



## Domestic Gas & Electricity (Tariff Cap) Bill: Public Bill Committee Written Evidence

March 2018

### About SSE

SSE is a UK-listed company and the broadest based utility operating in Great Britain with separate retail, wholesale, networks and enterprise businesses. SSE's core purpose is to provide the energy people need in a reliable and sustainable way and, as of 31 December 2017, SSE had 7.67 million energy customers across Great Britain and Ireland. As a responsible company, SSE seeks to maximise at a national and local level the economic benefits that are created by its activities and in 2016/17, SSE made a contribution of £9.3 billion to UK GDP. SSE is proud to be one of the UK's largest Living Wage employers and the first FTSE 100 company to be awarded the Fair Tax Mark.

### Summary

- On 26 February 2018, the Government introduced to Parliament the *Domestic Gas and Electricity (Tariff Cap) Bill*, which sets out plans to introduce a temporary 'absolute' price cap on standard variable and default tariffs (SVTs). Second Reading of the Bill took place on Tuesday 6 March 2018, and the legislation is now being considered by Public Bill Committee.
- SSE strongly believes that competition, not caps, is in customers' best long term interests. There is strong evidence to indicate the GB energy market is highly competitive and that competition is intensifying even further, with over 60 suppliers now active in the market, 5 million customers switching last year alone, and one in five customers now supplied by small and medium suppliers. The regulator has already put in place price caps for vulnerable customers, with prepayment meter (PPM) customers and those eligible for the Warm Home Discount (WHD) having the price they pay for their energy capped by Ofgem.
- Although SSE does not support the legislation, with the Bill now progressing through Parliament, we are keen to work constructively with Government, Parliament and Ofgem to ensure the legislation is implemented in a way that mitigates the risk to the competitive market, thereby customers. There are *three* key issues which SSE would encourage Parliamentarians to raise at Second Reading:
  1. the criticality of ensuring that the **methodology** Ofgem used to set the level of the cap accurately reflects the costs of supplying energy – it would be unworkable to simply recycle the methodology used for the PPM cap or WHD cap, which is set below the cost of supplying energy at scale.
  2. in-line with other price controls, suppliers should have the right to appeal the level of the cap on the merits via the **CMA appeal route**; and
  3. urgent clarity is required around the **conditions under which an SVT price cap would be removed**.

### 1. The methodology is critical and must accurately reflect the costs of supplying energy.

- Designing the methodology for such a significant intervention as a price cap will be a complex undertaking for Ofgem. In setting the level of any cap, it is essential that Ofgem completely rebuilds the methodology it established for the PPM cap and vulnerable customer safeguard tariff to ensure it accurately reflects the costs of an efficient supplier with sustainably priced tariffs that serves the needs of all customers. Currently, the PPM cap and the vulnerable customer safeguard tariff do not and, amongst PPM customers, SSE has witnessed a significant reduction in switching rates.
- Specifically, SSE has concerns that: the cost to serve benchmark is too low, set on the basis of companies that do not earn a profit or serve all customer segments; the significant and growing cost of delivering the smart meter roll-out is not recognised; the cost of managing customers' energy demand against supply; and policy costs, like those that support low-carbon investments, have escalated far more quickly than the cost inflation index. Despite consistently having one of the lowest costs to serve of all the major suppliers, MPs should be aware that SSE is making a loss on these regulated tariffs.
- Proposed amendment 4 (Clause 1, page 2, line 15) to include in legislation a target to reduce bills by £100 would undermine the independence of the regulator in setting a cost reflective, sustainable methodology. Applied unilaterally it would likely have the unintended consequence of penalising the most efficient suppliers.
- Proposed amendment 6 (Clause 6, page 4, line 31) would reduce Ofgem's periodic review of the cap from a minimum of every six months, to a minimum of every three months. Requiring Ofgem to review the cap every three months is not practical and would increase volatility in the market to the detriment of customers. The six month review currently required in the legislation would allow for a timely and proportionate evaluation of the cap in order to reflect changes in the costs of supplying energy, including changing wholesale costs.

## **2. Suppliers should have the right to appeal the level of the cap on the merits via the CMA appeal route.**

- The planned legislation places a duty on Ofgem to set a price cap for SVTs and default tariffs without the ability to appeal the level at which the cap is set to independent experts (i.e. an appeal on the merits). SSE believes appeal rights to an independent and expert body, like the Competition and Markets Authority, are a faster and more effective appeal mechanism than judicial review and would ensure that any appeals are treated in a manner consistent with other price controls.
- It is essential that suppliers have appropriate appeal routes should they need to challenge the level of the cap to ensure best outcomes for consumers and maintain investor confidence. This isn't about delaying the implementation of a price cap. It's about protecting customers from the unintended consequences of getting implementation wrong, including stifling competition and deterring potential new entrants and investment.

## **3. Urgent clarity is required around the conditions under which an SVT price cap would be removed.**

- The Bill makes provision for Ofgem in 2020 to review whether the conditions are in place for effective competition and to determine whether the price cap should be extended. There is potential for it to be extended up until 2023.

- SSE has concerns that a price cap could have a detrimental impact on competition and therefore believes the review provided for in the legislation is likely to conclude that competition has reduced, making the cap self-perpetuating. There is strong evidence to demonstrate that the introduction of the price cap for PPM customers has undermined competition, with SSE having seen a significant decrease in PPM customer switching and a convergence of tariffs around the level of the cap, which has reduced customer choice. SSE is concerned that the impacts on the competitive market will be even more significant as a result of an SVT price cap.
- As was raised by numerous witnesses during the BEIS Select Committee's pre-legislative scrutiny, greater clarity is needed around the conditions under which a price cap would be removed from 2020, not least because this would give suppliers a better idea of how to target their efforts to improve outcomes during the intervening period.