand this potential subset of customers further. Our research indicates that PPM customers are not a homogenous group. For example, there appear to be five clear segments emerging based around property tenure, income and refused credit flag; see Table 1. In addition, the debt levels of indebted PPM customers also vary (using the £500 DAP limit as the threshold); see Table 2.

**Table 1: Segmentation of EDF Energy prepayment meter customers**

[redacted]

**Table 2: Breakdown of EDF Energy prepayment meter customers in debt (2015)**

[redacted]

- (d) Crucially, [redacted]% of EDF Energy's PPM customers are not in debt and so should be able to switch to the credit sector and access the full range of tariffs available in the market if they so wish. The key AEC in respect of these customers is likely to be weak engagement. PPM customers with debts under £500 should be in a similar position (due

<sup>1</sup> [redacted].

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to the DAP POA), but we agree that some customers do sometimes continue to face obstacles to switching (e.g. imposition of upfront costs for changing meters) and we consider these separately below.

- (e) As noted above, many PPM customers value the ability to prepay as it provides them with both a sense of control and peace of mind, allowing them to budget effectively for their energy use and help avoid 'bill shock'. The CMA recognises this (Addendum, paragraph 22) but has not identified the proportion of such customers.
- (f) The PPS is evolving. Recent years have seen a proliferation of new tariff offerings and the imminent roll-out of SMETS 2 is expected to open up more tariff opportunities to customers in this segment, as well as facilitating their move to credit payment arrangements, for those desiring this.
- (g) The move to SMETS 2 presents some challenges that will affect some PPM customers. For example, we note that a higher proportion of PPM customers live in flats, and those living in particular housing types (such as high rise buildings) will present higher costs in terms of infrastructure upgrades - even if suppliers and their customers ultimately absorb these costs. There is also a potential issue for the cost of supporting the old infrastructure for PPM customers when a significant roll-out of smart meters has occurred. Prima facie, the common infrastructure costs need to be recovered when there are far fewer customers to recover this from. EDF Energy is committed to ensuring that these customers are treated fairly as part of the general upgrade and that those customers who are slowest to switch are not left paying higher tariffs as a result of incremental increases in the costs to serve these customers (as the old prepayment infrastructure becomes obsolete). To achieve this, the CMA should consider how such costs can be fairly borne by the entire industry so that this does not negatively impact on an ever decreasing number of such customers.
- (h) The CMA will also be aware that Ofgem has recently completed a consultation on matters relevant to this segment, including supplier objections and the use of security deposits. In addition, we note that Ofgem is currently consulting on proposals to improve outcomes for prepayment customers. A decision on these points is expected later this year.

### **3. Incentives to compete for prepayment meter customers**

3.1 EDF Energy considers that both it and its rivals (i.e. both the Six Large Energy Firms ("SLEFs") and new entrants) are incentivised to compete to retain and acquire PPM customers but recognises that the ability to do so is impacted by the technical constraints that exist with respect to PPM customers. The CMA's analysis in part reflects this. For example:

- (a) EDF Energy has around 14% of its customer accounts on PPMs. This is a substantial part of our total number of customer accounts. Only a small proportion of our PPM customers are in debt (<10%) and, as discussed in Section 5, we have only objected to switches for customers with debt lower than £500 in very few cases (where exceptional circumstances exist).
- (b) EDF Energy offers a PPM-only, fixed-price, fixed-term tariff (Addendum, paragraph 14). The launch of our Blue+ Fixed Prepay October 2016 tariff in July 2014 helped provide both new and existing PPM customers with more choice and access to a long-term fixed tariff, as well as the flexibility to leave for free at any point. Our research had indicated that the need for a fixed tariff was not immediately apparent to PPM customers because many failed to connect rising prices with the amounts they were topping-up. However,

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once explained, PPM customers valued the benefits in terms of budgeting and peace of mind. Since the launch of our Blue+ Fixed Prepay tariff, approximately [3<] % of our PPM acquisitions have chosen the fixed-rate tariff over the standard variable variant.<sup>2</sup>

- (c) Small and mid-tier suppliers have increased their market share in the PPS, and those focusing on the PPS have been able to make a significant impact. Over 99% of the customer accounts of Utilita and Economy Energy are on PPMs. Our analysis<sup>3</sup> suggests that the non-Six Large Energy Firms had a total PPM market share of approximately [3<] % at the end of 2014, up from just [3<] % in 2012.
  - (d) EDF Energy has itself not historically differentiated between indebted and non-indebted customers within its acquisition strategy. However, the discount on debt for an acquired customer, which the CMA describes as an incentive for incumbent suppliers to retain customers, could also act as an incentive to acquire.
  - (e) As noted by the CMA, other suppliers have responded to increased competitive pressures by also introducing fixed-term tariffs in the PPS.
- 3.2 EDF Energy does recognise that conversion rates (i.e. the average success rate at which a supplier persuades a customer to switch) may be lower in this segment but this has not deterred our own interest in acquiring PPM customers. We do, however, agree with the CMA that there are practical constraints that impact on the ability to target and obtain PPM customers as detailed below.

#### 4. Tariff choices available to prepayment meter customers among the Six Large Energy Firms

- 4.1 The CMA, at paragraph 15 of the Addendum states: "*We consider that none of the tariffs set out in paragraph 14 are competitively priced acquisition tariffs (compared with the DD segment).*" We do not agree with this assertion and suggest the language used can be improved because competitive tariffs in the PPS *do* exist. The CMA's provisional finding that tariffs in the PPS are not "competitive" is premised on the assumption that a competitive tariff in the PPS would consist of the cheapest DD tariff in the credit meter sector plus an average cost-to-serve differential. As discussed further below, we note that the CMA has yet to form its own view on what this differential should be.
- 4.2 The definition used by the CMA is essentially that a competitively priced acquisition tariff is one that is the lowest price in the market. In a well-functioning market, we do not agree that the appropriate benchmark would be the absolute lowest priced DD acquisition tariff plus cost-to-serve differential (Addendum, paragraphs 12(b), 13 and 26). Further, the appropriate measure (or definition) for determining whether or not a tariff is a "*competitively priced acquisition tariff*" must be whether it has been successful in attracting customers from other tariffs and hence forms a competitive constraint. The movement of customers between suppliers, coupled with changes in PPS market share, indicate that there are competitive tariffs in the PPS.
- 4.3 For example, we acquire new PPM customers on both our SVT prepayment and Blue+ Fixed Prepay tariffs. In setting the level of the tariff, we consider the full range of PPM tariffs offered in the market.

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<sup>2</sup> [3<].

<sup>3</sup> EDF Energy estimate based on Cornwall Energy and Ofgem data.

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- 4.4 More broadly, the CMA states at paragraph 3 that non-SLEFs (particularly Utilita) have a market share of approximately 6% in the PPS and that this is increasing.<sup>4</sup>
- 4.5 The CMA's provisional finding is that the 3% PPM to credit switching rate in 2014<sup>5</sup> is in itself evidence that tariffs in the PPS are not competitively constrained by those in the credit sector but we note that there is no analysis as to whether 3% is sub-optimal from a consumer perspective. In addition, EDF Energy currently finds it difficult to differentiate the impact of customer disengagement from other factors. It may be that the profile of customers on PPMs means that customer disengagement is higher than in the wider retail market because their characteristics more closely match those customers identified by the CMA in its main Provisional findings report (Provisional findings, paragraph 118).
- 4.6 We note that the CMA has made a working assumption that the incremental cost-to-serve for customers in the PPS is £80 (Addendum, paragraph 11). In this regard, it appears that the differential between EDF Energy's DD SVT rate and prepayment SVT rate (at typical consumption) broadly relates to the cost differential identified by the CMA.
- 4.7 We agree with the CMA that it is appropriate for it to undertake its own analysis into the cost-to-serve differential (Addendum, paragraph 10). This will be affected by the methodology used for bad debt allocation (potentially raising the cost of DD and decreasing the cost of prepayment). We encourage the CMA to take into account the wide variance in customer consumption between PPM and credit customers rather than use Ofgem typical consumption. We believe that this difference in consumption averages would materially impact on the analysis set out in Figure 1 of the Addendum. In particular, the comparator benchmark is questionable, owing to the considerable differences in average customer consumption: see Table 3 below for EDF Energy data (from 2015) on average customer consumption by payment method.

*Table 3: Average EDF Energy customer consumption by payment method (2015)*

[§<]

## **5. Difficulties switching either to other prepayment meter suppliers or to credit meters**

- 5.1 EDF Energy agrees with the CMA's provisional finding (Addendum, paragraphs 54-60) that the DAP as currently implemented can operate as an obstacle to customers switching supplier, and to suppliers specifically targeting indebted customers (Addendum, paragraphs 61-64). We believe that the DAP POA model currently adopted by 11 suppliers will help overcome this barrier - but it is necessary for all suppliers to adopt the process for this to be the case.
- 5.2 We also note the CMA's caveated finding (Addendum, paragraph 22) that "*It seems, however, that switching to a credit meter is a choice available which might make financial sense ... to a significant number of PPM customers*" and observation that at present (and pending wider roll-out of smart meters) "*only a small number of PPM customers make that choice*".
- 5.3 EDF Energy agrees that certain categories of customer would face particular difficulties switching to the credit sector (those in debt or with a poor credit history - paragraphs 47 *et seq.*).<sup>6</sup> EDF Energy does not believe that there is an AEC in respect of customers who face additional procedural complexities (switching either to credit or supplier) as a result of holding debt over

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<sup>4</sup> It is perhaps the case that other new entrants have had greater success in the credit DD segment, but in our view this is likely to be materially affected by the level of customer engagement.

<sup>5</sup> [§<].

<sup>6</sup> EDF Energy also recognises that any customer may be deterred from switching by the need to set up an appointment / be at home for meter replacement.

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£500. Indeed, a recent Ofgem panel on this subject concluded that *"Most Panellists end up thinking that in most circumstances, customers with debt should not be allowed to switch."*<sup>7</sup> It seems sensible that a customer who generates a very large debt should be obliged to reduce that debt before being able to switch so as to discourage the incurring of such debt levels.

- 5.4 The position is different for customers with low amounts of debt who also encounter difficulties switching to another supplier under the DAP. In such circumstances, EDF Energy considers that there is an AEC due to a flaw in the process.
- 5.5 EDF Energy does not currently charge PPM customers for the installation of credit meters (either upfront or deferred over a period of time) [§<]. Any upfront charging for the full cost of meters would be likely to discourage switching in a situation where there is willingness or already weak customer engagement. Therefore, we agree that any upfront charge would impede the ability of some PPM customers to make the switch and so limit their ability to access tariffs available to credit meter customers only. It also appears that this may impact most on those who are financially vulnerable.
- 5.6 EDF Energy only refused [§<] electricity and [§<] gas PPM switches to credit meters in 2014 where the customer was not in debt. The majority of the cases related to customers changing their mind or becoming uncontactable midway through the switching process. This contrasts with the figure for the industry as a whole, at 17,000, in 2014 (Addendum, paragraph 19). Clearly, other suppliers are objecting on a more frequent basis. However, while this level is unwelcome, it should be noted that it forms just a small proportion of the total number of PPM customer accounts in the market (approximately 0.2%).

## **6. Technical constraints in the prepayment meter infrastructure limiting prepayment meter tariffs**

- 6.1 EDF Energy agrees with the CMA that all of the current technical constraints taken together give rise to or contribute to an AEC. These can only currently be - partially - overcome by the installation of SMETS 1 meters which address the current technical constraints. However, SMETS 1 meters in themselves introduce barriers to switching in that these are not currently interoperable between suppliers and so installation of these meters may render it more difficult for customers to switch supplier again (in particular, on switching supplier, customers will lose the smart capability or have to have another type of SMETS1 meter installed).
- 6.2 The Addendum (paragraphs 31 *et seq.* and Appendix A) sets out a detailed description of the prepayment infrastructure and the constraints it imposes on tariff proliferation. In particular, the PPM infrastructure was designed with the capacity to hold only a limited number of tariff codes, meaning that suppliers can offer only a limited number of tariffs, particularly given that separate codes will generally be required for different regions (to reflect differing costs). Tariffs that are updated monthly (e.g. fixed price acquisition tariffs, which suppliers typically make available only for short periods, given fluctuating wholesale prices) would require separate codes for each tariff that currently has customers, even where such tariff is no longer available on the market to new customers. Consequently, it is particularly difficult for suppliers to offer fixed price tariffs in the PPS. Tariff variants such as Economy 7 also increase the number of codes required.
- 6.3 EDF Energy agrees with the CMA's analysis, and notes that technical constraints are a key factor in constraining tariff availability in the PPS. [§<]. No doubt smaller suppliers face similar hurdles.
- 6.4 EDF Energy's experience in this regard appears to be slightly at odds with the CMA's statement (Addendum, paragraph 34) that it has *"not found that the dumb prepayment infrastructure is currently being operated at its technical limits, except possibly for new entrants."* As explained

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<sup>7</sup> Ofgem Consumer First Panel, Year 6, Wave 4, "Switching Suppliers for Domestic Customers with Debt", p18.

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above, if we had offered a PPM version of each of our short-term fixed-rate tariffs in 2014, we would have run out of slots by [3<] 2014 and [3<]. Therefore while the system may not necessarily be operating at its technical limits per se, a risk for suppliers is that using more slots could restrict future tariff options. We would therefore welcome any measures to reduce and remove these technical constraints which will lead to greater competition in the PPS, and would be willing to explore with the infrastructure operators if the system can be used more fully (e.g. whether more pages/slots can be added or whether any unused ones could be reallocated between suppliers). However, we would caution against expensive interim fixes given the impending roll-out of SMETS 2 meters (i.e. ones that are fully interoperable immediately upon adoption by the DCC), scheduled for late 2016.

- 6.5 The CMA references that the roll-out of smart prepayment meters can side-step all aspects of the dumb prepayment infrastructure (Addendum, paragraphs 35 et seq.). To emphasise the point, EDF Energy agrees that *SMETS 2 PPMs* will remove technical barriers around the proliferation and availability of tariffs in the PPS *but not, without constraints to interoperability, SMETS 1 meters*. While Utilita and Ovo Energy have been able to sidestep some of the technical constraints relating to tariff slot availability by providing new customers with SMETS 1 meters, we do not believe that expediting SMETS 1 roll-out is a cost-effective and hence proportionate solution across the market.
- 6.6 Please see EDF Energy's response to the Remedies Notice (August 2015) for further views on the smart meter roll-out.
- 6.7 The CMA has not referred to one potential issue that comes with the move to smart meters relating specifically to customers on 'dumb' PPMs. As described above, this is that there is a risk of cost-to-serve for remaining PPM customers materially rising - as, under the current scheme, the legacy infrastructure costs will need to be recovered across a diminishing number of customers. There are a variety of potential solutions to this, such as spreading the costs across all customers but the issue is complex, and requires further consideration.

## 7. Softer incentives to compete to acquire prepayment meter customers

### *Higher acquisition costs*

- 7.1 EDF Energy notes the CMA's provisional finding that competition may be lower in the PPS due to higher costs of acquisition (Addendum, paragraph 42). However, we do not fully agree with the CMA's analysis, in particular with respect to our incentives to compete for such customers. We are always seeking to acquire new customers across all segments but we recognise that there are constraints on our ability to do so and temporary limitations as we await second generation smart meters.<sup>8</sup>
- 7.2 EDF Energy agrees that the roll-out of the *second generation* of smart prepayment meters will, *when the DCC is in place*, lead to decreased technical barriers as well as reduced acquisition and engagement costs as regards PPM customers, and therefore will lead to stronger competition between suppliers in the PPS, particularly as regards new entrants. As noted above, EDF Energy considers these benefits specific to SMETS 2 meters (supported by the DCC). Without SMETS 2 meters and the DCC, smart PPM customers are currently likely to lose their smart functionality and their ability to top-up remotely on change of supply. This could result in a poor customer experience and act as a disincentive to switch supplier, leading to customers being unable to access other PPM tariffs in the market.

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<sup>8</sup> Although not addressed by the Addendum, reduced doorstep selling due to challenging compliance requirements may have had an effect on successful acquisition rates in the PPM sector, albeit EDF Energy does not have analysis on the impact of this.

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- 7.3 We therefore disagree with the general assertion made that "...only very few suppliers (and none of the Six Large Energy Firms) have focused their strategy in the PPS on installing smart meters with a view to offering cheaper tariffs." (Addendum, paragraph 37). [X] This does not mean that we are not incentivised to do so, only that we are considering the issue prudently given the costs involved and the scale of the project. In our view, the prioritisation of PPM customers in the smart meter roll-out should only take place once the DCC is operational (providing the communications platform for switching) and a tested SMETS 2 prepayment solution is available. The prioritisation of PPM customers would introduce inefficiencies into the smart meter program and so careful consideration should be given to the impact on the overall cost and delivery timescales given that the timelines for smart delivery are already highly challenging.
- 7.4 EDF Energy notes the CMA's comment at paragraph 42 of the Addendum that suppliers cannot readily identify PPM customers with smart meters already installed by another supplier (unless informed by the customer). Even if suppliers were able to do so, interoperability problems with the current generation of smart meters could mean that on change of supply ("COS"), suppliers may not actually be able to maintain the SMETS 1 meters in smart mode and so would need to replace them before they could start serving the customer. It is possible, at some point after the DCC is in place, that such SMETS 1 meters will become interoperable once they are adopted into the DCC system. However, the feasibility of this is not guaranteed and is currently under review. This is because the DCC is likely to require substantial modification to support this initiative and there is a risk that site visits may be required in order to complete the adoption process, and that the cost of building the appropriate interfaces to each system will outweigh the short-term benefit. The principle behind SMETS 2 and the DCC is that it ensures meters can be retained as smart on COS by implementing a standard industry system and interface. We are therefore concerned that requiring smart services on COS for SMETS 1 PPM would undermine this, and lead to increased costs for customers. Nevertheless, as noted above, EDF Energy does not agree with the CMA's premise that potentially higher acquisition costs in themselves discourage us from targeting PPM customers, who, on the contrary, form a significant proportion of EDF Energy's customer base.

*Additional difficulties faced by prepayment customers wishing to change suppliers, including the DAP*

- 7.5 EDF Energy fully agrees that complexities or inconsistencies in application of the DAP rules (that discourage customers eligible to switch suppliers from doing so) adversely affect competition (Addendum, paragraphs 54 *et seq.*). The process is problematic given, as the CMA states, certain suppliers reject the switch due to levels of debt that should be unproblematic. The CMA should note that, to address this, EDF Energy and nine other suppliers (from April 2015) proactively took steps to change the operation of the DAP (and were joined by an additional supplier in July 2015). The changes under the POA approach aim to make it easier and simpler for PPM customers who are repaying a debt of £500 or less per fuel to switch, including by removing the requirement for customers to give permission to their old supplier to share data with the new supplier as part of an objections process. However, the POA is a voluntary commitment that has not been adopted by all suppliers (including a significant number of smaller parties) which has reduced its effectiveness. As stated above, we believe that all suppliers should be required to adopt this new process so that all customers can benefit from the improved outcomes. Industry has already started to make some changes to allow this to happen (by adding the DAP to the MRA) and it is essential that it is completed. The CMA should support this change and ensure that this is passed and successfully implemented at the earliest opportunity.
- 7.6 Finally, EDF Energy notes the CMA's view that suppliers are dis-incentivised from specifically targeting indebted customers (Addendum, paragraph 64) and that *"this may contribute to some*

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*extent to the softening of suppliers' incentives to compete to acquire PPM customers".* The CMA thereby implies that acquisition of indebted customers is not inherently unattractive other than for the reason that *"the probability of sales completion [is] very low"*. For information, EDF Energy has not historically differentiated between indebted and non-indebted customers as part of its acquisition strategy. Our incentive to compete for these customers has therefore not been affected by any potential relative attractiveness of indebted customers.

## **8. Regulatory barriers - Retail Market Review rules**

- 8.1 The CMA notes (Addendum, paragraph 74) that the simpler choices component of the Retail Market Review may restrict innovation in the PPS, by reducing the availability of dedicated PPM tariffs. We agree with this assessment, which is in line with the CMA's views as set out in its Provisional findings. EDF Energy refers to our submissions made in response to the Provisional findings and to the Notice of Possible Remedies, where we confirm our support for the removal of the 'simpler choices' component of the RMR rules, as proposed under Remedy 3.
- 8.2 EDF Energy considers that the removal of the four-tariff rule will help increase competition in the market, and lead to greater innovation and diversity of tariff offerings to consumers and increased switching overall. EDF Energy would like to be able to offer PPM customers further choice, but this is contingent on addressing the technical constraints noted above.

## **9. Conclusion**

- 9.1 In conclusion, EDF Energy is supportive of the focus on the PPS. A number of the CMA's findings identify features that are particularly problematic for PPM customers given the wider context of weak customer engagement. There are certain assumptions and features - as well as nuances of the sector - that a more detailed consideration of will enhance the CMA's analysis. Overall, however, the CMA is right to provisionally find that there is a feature or features giving rise to an AEC such that consideration of an appropriate package of remedies is required.

**EDF ENERGY**  
**JANUARY 2016**

# COMPETITION AND MARKETS AUTHORITY ENERGY MARKET INVESTIGATION



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**Response to the Second supplemental notice of possible remedies**

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**13 January 2016**

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Redactions are indicated by [X] and reflect items omitted due to reasons of commercial confidentiality or due to the terms of our licensing agreements with third parties

## SUMMARY

1. This submission is made by EDF Energy plc ("EDF Energy") on behalf of EDF Group companies. EDF Energy welcomes the opportunity to respond to the Competition and Markets Authority's ("CMA") Second supplemental notice of possible remedies ("Second Supplemental Remedies Notice"), dated 16 December 2015, as part of its market investigation in respect of the supply and acquisition of energy in Great Britain. This response should be read in conjunction with EDF Energy's response to the CMA's Addendum to provisional findings ("Addendum").
2. EDF Energy regards prepayment meter ("PPM") customers as an important and valued segment of our customer base. We currently serve approximately 760,000 PPM customer accounts [X]. This is equivalent to about 14% of our customer accounts and represents a wide demographic base. Many of our PPM customers value the ability to prepay as it provides them with both a sense of control and peace of mind, allowing them to budget effectively for their energy use and help avoid 'bill shock'.
3. EDF Energy wishes to see fully engaged and empowered customers making informed decisions with respect to their choice of tariff and supplier, within a trusted and trustworthy market. While PPM customers may be more aware of their energy purchasing than non-PPM customers (due to the need to top up their key or check how much money is left on the meter), we consider that the key adverse effect on competition ("AEC") affecting these customers (as in the broader retail segment) is weak engagement. EDF Energy therefore supports remedies that increase customer engagement in the prepayment sector (and more widely).
4. In our response to the first Supplemental notice of possible remedies (published in October 2015), and building on the Notice of possible remedies (published in July 2015), EDF Energy proposed a package of changes that we believe will increase the number of customers who actively choose their energy tariff, including PPM customers. This package included:
  - (a) The introduction of a fixed term of 12 months, and at a fixed price, for all default tariffs (i.e. tariffs not actively chosen by the customer).
  - (b) Regulated prompts every six months for customers that have not chosen a tariff.
  - (c) No cost to exit the tariff if the customer wishes to switch to an alternative tariff with the same or an alternative supplier.
  - (d) Monitoring of the relative rate at which suppliers engage customers by Ofgem.
  - (e) Additional powers for Ofgem to ensure that the tariffs suppliers offer disengaged customers are fair.
  - (f) A new deal for vulnerable customers, including a discount for those identified as eligible through enhanced data sharing with the Government.
5. The Second Supplemental Remedies Notice usefully examines the potential specific requirements of PPM customers. We have considered how our package of proposals could be enhanced in the interests of PPM customers. In this response we additionally propose:
  - (g) Suppliers must put PPM customers who have not made an active choice of tariff onto a tariff with a fixed price for 12 months from the launch of the tariff (due to limitations in the PPM infrastructure it will not be possible to provide customers with a 12 month fixed price from the date at which they start the tariff, as explained in answer to 22 (g) below).

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- (h) The six monthly prompts proposed must make clear the potential savings achievable from switching tariffs, including switching from PPM tariffs to tariffs that require a meter change i.e. to a credit meter, and include details of any charges that would be applicable.
- (i) Customers should have the option of spreading over time any charges for a meter change rather than paying upfront and there should be sensible and fair restrictions on the use of security deposits.
- (j) All suppliers should be required to apply the PPM Debt Assignment Protocol (“DAP”) Point of Acquisition (“POA”) model.<sup>1</sup> This will make it easier and simpler for all PPM customers who are repaying a debt of less than £500 to switch suppliers.
6. In our response to the Notice of possible remedies in August 2015, we recommended exploring whether there was a case for introducing additional protection for PPM customers, such as through a transitional safeguard regulated tariff. We therefore welcome the CMA further analysing this matter specifically for PPM customers. Having considered the evidence presented by the CMA, as well as our own experience of this part of the market, we do not believe, on balance, that a safeguard price cap is a justified or proportionate response to the harm identified in the Addendum to provisional findings. We agree with the CMA’s comment (paragraph 49) that any remedies to protect customers should be primarily aimed at PPM customers unable to switch away from a PPM (if they wish to do so) or those who would not benefit from increased competition within the prepayment sector resulting from the CMA’s other proposed remedies.
7. Our proposed package of changes are aimed at ensuring that PPM customers are better able to benefit from increased competition, and that the small number unable to switch supplier (e.g. those with debts in excess of £500) are protected under our proposed extension of Standard Licence Condition 7a. This gives Ofgem the necessary powers to act if they consider the prices to be “unduly onerous”.
8. We also note that the launch of the infrastructure to support fully secure and interoperable smart PPMs is expected in October 2016. This development will mean that suppliers wishing to target the PPM market will be able to avoid the technical constraints of the existing PPM infrastructure, by fitting new smart meters. This business model is already being pioneered by some suppliers although their customers will not currently be able to switch to an alternative supplier and keep the functionality of their meter due to the lack of interoperability between suppliers’ systems.
9. In summary, our response to the proposed new remedies is:
- **We do not support remedy 19:** *Sharing contact data of PPM customers with all suppliers* – we do not believe that this remedy is necessary to facilitate market entry by new suppliers and an unintended consequence may be customer confusion from multiple contacts. This could lead to less, not more, engagement.
  - **We support remedy 20:** *Removing the barriers to switching from PPM to Standard Credit* – we do not charge for meter changes or impose security deposits. We support removing barriers to switching as long as suppliers are still able to manage, fairly, their credit risk. Where meter charges are made, customers should have the option of spreading these over time. We welcome prompts for PPM customers to engage, including by switching meter type if they wish.

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<sup>1</sup> 11 suppliers have already adopted the DAP POA model, including EDF Energy.

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- **We support remedy 21:** *Reform of the debt protocol which allows customers in debt to switch supplier* - most of the industry has already implemented this change voluntarily. It should now become compulsory for all suppliers.
  - **We do not support remedy 22:** *A safeguard price cap for PPM customers* – we believe that a price cap would have severe negative unintended consequences for customers and would likely lead to customers becoming less engaged in the market. In addition, it would be very challenging to implement and administer effectively.

### Specific questions

#### Remedy 19 - Facilitating sharing of data relating to prepayment meter customers

10. EDF Energy supports efforts to reduce barriers to entry into the PPM market. We note that the roll-out of fully interoperable second generation (“SMETS 2”) smart meters is due to commence in low volumes during Q4 2016. The mass deployment of such meters (likely from Q1 2017) will allow suppliers to target the market and avoid the technical constraints associated with the current PPM infrastructure. These constraints limit the numbers of PPM tariffs available in the market as well as the ability to frequently update prices and so potentially constitute a barrier to entry.
11. We do not believe that the sharing of data relating to PPM customers is necessary in addition to the package of remedies we have proposed above, which builds on the provision of an independent price comparison service (as outlined in remedy 6). Organisations such as Citizens Advice may use a comparison service to provide independent advice, providing a more effective trusted and proportionate approach to supporting PPM customers.
12. We are not opposed to the sharing of data in principle; as the CMA has noted this remedy has been implemented for a segment of the customers of Engie (formerly GDF Suez) in France, and EDF in France voluntarily decided to also share customer data. Since 2015, any supplier has been able to request data relating to those EDF customers for whom regulated tariffs are coming to an end (i.e. large and medium-sized electricity consumers) and most suppliers have done so. However, the context in France is quite different from the UK, not least due to the lower number of suppliers participating in the retail market.
13. If the CMA were minded to require data sharing, we would strongly recommend testing the reaction of customers with comprehensive trials. We would be happy to share details of the experience in France when results become available, but it will only be through testing that the effectiveness of the whole package of remedies can be assessed and any unintended consequences avoided.
14. EDF Energy notes that in the context of the CMA’s Retail Banking Market Investigation, the CMA has indicated that the introduction of a similarly data-heavy account number portability system was likely to be “relatively costly and intrusive”<sup>2</sup>. We would welcome the CMA’s estimate of how many customers would benefit from remedy 19 and the costs of such a proposal.
15. We do not believe that this remedy is necessary to facilitate market entry by new suppliers and an unintended consequence may be customer confusion from multiple contacts. This could lead to less, not more, engagement.

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**(a) Would this remedy be effective and proportionate in increasing competition for non-smart prepayment meter customers?**

16. Direct mail campaigns from companies that do not have a direct relationship with a customer typically result in very small response rates - in the range of 1 to 3% in EDF Energy's experience. We are also concerned by the potential unintended consequence of reducing trust in the market further through customers receiving large amounts of unwanted promotional material. With around 35 domestic suppliers now active in the market, customers might receive up to 34 direct mail approaches, and many more from price comparison websites and other brokers. If widely adopted by suppliers, this remedy could result in the regular sending out of more than 100 million letters to approximately five million PPM customers. It may also result in the resumption of doorstep selling to customers, including vulnerable ones, who have not opted-out of the process, but may not welcome frequent visits.
17. The cloud database would also need to be set up and managed to continually update the records of five million customers and control the access rights for more than 35 suppliers and third party intermediaries. Ofgem would need to monitor the use of this data to ensure that it was used appropriately and that customers were benefitting from the information that they received.
18. Our research has shown that customers fear making a poor choice of tariff and that being presented with too much choice, without a method for making simple comparisons, can become a barrier to engagement (i.e. a 'loss aversion' impulse). We suggested an alternative approach in our response to the first Supplemental notice of possible remedies, namely a six-monthly prompt from a customer's own supplier, with an indication of savings available in the wider market for all customers on default tariffs. Regulated by Ofgem, we believe that these prompts would provide a more effective and proportionate way to engage PPM customers.

**(b) Are there additional legal considerations that are relevant to this remedy (eg under the Data Protection Act 1998 or the Privacy and Electronic Communications (EC Directive) Regulations 2003)?**

19. While EDF Energy can understand why the CMA may believe that providing consumers with the ability to opt-out (rather than having to opt-in) would enable suppliers to send non electronic promotions to PPM customers in a manner consistent with current Data Protection legislation, this might not remain the case once the new European Data Protection Directive has taken effect.
20. Our interpretation of the current legislation is that it is not possible to infer an opt-in or opt-out from a lack of response - a communication needs to be received from the customer. In our experience, return rates in relation to such questions are low. We suspect this would also be the case for PPM customers, and would result in the database being extremely limited.
21. It is also our experience that many customers are now very wary of providing consent to marketing on a broad basis. If the CMA wants to ensure that the database is as broad as possible it may need to consider (in conjunction with the Information Commissioner's Office ("ICO")) whether it would be appropriate to introduce specific legislation permitting disclosure by suppliers of this personal data irrespective of either an opt-in or opt-out being provided.
22. If specific legislation is not introduced, then promoting suppliers will need to receive appropriate reassurances and indemnification from the existing supplier or any central organisation which held the data, such as Ofgem, to confirm that the relevant consents have been delivered.

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**(c) Is Ofgem the right party to have oversight of this process?**

23. EDF Energy would expect the ICO to be involved and have oversight of data protection compliance. Ofgem would seem to be the right party to coordinate the database, and the scheme would need to be supported with adequate reporting to ensure that the approach was fair. In this respect, the process for securing consents would need to be clearly defined and applied consistently and uniformly by all suppliers.

**(d) What limitations would need to be imposed to ensure that the data was disclosed and used appropriately?**

24. Clarity through explicit rules would be required on the appropriate uses of the data and the type of marketing activity that would be acceptable to the regulatory authorities. For example, would the promotion of bundled non-energy products with energy tariffs be an appropriate use? It would also need to be clear which types of organisation should have access to the data e.g. suppliers only or third party intermediaries.

**(e) When should the continued need for this remedy be reviewed?**

25. We believe that any proposed data sharing exercise should be tested before being widely adopted. If introduced, the effectiveness should be assessed after one data sharing exercise has been completed before any ongoing commitment is made.

**(f) What might be a suitable frequency with which to share customer data?**

26. The frequency for sharing any data would need to be linked to the speed with which the data became out-of-date and how often suppliers were permitted to contact customers. We have found that contacting customers too frequently can have a negative effect (in terms of the customer experience) and so a limitation of contact to once a year might be appropriate. This would then also be the frequency with which the data is shared.

**(g) Should this remedy apply to prepayment customers with smart meters?**

27. Once the Data Communications Company (“DCC”) is operational and SMETS 2 meters are installed, there will be no continuing technical barriers to PPM customers fully engaging in the market. Customers with SMETS 2 meters will have the potential to switch their meter between prepayment and credit functionality, and be able to choose between a range of tariffs in the market. We therefore do not see the need for specific remedies once such meters have been fitted.

**Remedy 20 - Removing the barriers that prepayment meter customers without a debt face when attempting to switch to a credit meter**

28. EDF Energy recognises that 3% of PPM customers switched nationally from PPM to credit meters in 2014. However, we would note that EDF Energy’s PPM customers switch to credit meters more [3<] in 2014. This is likely to be at least in part because we do not levy a security deposit or charge for meter changes, highlighted by the CMA as barriers for customers attempting to switch meters.
29. While we support some restrictions on the use of security deposits, we do not believe that these should be overly prescriptive as it is appropriate that suppliers are able to manage their credit risk

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exposure. Such criteria could be regulated by Ofgem under Standards of Conduct to ensure that they are fair.

30. We support spreading the cost of the meters, if charges are applied at all, over 6 to 12 months as this would represent only a modest increase in bills. It is possible that the savings available to PPM customers from accessing a wider range of tariffs would offset the charge for the meter change in the first year.
31. We also support prompts to customers who are on default contracts, including PPM customers, to encourage them to switch tariff, and have proposed that these be on a six monthly basis rather than annually as the CMA proposes.

### **Remedy 20a - Prohibit the charging of a security deposit in circumstances when a customer is not in debt and has not incurred any fines, charges or interest for late payment in the last six months**

**(a) Would this remedy be effective and proportionate in removing the barrier to switching that security deposits can pose?**

32. We support some restrictions on the criteria used for applying security deposits, although we note that the numbers of customers affected may be relatively modest.
33. EDF Energy does not charge security deposits and in 2014, only refused [X] electricity (out of a total [X]) and [X] gas (out of a total [X]) meter switches to a standard credit meter where the customer was not in debt. The majority of these cases related to customers changing their mind or becoming uncontactable midway through the switching process.

**(b) Are these the right criteria to apply in determining circumstances in which suppliers can charge a security deposit?**

34. While the criteria appear appropriate, we believe that a customer's credit score is another one that may also be appropriate. However, rather than restrictive criteria, it would be proportionate for Ofgem to introduce guidance on the reasonable interpretation of security deposit rules, which could then be regulated under Standards of Conduct and require suppliers to justify the measures they use as being fair to customers.

**(c) What are the potential unintended consequences of being explicit about when customers can be charged a security deposit?**

35. Suppliers may wish to take different approaches with respect to deciding when it is appropriate to charge a security deposit, as part of differentiating their offer to customers and the cost base on which they operate. It is legitimate for suppliers to be able to judge the level of credit risk that is appropriate for their business.
36. If large numbers of PPM customers are encouraged to switch to credit meters during the roll-out of smart meters, it will result in some of these non-smart credit meters having very short operational lives and result in stranded asset costs (which ultimately increase prices for all customers). However, as described above, the number of customers switching nationally, compared with the level of EDF Energy's customers making this switch in 2014, indicates that other suppliers have very low levels that could be increased to our levels without having a substantial impact.

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**(d) Is there a preferable alternative way of mitigating detriment arising from the impediments to switching posed by the potential need to pay a security deposit?**

37. Rather than strict rules, we recommend principles-based regulation for managing the charging of security deposits, such as requiring suppliers to satisfy Ofgem that their approach is fair.

**(e) Should the CMA implement this remedy itself, or should the CMA make a recommendation to Ofgem to do so?**

38. Our proposed alternative of principles-based regulation of the criteria for security deposits would require ongoing monitoring by Ofgem.

**Remedy 20b - Suppliers are prohibited from charging customers upfront for the cost of a new meter when switching away from prepayment**

**(a) What length of time is reasonable and appropriate to allow the recovery of the cost of the meter and installation?**

39. A repayment plan of between six months and a year would result in customers paying approximately £2 to £5 a week, which is the typical range for debt repayments through PPM and in our view seems appropriate.<sup>2</sup> A longer time period would increase the risk of a customer having their meter replaced with a smart meter or moving home before they had finished paying for the meter.

**(b) Is this a proportionate remedy given the number of cases in which suppliers charge for removal of a prepayment meter?**

40. We believe that the approach is proportionate as spreading the costs would have limited financial impact for suppliers who currently charge for meter changes. The fact that proportionally more EDF Energy customers switch to alternative meters than on average for the industry, and EDF Energy makes no charges for meter changes, suggests that there is the potential for this remedy to help some customers.

41. It is important that customers are made aware of any charges that their supplier applies in a transparent manner, and that customers can easily find out if other suppliers also make a charge.

42. The voluntary approach to removing these charges which Ofgem is currently consulting on should mean even fewer customers will be charged for the installation of new meters in 2016 than was the case in 2015. Looking further into the future, such charges are likely to not exist at all (or will be very small) as with the roll-out of smart meters, suppliers will be capable of switching between PPM and credit modes without visiting the customer.

**(c) Is there an equally or more effective alternative way to reduce the costs of prepayment meter removal and replacement?**

43. Some suppliers do not charge for meter replacements and some specialise in fitting smart meters for their new customers. Effective prompts and greater transparency will enable customers to engage in the market and secure exchanges of meters for free.

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<sup>2</sup> Based on Ofgem, Domestic Suppliers' Social Obligations 2014 annual report

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**(d) Should the CMA implement this remedy itself, or should the CMA make a recommendation to Ofgem to do so?**

44. Ofgem already monitors activity such as this through Domestic Suppliers' Social Obligations reporting. It therefore seems appropriate for this requirement to be added to the existing reporting requirements.

**Remedy 20c - Require suppliers to provide annual notifications to prepayment meter customers setting out their right to switch and highlighting any potential restrictions or charges that may be payable**

**(a) Would this be an effective means of facilitating switches away from prepayment meters?**

45. We support customers being given annual notifications which make clear the right to switch to a different meter type and any charges that apply. In addition, in our response to the first Supplemental notice of possible remedies, we proposed prompts every six months for all customers on default contracts, including PPM default contracts. These prompts could contain the relevant information to facilitate switching such as the potential savings available should the customer switch to another PPM tariff or a standard credit type contract. This should be in a format regulated by Ofgem and extensively tested with customers in the design process to ensure that the format is effective.

**(b) What would be the most effective means of communicating this information to customers?**

46. The most appropriate method of communicating will depend on the customer's stated preferences, either by post or electronically, sent from their existing supplier.

**(c) What is a suitable frequency with which to contact customers? Would this messaging be more appropriately included alongside other messages or be triggered by particular events (such as outstanding debt being paid off)?**

47. In our response to the first Supplemental notice of possible remedies, we proposed prompts every six months for customers on default tariffs. We believe that annual prompts would be appropriate for those PPM customers who have actively chosen an alternative (i.e. non-default) PPM tariff.

48. The format and messaging within the prompts should be regulated to ensure consistent and fair treatment of customers. The relative success of suppliers in engaging their customers should be monitored by Ofgem. Suppliers with historic incumbent areas that have higher proportions of disengaged customers should be required to accelerate their efforts to match, and then maintain, equivalent levels of engagement to the better performing suppliers with historic incumbent areas.

**(d) Should a prompting remedy such as this be introduced directly by the CMA or should this be an area that Ofgem considers running randomised controlled trials to assess its effectiveness?**

49. It is essential that thorough testing of prompts is conducted with customers to ensure that the design is effective, whether these are introduced by the CMA or Ofgem. We have proposed that

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Ofgem has an ongoing role to ensure that suppliers are applying the successfully tested prompts consistently and effectively under Standards of Conduct.

### **Remedy 21 - Reform the protocol for assignment of debt on prepayment meters**

50. EDF Energy believes all suppliers should adopt the POA model for debt assignment, although an Order from the CMA may not be required for this to occur due to ongoing actions by Ofgem.
51. EDF Energy has already adopted, since April 2015, the PPM DAP POA model for debt assignment which removes the main barrier to switching supplier for customers with debts of less than £500. The POA model removes the requirement for customers to give permission to their old supplier to share data with their new supplier as part of an objections process.
52. However, not all suppliers have adopted this new model and so the experience of customers across suppliers will be different. We believe that all suppliers should be required to adopt this new process so that all customers benefit.
53. It is important that any proposals for PPM customers take into account the impacts of other remedies on the debt process. There may be a requirement for greater portability of debt to facilitate the move to 24 hour switching as proposed under remedy 4a. If this is the case, a more comprehensive change to the debt process may be required for all customers, including PPM customers.
- (a) Would a remedy recommending Ofgem to address the above-mentioned issues be effective in ensuring that adequate changes to the DAP are implemented promptly? Or should the CMA instead use its order-making power to support Ofgem's ongoing work?**
54. There is a continuing problem with suppliers not having adopted the new process. Around [X] of EDF Energy's PPM customers in Q3 2015 who tried to switch supplier (and had a debt of less than £500) applied to switch to a supplier that had not adopted the POA model.
55. The CMA and Ofgem should require all suppliers to adopt the POA model to ensure customers have clarity over the circumstances under which they are allowed to switch supplier.
- (b) What is the most efficient way for Ofgem and the industry to improve the DAP process in relation to the above-mentioned areas identified by Ofgem in order to increase the switching rates of indebted PPM customers?**
56. The adoption of proposed changes to Master Registration Agreement ("MRA") Agreed Procedure 13 ("MAP 13"), will make the new process mandatory for all suppliers and also introduce further improvements such as reducing the cases of complex debt.
57. Industry has already started to make some changes to allow this to happen (by adding the DAP to the MRA) and it is essential that is completed. The CMA should support this change and ensure that this is passed and successfully implemented at the earliest opportunity.
- (c) How would this remedy interact with the other remedies to address the Domestic AEC and/or detriment?**
58. In response to the first Supplemental notice of possible remedies, and building on remedy 10, we have proposed that prompts every six months to all customers on default tariffs are appropriate.

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59. Specific messaging for PPM customers in debt is incorporated into the POA model covering their right to switch supplier so that customers transparently see the potential benefits of switching. Making the process for debt protocols common for all suppliers would make the market easier to understand and reduce the barriers to engaging customers.
60. The greater portability of debt to facilitate a possible future move to 24 hour switching as discussed under remedy 4a may lead to the requirement to change the debt assignment process for all customers, including those with a PPM.

**(d) Are there other impediments to switching for indebted PPM customers – other than those identified by Ofgem – that need to be addressed? If so, what are these and how should Ofgem or the industry address them?**

61. The POA provides a simple process for switching supplier for those in debt. When combined with the remedies to increase prompts and transparency of charges, this package of remedies will support PPM customers in debt to switch supplier if they wish to do so.

**Remedy 22 - A transitional 'safeguard price cap' for domestic prepayment customers**

62. As stated in our response to the Notice of possible remedies in August 2015, we acknowledge the technical limitations which affect PPM customers and that some form of protection might be appropriate in respect of such customers.
63. In our response to the first Supplemental notice of possible remedies, we proposed extending the protection of Standard Licence Condition 7a, namely that deemed prices should not be "unduly onerous", to all default prices. We believe that this protection would be sufficient for Ofgem to monitor and act if customers were being treated unfairly, including PPM customers.
64. We also note that the roll-out of second generation (SMETS 2) smart meters, which will overcome the technical constraints of the existing PPM infrastructure, will commence in low volumes during Q4 2016. This will allow suppliers a way to avoid the technical limitations of the existing infrastructure and allows them to attract PPM customers with new and innovative offers. Customer demand for these offers may in turn increase the demand for the fitting of smart PPMs, in effect delivering prioritisation of PPM within the smart roll-out programme through increasing customer engagement.
65. As more PPM customers benefit from smart meters, Ofgem and other stakeholders will need to consider the fair allocation of the cost of the existing PPM infrastructure. As fewer customers utilise the infrastructure the fixed costs per customer will increase, and this is an issue that requires further consideration.
66. EDF Energy believes that the package of remedies that we have proposed and support to engage PPM customers will be effective and that a safeguard price cap to protect PPM customers is not necessary.
67. We also have serious concerns over the difficulties in setting a safeguard tariff price and implementing it, which are described in the detailed answers below, and the unintended consequences set out in answer to (m) below.
68. Although we do not support the introduction of a transitional 'safeguard price cap' for domestic prepayment customers, we have provided answers to the remaining questions in the section for completeness.

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**(a) If the transitional safeguard price cap for PPM customers were set relative to other prices in the domestic retail energy markets, how should we identify an appropriate level of prices and how can we ensure the level of the cap remains appropriate for the duration of the period it is in effect?**

69. It will be very difficult to set a price relative to other prices in the retail market. These are constantly changing and are subject to different restrictions such as fixed terms, termination fees and different types of customer service offering. This will be further complicated by the CMA's proposed remedies which are likely to result in greater innovation and more offers in the credit and direct debit market, as well as increasingly the smart market (albeit with different restrictions and conditions attached). It would not be appropriate, for example, to set the safeguard price cap with reference to prices which may have been set very low as special introductory offers for a limited number of customers and for a fixed period with conditions such as exit fees and restricted methods of contact with customer services centres (e.g. online only).
70. There is also a considerable challenge in keeping a safeguard price cap reflective of retail market prices. Frequent changes would allow prices to reflect changes in retail market conditions and costs. Less frequent changes would require greater headroom to manage the risk of changing costs and volumes of customers. We would suggest that the CMA explores the capability of the current PPM infrastructure to deliver price changes to the PPM customers of all suppliers within a limited time period. The limitations on the number of messages that can be sent to each terminal to deliver such updates to PPM keys may result in some customers not paying updated prices for some time, leading to consumption and pricing being out of step with the potential for negative impact on customer confidence and trust and potentially requiring new systems to track such updates.
71. We are also concerned that, without careful and close monitoring, there is the possibility that actions by suppliers, such as introducing large numbers of similarly priced tariffs which change any averaging calculation, could distort any safeguard price cap calculation.
72. The alternative to a retail market reference for setting prices would be to calculate costs on a bottom-up basis with allowed headroom and margin. However, this is also fraught with difficulties in setting prices on this basis. It would be time-consuming and would need to be subject to robust challenge to ensure that it was set at an appropriate level. We do believe, however, that it is a more appropriate method than retail market reference.
73. In our view, the difficulty in setting and keeping a safeguard price cap at an appropriate level is a strong argument against introducing one.

**(b) Could the imposition of a transitional safeguard price cap for PPM customers result in energy suppliers reducing the quality of service offered to customers on these tariffs?**

74. EDF Energy believes that it is unlikely that suppliers would reduce the level of service made available to PPM customers unless the reference price was based on a similarly reduced level of customer service. As the CMA acknowledges, the level of competition in the PPM market is increasing, and the remedies to engage more customers will accelerate this process. We believe that competition is the best incentive for suppliers to improve customer service, but suppliers will need to ensure that the costs for serving PPM customers are linked to the assumed costs in a safeguard price cap.

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75. Any financially vulnerable PPM customers would also benefit from the priority services that suppliers offer to support those customers who need it and, under our proposed package of proposals, would also receive a discount on their energy bill.

**(c) How should the headroom be calculated to provide the right level of customer protection while not unnecessarily reducing healthy competition?**

76. We believe that setting a cap with sufficient headroom would be vital. Headroom should be sufficient to give customers an incentive to engage in the market and switch tariff. EDF Energy's research has shown that a price differential of at least £150 is required to provide the incentive for more than 70% of customers to say that they would switch tariff, but this research was not based on customers who were protected by a regulated tariff. We recommend that if the CMA does intend to introduce a safeguard price cap that it undertakes customer research to understand the headroom necessary to provide customers with an incentive to switch from a regulated tariff. Our qualitative research indicates that some customers would find such a tariff, even with substantial headroom, attractive and wrongly believe that it was the best deal for them.

77. The headroom would also need to provide sufficient scope for suppliers to manage the risk of changes in costs and the volumes of customers leaving or joining the tariff. More frequent changes to prices would allow suppliers to reduce the risk and hence cost associated with this uncertainty. Conversely, less frequent changes would require more substantial headroom. The volatility of costs and volumes would be difficult to quantify so ongoing monitoring of these would be required with the ability to make adjustments for unexpected events or results. A potential restraining factor on how frequent price changes may be possible would be the capabilities of the PPM infrastructure, as explained in our response to (g) below.

78. However, if the cap is set too high it will allow suppliers with high levels of default PPM customers to maintain a competitive advantage over suppliers with low numbers of these customers.

**(d) What regulatory information would be required to set the transitional safeguard price cap?**

79. We do not believe that a safeguard price cap could be set without a full understanding of the costs of serving the customers, including the risks associated with volume uncertainty, and volatility of wholesale and non-energy costs.

**(e) How long should the transitional safeguard price cap be kept in place?**

80. If a safeguard price cap is introduced, it must be closely monitored to ensure that the effect of the tariff is positive and the potential unintended consequences do not exceed the expected benefits.

81. The timescale for removing a safeguard price cap could be linked to the smart installation programme, and so should not extend beyond the roll-out timescale.

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**(f) Should the termination date of a transitional safeguard price cap remedy be linked to the roll-out of smart meters? If so then should this be done explicitly, in aggregate or on a customer-by-customer basis?**

82. Customers with smart PPMs will benefit from the increased flexibility of the new infrastructure, and so the installation of such meters could be a trigger point for removing a safeguard price cap or perhaps a set time afterwards.

83. However, a potential unintended consequence is that if a safeguard price cap proved popular with customers it is possible they would be reluctant to have a smart meter fitted if it meant that they would lose the capped price.

**(g) How frequently – if at all – would the level of the cap need to be reassessed?**

84. The frequency with which a review of a safeguard cap would be required will depend on the level of headroom allowed in the price. Please see our response to (c) above.

85. A potential factor in determining how frequently the cap could be reviewed is the ability of the PPM infrastructure to handle a price change for all suppliers at the same time. The limited capacity of terminals to update prices may result in customers not receiving their new prices for some time and result in them paying an incorrect amount for their energy. We recommend that the CMA investigates further the ability of the infrastructure to deliver price changes to all PPM customers at the same time and the potential impact on customers who do not receive updates immediately. However, we would caution against expensive interim fixes given the impending roll-out of SMETS 2 meters (i.e. ones that are fully interoperable immediately upon adoption by the DCC), scheduled for late 2016.

**(h) Which prepayment customers should this remedy apply to?**

86. We do not believe this remedy is proportionate for any PPM customers. As previously stated, we believe that extending the protection of Standard Licence Condition 7a is sufficient to allow Ofgem to appropriately protect customers that need protection and most customers will benefit from the remedies to increase engagement.

**(i) Which energy suppliers should be subject to the transitional safeguard price cap, and why? Should it be restricted to the Six Large Energy Firms, or should all retail energy suppliers be covered?**

87. If introduced, all energy suppliers should be subject to this remedy, otherwise the customers of exempt suppliers would not be offered the same level of protection as those with non-exempt suppliers.

**(j) How should the transition from the current arrangements be managed? Should there be a period over which the transitional safeguard price cap is phased in? If so, how long should this period be and how should the transition work?**

88. The transition arrangements need to take into consideration the already committed costs of suppliers (such as hedged energy costs), and the ability of customer service centres and the PPM infrastructure to manage the transition. A more detailed examination of these factors is required to assess a suitable timescale.

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**(k) Would energy suppliers have the ability to circumvent the remedy, for example, by encouraging domestic prepayment customers to switch on to less favourable, unregulated tariffs, and how could such risks be mitigated?**

89. Any misleading approaches to customers would be non-compliant under the existing Standards of Conduct licence condition.

**(l) Should the CMA set the level of the transitional safeguard price caps itself, or should the CMA make a recommendation to Ofgem to do so?**

90. We believe that any price must be set in full knowledge of the costs of supply and must include the appropriate level of headroom to incentivise customers to switch tariff and allow suppliers to manage costs and customer volume risks appropriately and fairly. This could be implemented by the CMA or Ofgem.

**(m) Are there any potential unintended consequences of setting a transitional safeguard price cap, for example, in terms of their potential impact on the level of other, unregulated tariffs?**

91. There are many potential unintended consequences of setting a safeguard price cap. These include:

- Eligible customers are attracted to a tariff with regulated prices rather than engaging in the market.
- If the headroom is set too low, new entrants and existing competitors will struggle to persuade customers to leave the protection of regulated prices, reducing the market for new entry and ultimately the amount of competitive deals available to PPM customers.
- A relatively high safeguard price cap allows suppliers with high levels of default PPM customers to maintain a competitive advantage over suppliers with low numbers of these customers.
- The level of the safeguard price cap is not capable of changing as rapidly as the market and so insufficient headroom could mean suppliers are unable to manage market risks.
- Customers fear losing their protected prices if they have a smart meter fitted and so resist the roll-out programme, thus increasing the costs of the programme.

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