



House of Commons

Business, Energy and Industrial
Strategy Committee

**Pre-legislative scrutiny
of the draft Domestic
Gas and Electricity
(Tariff Cap) Bill**

Fourth Report of Session 2017–19



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*Report, together with formal minutes
relating to the report*

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Business, Energy and Industrial Strategy Committee

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Summary

Following months of speculation, manifesto commitments and exchanges with the regulator (Ofgem), the Government published on 12 October 2017 the draft Domestic Gas and Electricity (Tariff Cap) Bill in which it set out its plan to introduce a temporary absolute price cap on standard variable and default tariffs. This report is our response to the Government's invitation to scrutinise the Bill and make recommendations to improve it. It contains our assessment of the situation the Bill aims to redress and the outcomes it aims to achieve against extensive evidence.

Energy is a special and essential service. For this reason, the operation of energy markets is held to high standards. Sadly, competition in the domestic energy market is not working effectively for 12 million customers stuck on poor-value tariffs called standard variable and default tariffs. This market has become two-tiered, with some consumers paying up to £300 more than others each year. Customer loyalty should be rewarded by suppliers, not exploited. Regardless of customers' reasons or obstacles to switching suppliers, no one should be penalised disproportionately for not engaging with competition, nor should it be a requirement that consumers constantly defend themselves against excessive charges. Where markets fail to deliver fair outcomes, intervention is justified.

Suppliers most at fault did not take repeated warnings from the Government seriously enough: we were underwhelmed by the feeble steps announced by some of the Big Six in the hope to avoid a cap. Those retailers who were found by the Competition and Markets Authority to be operating inefficiently and passing excess costs onto standard variable and default tariff customers have brought this intervention upon themselves. We hope they start treating their loyal customers more fairly in the future.

The market has been dysfunctional for years. And yet Ofgem has been too slow and reluctant to use its extensive powers to step in and protect the interests of customers, especially vulnerable customers. It took repeated nudging and too much time for the regulator to start actively protecting some customers from overcharging. We urge Ofgem to be more proactive in the future in meeting its statutory duties towards consumers. We expect it to work hard with various stakeholders to find new ways to engage customers who have the most difficulty in switching in the future.

These repeated failures have led us to support the Government's initiative to set a temporary absolute price cap on standard variable and default tariffs. We agree with the Government that the evidence is on balance against a relative price cap: it would create a perverse incentive for suppliers to increase their lowest prices to keep their profit levels constant. An absolute cap also bears a risk of increasing prices but this risk is lesser and it will be the most effective measure at delivering the Bill's key goals: improving fairness and reducing the overcharging of standard variable and default tariff customers. We concluded that the Competition and Markets Authority's Energy Market Investigation remedies alone would not necessarily fix the problems in the market soon enough.

We trust Ofgem will be able to set a cap that meets most of the requirements listed in subsection 1(6) as the Northern Ireland experience proves that regulation and competition can co-exist usefully. We recognise that setting a cap that meets all five

requirements will be a challenging task which may lead to legal challenges. We are confident these challenges could be won by the regulator provided that the Government clarifies that not all requirements need be achieved at once. The Bill should be amended to require that Ofgem review the level at which the cap is set at least every six months.

We believe the Government should take Ofgem's concerns about the green electricity tariff loophole seriously and amend the Bill accordingly. The exemption, which we otherwise welcome, should be extended to green gas tariffs.

We support the Bill's sunset clause as it guarantees the temporary nature of this intervention.

We were satisfied with the Government's rationale for leaving the regulator in charge of assessing the "conditions for effective competition" both when setting and recommending whether to keep or remove the cap. It is also right that the final decision sits with the Secretary of State.

This inquiry has helped to shed light on the role that smart meters will be called to play in customer engagement once fully rolled-out. We will welcome confirmation from the Government that it does not place undue hopes on smart meters and that instead it will work to ensure that once the cap is lifted suppliers cannot go back to their exploitative practices.

Finally, we ask the Government to confirm what long-term measures it will implement for the protection of vulnerable customers and that it seeks to ensure the Bill receives Royal Assent before the parliamentary summer recess.

1 The draft Domestic Gas and Electricity (Tariff Cap) Bill

Pre-legislative scrutiny of the draft Domestic Gas and Electricity (Tariff Cap) Bill

1. Following a Conservative Party manifesto commitment to extend existing price controls to “more customers on the poorest value tariffs”¹, the Queen’s Speech 2017 outlined the Government’s plans to ensure “fairer markets for consumers.”² The Secretary of State for Business, Energy and Industrial Strategy, Rt Hon. Greg Clark MP, then asked the gas and electricity regulator, Ofgem, what steps it would take regarding “the future of standard variable tariffs” and the “safeguarding” of customers on the poorest value tariffs.³ Ofgem’s reluctance to introduce a market-wide cap without the introduction of primary legislation⁴ prompted the Government to take action and publish the draft Domestic Gas and Electricity (Tariff Cap) Bill on 12 October 2017.⁵

2. In a statement to the House of Commons on the same day, the Secretary of State for Business, Energy and Industrial Strategy formally asked us to scrutinise the Bill.⁶ We agreed to do so, partly on the basis that it complemented our existing work on energy price controls.⁷ We received written evidence from energy stakeholders, Members of Parliament and members of the public. We heard oral evidence from competition experts, consumer bodies, energy suppliers, Ofgem and the Department for Business, Energy and Industrial Strategy. We are grateful to all those who have provided evidence to this inquiry.

3. We had also agreed to meet the Secretary of State’s request to report by the end of January.⁸ However, the Cabinet reshuffle in January 2018 delayed our oral evidence session with the Minister of State for Energy and Clean Growth, Rt Hon. Claire Perry MP, and, consequently, this report. Nonetheless, the publication of this report in February should provide sufficient time for a committed Government to seek parliamentary approval of the Bill before the summer recess. This would guarantee that energy customers receive protection from excessive prices in time for winter 2018.

Improving fairness and effective competition

4. From 1986 onwards, the GB energy market was progressively liberalised but even today it remains partially regulated and held to high standards. Policy interventions are taken regularly by government or the regulator to ensure that the market delivers both effective competition and fairness for all energy consumers, especially for those who are

1 Conservative Party, [Forward Together - The Conservative and unionist party manifesto 2017](#), p60

2 Cabinet Office, [Queen’s Speech 2017](#), 21 June 2017

3 Department for Business, Energy & Industrial Strategy, [Letter from Rt Hon Greg Clark to Dermot Nolan, CEO Ofgem](#), 21 June 2017

4 ‘Legislation needed to tackle UK power price rises, regulator warns’, The Financial Times, 17 August 2017

5 [Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), Department for Business, Energy & Industrial Strategy, 12 October 2017

6 HC Deb, 12 October 2017, [col 474](#) [Commons Chamber]

7 Business, Energy and Industrial Strategy Committee, [Energy price cap inquiry](#), October–November 2017

8 Business, Energy and Industrial Strategy Committee, [Correspondence from the Chair to the Secretary of State, BEIS, on pre-legislative scrutiny of the draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), 25 October 2017

vulnerable. This is because energy is seen to be an “essential service”,⁹ an “unavoidable necessity of life, which amounts to a significant portion of household budgets”.¹⁰ In the words of the Minister:

[...] There is something very fundamental about energy—about heating and lighting a home—particularly for the most vulnerable customers.¹¹

5. We agree that where existing frameworks fail to deliver fairness or effective competition in the provision of essential services like energy, they must be amended. This report is our assessment of the Government’s proposed remedy for a market that is “not working for all consumers”.¹² We want to work constructively with the Government to make the Tariff Cap Bill as effective and beneficial as possible for all energy consumers.

6. One of the key objectives of the Bill, according to the Minister, is achieving fairness.¹³ The other one is “to protect domestic energy customers from unjustifiably high prices until the conditions for effective conditions are in place.”¹⁴ In our inquiry, we assessed the Bill and the evidence we gathered on it against these two objectives and make recommendations where we consider that they could be achieved better in a different way.

9 [Q361](#) [Dermot Nolan]

10 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, p1

11 [Q431](#) [Claire Perry]

12 [Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), Department for Business, Energy & Industrial Strategy, 12 October 2017

13 [Q431](#) [Claire Perry]

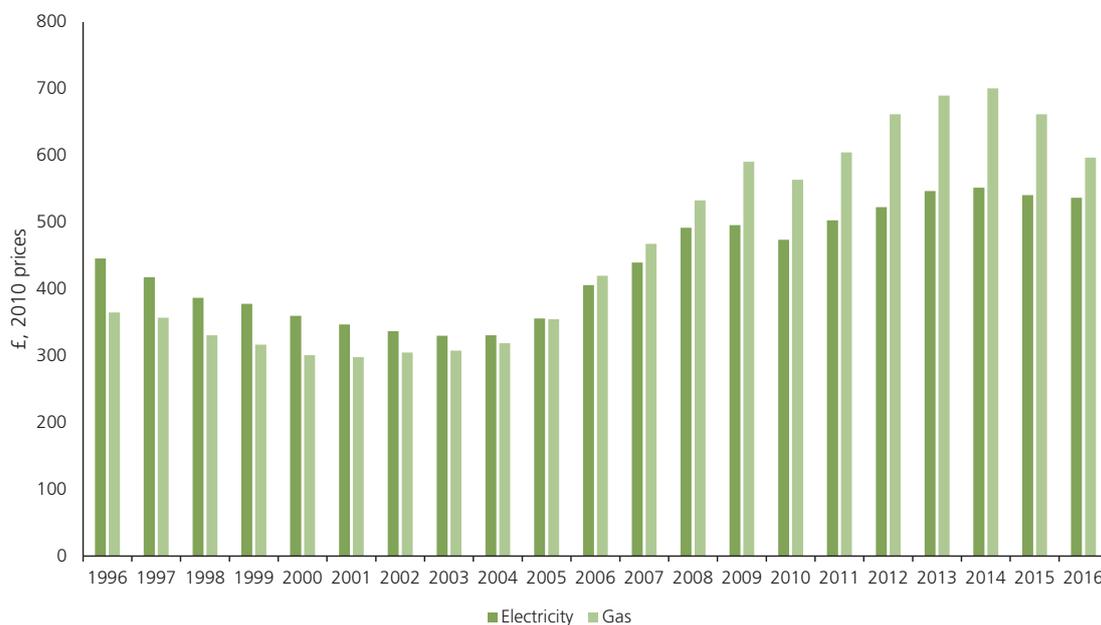
14 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, p1

2 The cost of inaction

A two-tier market

7. In a truly competitive market, loyalty should be rewarded, not exploited. This is both our view and that of the Government.¹⁵ Energy is an essential good and a significant portion of household budgets, especially for those on the lowest income: it amounts to up to nine per cent (9.3 per cent) of the poorest households' total expenditure. As a result, when the market fails to deliver good-value tariffs, those who can least afford it are disproportionately affected.¹⁶

Average annual bills for typical consumers



Source: House of Commons Library analysis (Quarterly energy prices, BEIS)

8. Between 2000 and 2008 energy prices rose steadily. Since 2008, prices have been more stable, although they have risen in real terms.¹⁷ Ofgem's latest assessment of the market made it clear that the domestic energy market does not currently deliver fair or effective competition for all: the market is two-tiered, rewarding those customers that are able and willing to shop for the best deals at the expense of those, especially vulnerable customers, who are less engaged.¹⁸ 58 per cent of non-prepayment energy customers—or 12 million households—remain on a “poor-value”¹⁹ variable tariff, paying up to £300 more than they would on a cheaper tariff.²⁰ This is only a 11 percentage point decrease from the 69 per cent of customers on a standard variable tariff (‘SVT’) recorded by Ofgem in March 2015.²¹

15 [Q425](#); Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, para.2

16 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, para.19

17 House of Commons Library, [Energy bills and proposals for reform](#), 5 October 2017, p6; Chart from House of Commons Library, [The Current Energy Market Reforms in Great Britain](#), 15 March 2017, p7

18 Ofgem, [State of the energy market 2017](#), 31 October 2017, p9

19 As above, p3

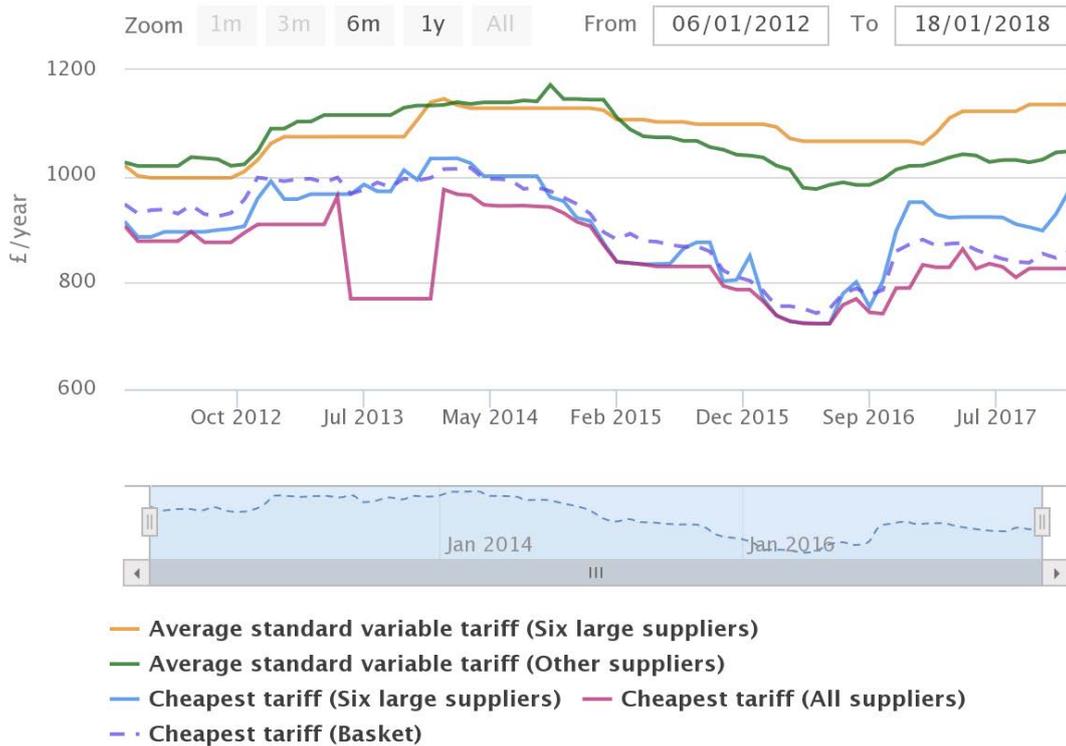
20 As above

21 Ofgem, [Retail energy markets in 2016](#), 3 August 2016, p3

9. Data gathered by Ofgem (see graph below)²² show that SVTs are “poor-value tariffs” because they are consistently more expensive than other tariffs available in the market, regardless of the type of supplier supplying them.

Retail price comparison by company and tariff type: Domestic (GB)

Retail price comparison by company and tariff type: Domestic (GB)



10. We were particularly concerned by the overwhelming evidence²³ that vulnerable and low-income customers are especially affected, with 83 per cent of those living in rented social housing, 75 per cent of those on low incomes, 73 per cent of those with no qualifications and 74 per cent of disabled customers on an SVT.²⁴ Evidence suggests that they struggle to engage with competition and are less likely to overcome obstacles to switching, even with the help of engagement measures.²⁵ Even with the advent of smart meters, we heard evidence that they may still require protection from overcharging as the Government’s proposed price cap would not help them engage with competition more actively.²⁶

11. We accept the evidence from Ofgem, consumer bodies and the Minister that vulnerable customers will benefit most from the Tariff Cap Bill and will, in all

22 Ofgem, Data portal, Retail Market Indicators, [Retail price comparison by company and tariff type: Domestic \(GB\)](#), accessed 29 January 2018

23 Citizens Advice [PLS0021](#), Scope [PLS0025](#), National Energy Action [PLS0037](#), Care & Repair Cymru [PLS0040](#); [Qq430-431 \[Claire Perry\]](#); Ofgem, [Vulnerable consumers in the retail energy market: 2017](#), 16 October 2017

24 Ofgem, [Financial protections for vulnerable consumers](#), para. 2.6, 11 October 2017

25 Citizens Advice [PLS0021](#), Scope [PLS0025](#), National Energy Action [PLS0037](#), Care & Repair Cymru [PLS0040](#), Ofgem [PLS0045](#); [Qq430-431 \[Claire Perry\]](#)

26 Ofgem [PLS0045](#); [Q334-336 \[Dermot Nolan\]](#)

likelihood, need some form of price protection for the foreseeable future, including after the Government's price cap is lifted. *We recommend that the Government provides details on its plans to protect vulnerable customers from overcharging when Ofgem's safeguard tariff and the Government's price cap are lifted.*

Protecting vulnerable customers through data-sharing

12. Because we agree that vulnerable energy customers may need additional protection for the foreseeable future, helping provide better protection of these consumers is a key priority for us. Both the regulator and suppliers struggle to identify at times who vulnerable customers are and how they can assist them best through essential services like the Warm Home Discount or the Priority Services Register. Ofgem told us²⁷ how data-sharing could be used to make this task easier: by amending the Digital Economy Act to allow data-sharing of government-held data on vulnerable customers with Ofgem and energy suppliers, the Government could provide increased protection to vulnerable customers. The Cabinet Office consulted on the issue²⁸ but both in correspondence²⁹ and evidence,³⁰ the Government did not commit to a clear timetable to respond to the consultation or follow Ofgem's advice on amending the Digital Economy Act.

13. **We agree with Ofgem that legislative obstacles to data-sharing of vulnerable customer data held by government with energy suppliers need to be removed so as to give vulnerable customers better protection. We recommend that the Government commits to removing these obstacles by seeking to amend section 36(3) of the Digital Economy Act 2015 in time for winter 2018.**

Ofgem's role in protecting customers

14. Ofgem's key mission is to protect the interests of gas and electricity customers, especially vulnerable customers.³¹ Yet, despite clear requests for advice from the Secretary of State³², cross-party support for price control measures³³ and extensive regulatory powers, Ofgem ruled out introducing a market-wide cap without the backing of primary legislation because of potential legal challenges.³⁴ Dermot Nolan, the Chief Executive of Ofgem, told us:

The second to last time I was in front of the Committee, before the last election and before the manifesto, I said very clearly—and I do not think it

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- 27 Business, Energy and Industrial Strategy Committee, [Letter from Ofgem Chief Executive to the Chair relating to energy price cap inquiry, 1 November 2017](#), published 22 November 2017
- 28 Cabinet Office, [Digital Economy Act, part 5: data sharing codes and regulations](#), closed consultation, accessed 31 January 2018
- 29 Business, Energy and Industrial Strategy Committee, [Letter from Secretary of State \(BEIS\) to the Chair relating to Tariff Cap Bill, 29 November 2017](#), published 5 December 2017
- 30 [Qq498-499 \[Claire Perry\]](#)
- 31 Ofgem, [Who we are](#), accessed 31 January 2018
- 32 Department for Business, Energy & Industrial Strategy, [Letter from Rt Hon Greg Clark to Dermot Nolan, CEO Ofgem](#), 21 June 2017; Oral evidence taken on 1 November 2017, HC (2017–19) 470, [Q145](#) [Greg Clark]
- 33 Conservative Party, [Forward Together: The Conservative and Unionist Party Manifesto 2017, p60](#); Labour Party, [For the Many, Not the Few, the Labour Party Manifesto 2017, p20](#); The Scottish Nationalist Party, [Stronger for Scotland, The SNP Manifesto 2017, p38](#)
- 34 Oral evidence taken on 17 October 2017, HC (2017–19) 470, [Q62 \[Dermot Nolan\]](#)

was contested at the time—that an intervention through a full, market-wide price cap, a significant policy change to the framework set up, was a matter for Government.³⁵

15. The regulator only confirmed its intentions to introduce a safeguard tariff for vulnerable customers in receipt of the Warm Home Discount in October 2017.³⁶ Due to statutory obligations to consult for several weeks, this policy was only put in place in February 2018.

16. Ofgem also allowed suppliers, at the end of a fixed-term contract, to roll over customers who have not made an active choice on to a further fixed-term tariff as long as that further tariff is similar in kind and no more expensive.³⁷ The regulator was considering setting mandatory targets for suppliers to take customers off SVTs³⁸ but it has now ruled it out as it would conflict with the Government’s price cap.³⁹

17. In evidence to us on 10 January 2018 Dermot Nolan apologised to vulnerable customers for not acting to protect them from overcharging sooner by introducing a safeguard tariff.⁴⁰ He also acknowledged that competition was “not as effective as it could be yet.”⁴¹ Ofgem recognises that even though it is currently implementing Competition Markets Authority remedies to increase engagement,

it will take time before disengaged vulnerable consumers (some of whom may never be able to fully participate in the market) see benefits from the market working properly.⁴²

18. The Secretary of State was clear that this Bill could have been avoided and customers could have received help more quickly if Ofgem had made use of its existing powers.⁴³ We support the Secretary of State’s view that customers could have received protection against overcharging more quickly if Ofgem had acted upon clear signs of market failure to put an end to SVTs and introduce price controls. We respect the regulator’s independence of government but we regret that Ofgem did not build on clear cross-party and government support to intervene to end the overcharging of customers on standard variable and default tariffs.

19. The Secretary of State argued that public policy is often subject to the possibility of legal challenges but that it does not mean they are always successful or that one should not proceed with policy.⁴⁴ We were unconvinced by Ofgem’s argument that primary legislation was required for them to set a market-wide cap. We concur with the Secretary of State that legal challenges can be won and should not be a deterrent from implementing policies that are in line with the regulator’s statutory duties to protect the interests of consumers.

20. We conclude that Ofgem have failed customers, especially vulnerable customers, by being overly cautious and reactive on the issue of poor-value standard variable and

35 [Q371](#)

36 Ofgem, [Statutory consultation for a vulnerable customer safeguard tariff](#), 11 October 2017

37 Ofgem, [Decision: Default tariffs for domestic customers at the end of fixed-term contracts](#), 11 October 2017

38 Ofgem [PLS0045](#)

39 [Q389 \[Dermot Nolan\]](#)

40 [Qq371-373](#)

41 [Q356](#)

42 Ofgem, [Statutory consultation for a vulnerable customer safeguard tariff](#), p2

43 Oral evidence taken on 1 November HC (2017–19) 470, [Q150 \[Greg Clark\]](#)

44 Oral evidence taken on 1 November 2017, HC (2017–19) 470, [Q151](#)

default tariffs. They should have removed the obligation to move customers at the end of their fixed-term contracts on default tariffs sooner and set mandatory targets for suppliers to take customers off standard variable tariffs when it was still appropriate to do so. We urge Ofgem to be faster and more proactive in using their extensive powers to protect customers from overcharging in the future.

21. The evidence highlighted that the Competition and Markets Authority remedies⁴⁵ currently being implemented may not be sufficient to redress the failures of the market on their own. Not only are these remedies slow to implement and show impact, but they are also unlikely to be a “game-changer”.⁴⁶ One of the evidence submissions said:

Overall, our assessment is that CMA package of measures will increase consumer engagement (including switching), but the improvement is likely to be insufficient to address the political pressures surrounding this market. CCP research on the effectiveness of demand-side remedies, across a range of sectors, finds that such remedies can be valuable for enhancing consumer engagement, facilitating switching, and driving more effective competition, but that they are unlikely to resolve all competition concerns in markets where firms are able to discriminate between engaged and unengaged customers. In the case of energy, even after the CMA’s remedies have had time to work, it is likely that a block of non-switchers will remain and profit maximising firms will retain an incentive to charge these disengaged consumers higher prices.⁴⁷

22. The same submission suggested alternative measures to reach out to some of the least engaged customers via opt-out collective switches. We think Ofgem, housing associations and consumer bodies such as Citizens Advice would be particularly well-placed to facilitate creative engagement measures of this kind.

23. We recommend that Ofgem continues to look for creative ways to encourage customer engagement and switching, especially by working with housing associations, consumer bodies, suppliers and comparison websites to find new ways of reaching out to those who are least engaged.

Distribution networks

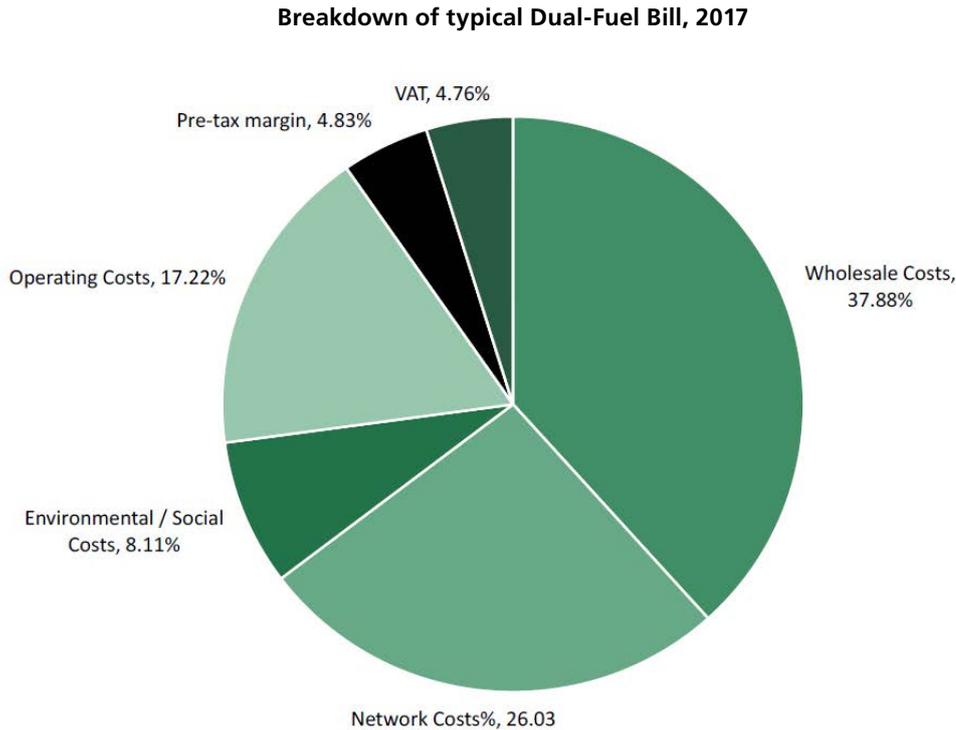
24. Network costs have received less focus than retail in the debates around energy prices and potential price controls. However, they make up for the second highest cost on a typical dual fuel energy bill (although this proportion varies from time to time and depending on the fuel considered).⁴⁸

45 Or ‘CMA remedies’ refers to a set of measures ordered by the Competition and Markets Authority following a two-year [Energy Market Investigation](#) to address some of the market failures identified by the Authority. Some of these remedies were specifically targeted at encouraging customer engagement and switching suppliers. In short, the Authority ordered for a database of disengaged customers to be created and shared with suppliers; a cap on prepayment prices; and a strengthened role for price comparison websites. For a more extensive overview of the investigation and its remedies, see House of Commons Library, [The Current Energy Market Reforms in Great Britain](#), 15 March 2017.

46 [Q388 \[Dermot Nolan\]](#)

47 Centre for Competition Policy [PL50049](#)

48 Chart and data from House of Commons Library, [Energy bills and proposals for reform](#), 5 October 2017, p6



25. Citizens Advice,⁴⁹ the Energy and Climate Change Intelligence Unit⁵⁰ and a group of Members of Parliament led by John Penrose MP⁵¹ have recently argued that Ofgem failed to predict accurately distribution network returns, thus allowing them to make unwarranted levels of profits and adding undue costs to customers' energy bills. We were concerned by these reports and we intend to monitor closely the next phase of network regulation (RIIO price control). We welcome Ofgem's announcement that energy networks should prepare for tougher price controls in the next phase.⁵² We may decide as a committee to come back to this issue in future work.

A defective market

26. Too many energy suppliers rely on a business model where they target cheap acquisition deals at engaged customers who switch, whilst making substantial profits from 'sticky' customers on expensive variable tariffs who do not or rarely switch.⁵³ We received worrying evidence that some suppliers actively work to prevent from switching onto another good-value tariff customers whose fixed-term contracts are coming to an end.⁵⁴

49 Citizens Advice, [Energy Consumers' Missing Billions](#), 12 July 2017

50 ECIU, [RIIO Carnival - How new Ofgem regulations are failing to hit high network company profits](#), January 2018

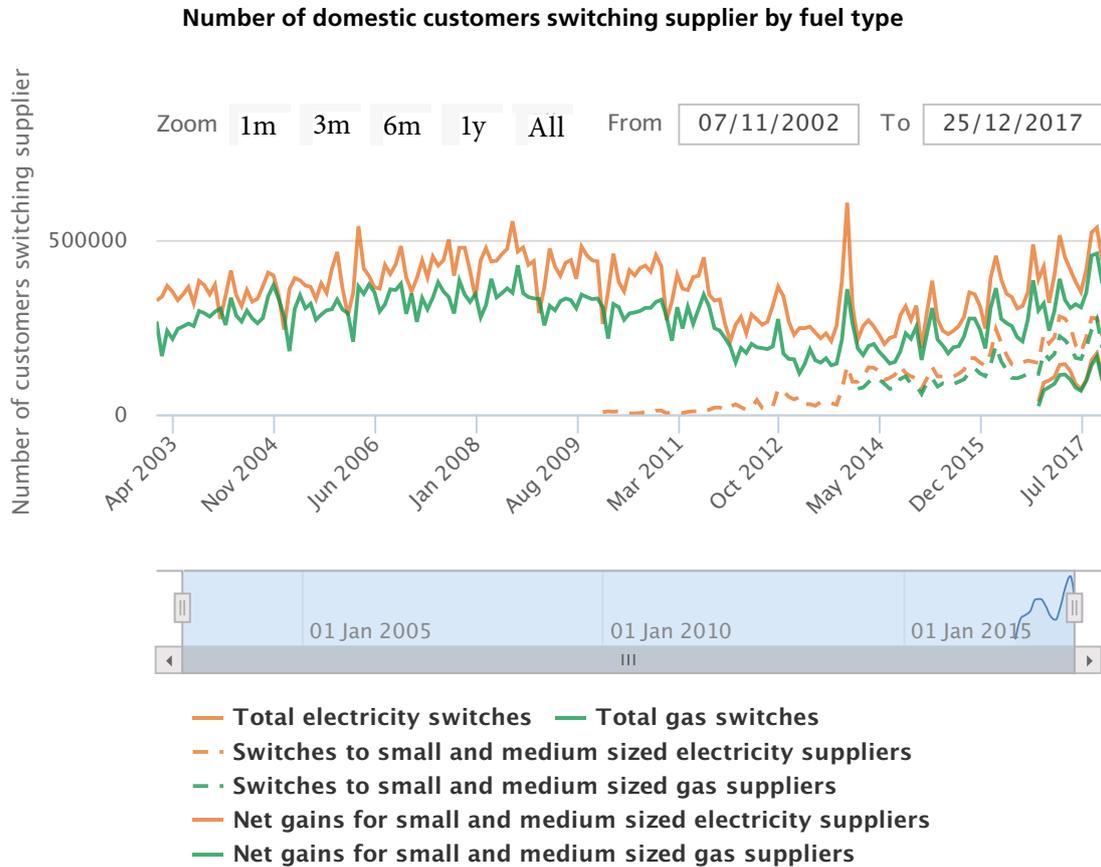
51 John Penrose Blog, [John Penrose MP demands 'sleeping' energy regulator pulls plug on £7.5bn power rip-off](#), 22 January 2018

52 Ofgem, [Energy networks should prepare for tougher price controls](#), 12 July 2017

53 As above, p6; see also oral evidence taken on 17 October 2017, HC (2017-19) 470, [Qq46-50 \[Sarwjit Sambhi\]](#)

54 Octopus Energy [PLS0035](#)

27. Despite the Competition and Markets Authority remedies and other measures aimed at increasing customer engagement and switching, switching rates amongst domestic energy customers have remained stubbornly low despite a peak in 2014 and recent moderate increases.⁵⁵



28. We were particularly concerned by recent reports⁵⁶ of Big Six customers being put on hold for up to 20 minutes when contacting their supplier, considering that 37 per cent of all customers of the Big Six have been on an SVT for more than three years and 58 per cent of all households have only switched supplier once or not at all.⁵⁷ Citizens Advice confirmed that energy generates a huge caseload: they provided help with energy issues to 8,000 vulnerable customers in 2017 and 500 people a day contact them for help with energy matters.⁵⁸

29. **Pricing practices through which some suppliers ensure that customers at the end of their fixed-term contracts do not benefit from the best available deals are fundamentally incompatible with the principle of fairness.**

55 Ofgem, Data Portal, [Retail market indicators](#), Switching and consumer experience, [Number of domestic customers switching supplier by fuel type \(GB\)](#), as of December 2017

56 'Big Six energy firms keeping callers on hold for more than 20 minutes', The Times, 16 January 2018

57 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), 29 November 2017, 11 December 2017, para.17

58 Business, Energy and Industrial Strategy Committee, [Letter from Citizens Advice on the pre-legislative scrutiny of the gas and electricity bill](#), 20 December 2017, published 10 January 2018

30. This is consistent with the conclusion from the Competition and Markets Authority’s Energy Market Investigation that domestic energy customers of the ‘Big Six’⁵⁹—who have between 41 per cent and 71 per cent of their customer bases on a variable tariff⁶⁰—were charged on average £1.4 billion a year in “excessive prices” between 2012 and 2015.⁶¹ The Authority refers to it as the “customer detriment”. We reviewed the methodology used by the Authority to calculate this figure⁶² and noted that no appeal was made⁶³ against the final findings despite strong criticisms.⁶⁴ **In the absence of any appeal against the Competition and Markets Authority’s findings and after review of the Authority’s methodology, we were unconvinced by criticisms of the £1.4 billion annual customer detriment figure. We found no valid reason to question this figure.**

31. The Competition and Markets Authority also found that “a large part of the detriment we have observed in the form of high prices is likely due to inefficiency rather than excess profits.”⁶⁵ Ofgem recently estimated that the Big Six make 26 per cent of their gross profit on SVT customers, as opposed to 14 per cent from fixed-term tariff customers.⁶⁶ This led the regulator to conclude that

if SVT prices were reduced so that they provided the same gross profit margin as fixed tariffs, then suppliers would have made a 6 per cent loss, unless suppliers could significantly reduce their operating costs.⁶⁷

32. The Authority estimated that a “normal” level of profits for suppliers who operate efficiently is 1.25 per cent. We were therefore concerned to learn that the Big Six made profit margins well above that benchmark in recent years.⁶⁸ The same suppliers also defied Ofgem’s warnings⁶⁹ against unjustified tariff increases by raising their prices in 2017.⁷⁰ Dermot Nolan told us that “in a competitive market that is working effectively, you would not expect to see huge differentials”⁷¹ between the highest and the lowest tariffs available in the market. The Government said this market “is not working for all consumers”.⁷² **We share the Government’s view that the energy market “is not working for all consumers” and is yet to demonstrate effective competition and fairness. We agree with Ofgem’s view that in a truly competitive market that works for all consumers and is fair, the differential between the highest and lowest comparable tariffs should be smaller.**

59 E.ON UK, Centrica, SSE, npower, EDF Energy, ScottishPower are commonly referred to as ‘the Big Six’ as they are the six largest suppliers in the domestic GB energy market.

60 Ofgem, [League table: latest trends in ‘standard variable’ tariffs \(September 2017 data\)](#), 20 December 2017

61 Competition and Markets Authority, Energy market investigation, [Summary of final report](#), para.194

62 [Qq46-51](#); Competition and Markets Authority, Energy market investigation, [Final report](#), Chapter 10. Analysis of detriment and [Appendix 10.2: Benchmark analysis of domestic energy bills](#), 24 June 2016

63 [Q47](#) [SimeonThornton]

64 [Qq2-6](#) [Stephen Littlechild, Stephen Smith]; Octopus Energy [PLS0035](#); Professor Stephen Littlechild [PLS0003](#); uSwitch.com [PLS0033](#); ScottishPower [PLS0034](#); Centrica plc [PLS0022](#)

65 Competition and Markets Authority, [Energy Market Investigation, Final report](#), para.10.29

66 Ofgem, [State of the energy market 2017](#), p31

67 As above

68 Ofgem, [Understanding the profits of the large energy suppliers, Aggregate profits in %: supply segment, as of August 2017](#)

69 ‘Ofgem warns Big Six firms against raising energy prices’, The Times, 20 January 2017

70 House of Commons Library, [Energy bills and proposals for reform, CBP 8081](#), 5 October 2017, pp6-7

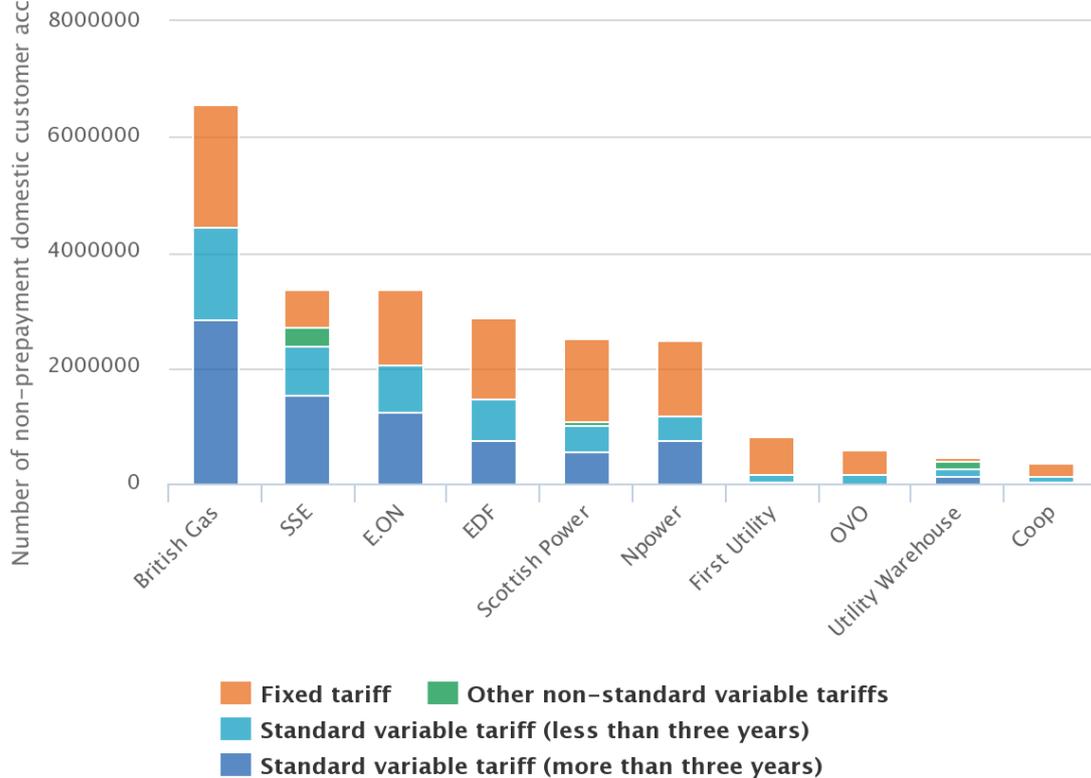
71 [Q345](#)

72 [Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), Department for Business, Energy & Industrial Strategy, 12 October 2017, Foreword

The Big Six

33. Ofgem recently published its standard variable tariff league table in which SSE, Centrica and E.ON had the largest number of customers on SVTs.⁷³ Between April and September 2017, at the height of political discussions around price caps, the Big Six have only seen the number of customers on SVTs fall by three to nine per cent, some not at all.⁷⁴ Data compiled by Ofgem (see chart below)⁷⁵ shows that the largest suppliers still have a long way to go in reducing the share of their customer bases on poor-value tariffs.

Number of non-prepayment domestic customer accounts by supplier: Standard variable, fixed and other tariffs (GB)



34. Some of these suppliers recently announced that they would take steps towards reducing the number of SVT customers in the future:

- E.ON was first in announcing that in 2018 they would stop rolling automatically onto an SVT customers who have a smart meter and whose fixed-term deal comes to an end.⁷⁶ This announcement will not affect the two million non-prepayment customers⁷⁷ who are already on an SVT, as was established at our oral evidence session.⁷⁸

73 Ofgem, [Standard variable tariffs: Latest trends at September 2017](#), 20 December 2017

74 As above

75 Ofgem, Data Portal, Retail market indicators, [Number of non-prepayment domestic customer accounts by supplier: Standard variable, fixed and other tariffs \(GB\)](#), accessed 29 January 2018

76 E.ON Blog, [Why we're saying goodbye to our standard variable tariff](#), 21 September 2017

77 Ofgem, [Standard variable tariffs: Latest trends at September 2017](#), 20 December 2017

78 [Q234](#) [Chair]

- SSE announced⁷⁹ in November 2017 that from April 2018 they would no longer automatically roll over customers whose fixed-term deals come to an end onto an SVT. These customers will instead be rolled onto another fixed-term deal that is either equivalent or cheaper. This announcement will not affect the 2.4 million SSE customers⁸⁰ who are already on SVTs and default tariffs.
- Centrica, the supplier with the largest amount of SVT customers, announced its seven steps to reduce this number.⁸¹ These steps are a mixture of obligations they already have as a regulated supplier (such as making energy bills simpler and easy to understand; engaging customers to switch to a better tariff at least once a year); things other suppliers are already offering to their customers (such as introducing fixed-term tariffs that have no exit fees or contacting their customers at least once a month⁸²); and crucially, an announcement that they would stop offering SVTs to new customers on fixed-term deals and would instead roll them onto another emergency fixed-term tariff with no exit fee. This offer will be limited to new customers and will therefore not address the 4.5 million⁸³ Centrica customers already on an SVT.

35. We assessed the suppliers' announcements about the steps they intended to take to reduce the number of customers on poor-value tariffs and concluded that they were insufficient to address the scale of the problem. We also noted the lack of any announcements on the part of the other three Big Six suppliers (ScottishPower, EDF Energy, npower) who still have large numbers of customers on poor-value tariffs. We believe the feebleness of these announcements shows a clear lack of will on the part of the Big Six to take the necessary steps towards redressing existing customer detriment.

36. We conclude that the Big Six have brought this policy intervention upon themselves by raising their prices in 2017 and by failing to take effective action against the overcharging of their customers on default and standard variable tariffs.

37. Stakeholders opposed to price cap policies argued that customers who do not engage with the market should expect to pay more for their energy.⁸⁴ We were also told that consumers in the UK were already “getting a fair deal” and prices reflected the time they were willing to spend looking for better deals, as in many other markets.⁸⁵

38. The Secretary of State told us otherwise: in his view, even “lazy” or “busy” consumers should not have to go through the process of “defending themselves against what the CMA has found is an excessive price.”⁸⁶ In the Government’s view, “this is why this intelligent intervention is required.”⁸⁷

79 SSE, [Steps to reduce number of customers on standard variable tariffs](#), 6 November 2017;

80 Ofgem, [Standard variable tariffs: Latest trends at September 2017](#), 20 December 2017

81 Centrica, [Centrica sets out proposals to deliver a fairer and sustainable energy deal for customers](#), 20 November 2017

82 [Q128 \[Ed Kam\]](#)

83 Ofgem, [Standard variable tariffs: Latest trends at September 2017](#), 20 December 2017

84 [Q127 \[Michael Lewis\]](#)

85 [Q7 \[Stephen Littlechild\]](#)

86 Oral evidence on 1 November 2017, HC (2017–19) 470, [Qq127-128](#)

87 [Q426 \[Claire Perry\]](#)

39. **The Committee agrees with the Secretary of State’s view that customers who are not able to shop for better deals should not be overcharged unfairly and that even customers who are able to switch tariffs but fail to do so should not be penalised disproportionately.**

40. **Energy is “special”: consumers should not be expected to constantly defend themselves from excessive prices. We conclude that government intervention is justified when markets fail to deliver fair outcomes for consumers and have a disproportionate impact on consumers who are the least able to protect themselves from overcharging.**

41. **There is a strong case for the Government’s Bill and the policy of introducing an intelligent, effective price control policy that will have the immediate impact of lowering the highest prices for millions of consumers and improve fairness in the delivery of an essential good.**

3 The case for an absolute price cap

Relative or absolute price cap?

42. The Government’s primary goal, which we support, is to reduce quickly and significantly the overcharging of the millions of customers on standard variable and default tariffs identified by the Competition and Markets Authority. To this end, the Government decided that the price cap should be an absolute one and the draft Bill is framed accordingly.⁸⁸

43. Some of the evidence we heard was strongly in favour of achieving this outcome with a relative cap. We heard evidence from several stakeholders that a relative price cap would be less disruptive for the market and would allow efficient suppliers to thrive.⁸⁹ For instance, John Penrose MP told us that a relative cap

restores the link between the prices which companies advertise in the marketplace and those which they charge the majority of their customers [...]; allows more price competition [...]; doesn’t limit the number & type of tariffs [...]; encourages innovation & fresh thinking and will reward efficient business models—those that maintain high SVTs will rapidly lose market share⁹⁰

44. Some suppliers, such as Octopus Energy and Ecotricity, argued that an absolute cap would not solve the issue of “tease and squeeze”⁹¹ (or “price gouging”⁹²) by which suppliers allegedly

offer far cheaper energy prices to new customers than they do to existing ones. [...] The incumbent customer base is used to subsidise the energy price of new customers.⁹³

45. Data from Octopus Energy suggests that some challenger firms would fare well under a relative price cap.⁹⁴ However, we were concerned by the evidence from Ofgem, the Government, Citizens Advice and others about the risks associated with relative price caps.⁹⁵ They convincingly argued it would bear the following risks:

88 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, para.33

89 Mr John Penrose [PLS0019](#), Ecotricity [PLS0015](#), Octopus Energy [PLS0035](#), ScottishPower [PLS0034](#), Cornwall Insight [PLS0027](#), Utilita Energy Ltd [PLS0001](#), Hudson Energy Supply UK Limited [PLS0007](#)

90 [PLS0019](#), p2

91 [PLS0035](#)

92 [PLS0015](#), para.2.1

93 As above

94 [PLS0035](#), figure 8

95 Rt Hon Caroline Flint [PLS0041](#), Centre for Competition Policy [PLS0049](#), Ofgem [PLS0045](#), Energy Policy Group [PLS0036](#), First Utility [PLS0004](#), OVO Energy [PLS0008](#), Bristol Energy [PLS0002](#), Citizens Advice [PLS0021](#), Co-op Energy [PLS0030](#), Martin Cave [PLS0044](#), uSwitch.com [PLS0033](#), Utility Warehouse Ltd [PLS0020](#); Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, para.35

(i) It may have a limited impact on the SVT prices of the Big-6; (ii) It poses a greater risk of distorting competition in the Fixed Term Tariff market; and (iii) The choice of what price differential to allow is essentially arbitrary. We want to make clear that the notion that a basic relative cap represents “less intervention” is false; the extent of intervention should be based on the impact of the intervention rather than the number of pages of text required to explain the intervention.⁹⁶

46. Even more worryingly, the same submissions argued a relative cap risked substantially increasing prices for many consumers and more so than an absolute cap. This is because, as explained by the Centre for Competition Policy

Different firms have different proportions of their consumers on FTTs⁹⁷ and SVTs. The Big-6, being the former incumbents, have a much greater proportion of their customers on SVTs, which are the more profitable product. To protect their profits, and knowing that their SVT customers are unlikely to switch, the Big-6 are likely to comply with a basic relative cap by increasing their FTT prices by significantly more than they reduce their SVT prices. While increasing their FTT prices means they will lose some of these customers, the profits lost through this would be lower than from an equivalent reduction in SVT prices.⁹⁸

47. We agree with this argument and think it likely predicts what would happen under a relative cap.

48. We acknowledge and accept the warnings we received that some prices may increase under an absolute price cap as early evidence from the prepayment cap suggests it leads to some cheap deals exiting the market.⁹⁹ However, we concluded that the greater risks of a price increase on both the highest and the lowest tariffs under a relative cap could not be reconciled with the aim of this Bill which is to reduce overcharging. Moreover, we believe that on balance the risks associated with an absolute cap are outweighed by the greater risks associated with a relative cap and the immediate benefit to consumers on poor-value tariffs.

49. We believe an absolute cap is the best price control to achieve the specific goal of removing overcharging for 12 million customers immediately and achieving greater fairness. It is right that the Bill does not allow for a relative cap to be implemented.

Lessons from Northern Ireland

50. The electricity price cap in Northern Ireland has allowed for switching rates to be as high as those in Great Britain and for competition to flourish with four suppliers currently competing in the market to beat the incumbent’s capped price. It has also allowed for a price differential to remain, meaning that customers still have some incentives to switch

96 Centre for Competition Policy [PLS0049](#), p13

97 ‘Fixed term tariffs’

98 Centre for Competition Policy [PLS0049](#), p13

99 [Q388](#), [Q409](#) [[Dermot Nolan](#)]

and that “regulation and competition can usefully co-exist.”¹⁰⁰ We acknowledge that only careful conclusions can be drawn from international examples as, in the words of a supplier:

The truth is that a mass-market GB price cap will be unique. Most countries with price caps have small, undeveloped and uncompetitive markets, introducing price caps as a staging post on the way to a more full market liberalisation.¹⁰¹

51. Nevertheless, we believe the Northern Irish case is the most directly applicable to the GB energy market amongst the many international comparisons cited in the evidence. **We conclude from the Northern Ireland experience that “regulation and competition can usefully co-exist” under an absolute price cap and maintain incentives to compete on prices.**

Alternative measures

52. There was some evidence that alternatives to price controls (e.g. collective switching, engagement measures, standing charge cap) would be as effective as an absolute cap in swiftly reducing overcharging.¹⁰² We agree with advocates of engagement measures that these are key to increasing switching and though they are slow to make a difference, they will be beneficial for the market in the long term.¹⁰³

53. However, switching is not an end in itself; nor is it the panacea for effective competition.¹⁰⁴ It is only one of several indicators of a competitive market.¹⁰⁵ There is confusing evidence on the link between price differentials — which are a normal feature of a competitive market — and switching rates. Although “saving money” is the biggest motivation for switching,¹⁰⁶ switching rates and average price difference do not appear to be positively correlated.¹⁰⁷ Switching rates are increasing¹⁰⁸ but they are still too low to have a lasting influence on driving prices down for consumers on standard variable and default tariffs.

54. We conclude that relying on engagement measures to deliver more effective competition via switching is unlikely to be sufficient. It will not deliver enough fairness for those customers that are currently on poor-value tariffs because they do not engage and the cap by itself will not help disengaged customers switch any more than they already do.¹⁰⁹ As a result, engagement measures have an important part to play alongside other policy interventions aimed at other issues in the market such as overcharging.¹¹⁰ We hope Ofgem will continue to implement the Competition and Markets Authority remedies alongside implementing the Government’s absolute price cap.

100 Consumer Council [PLS0047](#), para.8.3

101 First Utility [PLS0004](#), p5

102 [Q334](#) [Dermot Nolan]

103 [Q54](#) [Lesley Ainsworth]; [Qq124-127](#) [Michael Lewis]; [Q130](#) [Sarwjit Sambhi]; [Which? PLS0016](#)

104 Centre for Competition Policy [PLS0049](#); [Qq424-426](#) [Claire Perry]

105 [Q345](#) [Dermot Nolan]

106 Ofgem, [State of the energy market 2017](#), p24

107 Citizens Advice [PLS0021](#), Figure 6

108 Energy UK, [Energy switching hits record high in 2017](#), 10 January 2018

109 [Q336](#) [Dermot Nolan]

110 Professor Martin Cave OBE [PLS0044](#), [MoneySuperMarket.com PLS0024](#)

55. We support the Competition and Markets Authority's Energy Market Investigation remedies and we acknowledge Ofgem's role in referring the domestic energy market to the Authority for investigation. However, we conclude from the evidence that the market will only deliver fairer outcomes for all consumers once it combines both stronger engagement and reduced overcharging. Thus, in our view, alternatives to price controls and the Competition and Markets Authority remedies are positive for engagement but they do not go far enough to remove the customer detriment quickly and effectively, especially for non-prepayment vulnerable customers.

Timing for the Bill

56. Ofgem have told us that they would need at least five months to put a cap in place from the moment the Bill receives Royal Assent.¹¹¹ We welcome the Minister's intention to see the Bill receive Royal Assent in time for the cap to be in place by winter 2018 but recognise that there are other legislative priorities too.¹¹² *The Government should provide protection to customers in time for winter 2018 by seeking to ensure that the Bill receives Royal Assent before parliamentary summer recess 2018.*

57. We heard suppliers' and others' concerns about the lack of appeal rights to the Competition and Markets Authority.¹¹³ However, we believe such rights would be used by suppliers to delay the implementation of a cap that is not the result of a discretionary Ofgem decision but stems directly from a government intervention.¹¹⁴ We agree with Ofgem's view that judicial review is a common and satisfactory appeal route for energy decisions, even highly technical ones.¹¹⁵ We also note that if the court felt that additional technical expertise were necessary, it could sit with assessors. We contend the view that judicial review appeals would delay the implementation of a cap more than an appeal to the Competition and Markets Authority as appeals to the Authority can be subject to judicial review themselves. **We conclude that suppliers do not need appeal rights to the Competition and Markets Authority for this Bill. This could unnecessarily delay further the successful implementation of the cap.**

111 [Q421 \[Dermot Nolan\]](#)

112 [Qq422-423 \[Claire Perry\]](#)

113 [ScottishPower PLS0034](#), [uSwitch.com PLS0033](#), [Co-op Energy PLS0030](#), [Confederation of British Industries PLS0029](#), [Energy UK PLS0028](#), [Centrica plc PLS0022](#), [E.ON PLS0014](#), [EDF Energy PLS0012](#), [Professor Stephen Littlechild PLS0003](#), [Utilita Energy Ltd PLS0001](#); [Business, Energy and Industrial Strategy Committee, Letter from Energy UK Chief Executive to the Chair relating to Tariff Cap Bill, 29 January 2018, published 31 January 2018](#)

114 [Octopus Energy PLS0035](#); 'Energy challenger warns wider energy price cap appeal rights could delay implementation', [City AM](#), 31 January 2018

115 [Business, Energy and Industrial Strategy Committee, Letter from Ofgem Chief Executive to the Chair relating to pre-legislative scrutiny of the Tariff Cap Bill, 22 January 2018, published 23 January 2018](#)

4 Recommended changes to the Bill - How the cap is set

Subsection 1(6): the criteria to set the cap

Box 1: Subsection 1(6)

Under subsection 1(6), when setting the cap Ofgem is required to have regard to the five following matters:

- (a) the need to protect existing and future domestic customers who pay standard variable and default rates;
- (b) the need to create incentives for holders of supply licences to improve their efficiency;
- (c) the need to set the cap at a level that enables effective competition for domestic supply contracts;
- (d) the need to maintain incentives for domestic customers to switch to different domestic supply contracts;
- (e) the need to ensure that holders of supply licences who operate efficiently are able to finance activities authorised by the licence.

Source: [Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), Department for Business, Energy & Industrial Strategy, 12 October 2017

58. Some of the evidence we received argued that the five subsections in subsection 1(6) were ambitious and may be hard to achieve simultaneously: many stakeholders thought it unlikely that any price control or policy could achieve all five aims at once or that it could do so when the cap is first introduced.¹¹⁶ Some stakeholders even argued that some of the subsections were incompatible with one another or inconsistent with an absolute price cap. For instance, one submission argued that the cap would fail to meet subsection 1(6)(a) if it led to engaged customers facing higher prices.¹¹⁷ These arguments rely on the expectation that an absolute price cap will leave no room for competition on tariffs below the cap. Others were more optimistic and argued that, if carefully weighed, all five conditions could be met in the short or long term.¹¹⁸

59. We previously concluded from the Northern Ireland experience that, if set at the right level and with sufficient headroom, an absolute price cap would allow regulation and competition to co-exist, though it may prove challenging for suppliers that are not currently operating efficiently.¹¹⁹ Ofgem may also be challenged with judicial review on the way it will define an “efficient” supplier to accommodate the various kinds of suppliers

116 MoneySuperMarket.com [PLS0024](#), Which? [PLS0016](#), E.ON [PLS0014](#), EDF Energy [PLS0012](#), uSwitch.com [PLS0033](#), David Osmon [PLS0006](#), First Utility [PLS0004](#), Centrica plc [PLS0022](#), Centre for Competition Policy [PLS0049](#), ScottishPower [PLS0034](#)

117 Centre for Competition Policy [PLS0049](#)

118 Citizens Advice [PLS0021](#), Utility Warehouse Ltd [PLS0020](#), OVO Energy [PLS0008](#), First Utility [PLS0004](#)

119 Professor Martin Cave OBE [PLS0044](#)

operating in the market when setting the cap. Some stakeholders have argued in the past that the Competition and Markets Authority and Ofgem had miscalculated the costs they faced and what an efficient supplier was.¹²⁰

60. **We believe the Northern Ireland experience and the evidence show that it will be possible, if challenging, for Ofgem to set a cap that meets subsections 1(6)(a), 1(6)(b) and 1(6)(e). Some suppliers may struggle to adapt or challenge with judicial review how Ofgem will measure the costs of an “efficient supplier”.**

61. Subsection 1(6)(c) is not precisely defined in the Bill and “the conditions for effective competition” could be interpreted in different ways by various stakeholders.¹²¹ The Minister and Ofgem were both confident that the definition of “effective competition” should be left with the regulator to adjudicate and should not turn into a box-checking exercise.¹²² **We support the Government’s view that the determination of “the conditions for effective competition” in subsection 1(6)(c) should be left with Ofgem.**

62. The evidence suggested that subsection 1(6)(d) could prove challenging to achieve as switching rates may go down, at least at first, as a result of the cap being introduced.¹²³ This could therefore make Ofgem vulnerable to legal challenges which could hinder the implementation of the cap if they were successful. ***The Government should work with Ofgem to amend the wording of the Bill to make it as resistant as possible to successful legal challenge to subsection 1(6)(d).***

63. Suppliers of different sizes and operating with different business models face very different costs. All suppliers are also subject to the fluctuations of wholesale, network and policy costs. A price cap will not be able to insulate consumers against unpredictable global price fluctuations. An efficient supplier should be able to hedge for these fluctuations, but we think the price cap will need to be updated regularly to reflect these changes and keep up with the market.

64. ***We recommend that the Bill be amended to include a requirement that Ofgem review the level at which the cap is set at least every six months to keep up with changes in suppliers’ costs and consumer engagement.***

65. **We were unconvinced by the argument that the five goals in subsection 1(6) are incompatible. We acknowledge that they are challenging and may not all be achievable at once but we believe that the current wording of the Bill, with slight amendment, allows Ofgem to prioritise and weigh them carefully when setting the cap.**

66. ***To deter legal challenges that would delay unnecessarily the implementation of the cap, we recommend that the Government clarify in the Bill that Ofgem will not be required to set a cap that will meet all five subsections simultaneously, though it may eventually do so. This would be consistent with the main aim of the Bill of reducing overcharging, not increasing switching.***

120 Centrica plc [PLS0022](#), E.ON [PLS0014](#), ScottishPower [PLS0034](#), npower [PLS0031](#); SSE [PLS0052](#)

121 uSwitch.com [PLS0033](#),

122 [Qq424-427](#) [Claire Perry]; [Qq345-350](#) [Dermot Nolan]

123 [Qq345-346](#); [Q367](#)

5 Recommended changes to the Bill - The green tariff loophole

Clause 3: green electricity tariffs

67. Green electricity tariffs are exempt from the cap under clause 3. This is because although these tariffs are usually more expensive, they are actively chosen and purchased by consumers who want to support the generation of renewable energy.¹²⁴ **We accept the argument that customers should be allowed to pay more for renewable electricity if they actively decide to do so and if the tariffs in question truly encourage renewable generation. We support the exemption of green electricity tariffs from the cap.**

68. However, several submissions raised concerns about the exemption as currently drafted, saying it could create an opportunity for suppliers to game the system and avoid the cap if the bar for what constitutes a green tariff was not set at a higher standard. These stakeholders argued that the current standards to be met to sell energy as a green tariff were not stringent enough and would allow suppliers to re-brand SVTs as loosely environmental tariffs to avoid the cap.¹²⁵ Ofgem expressed similar concerns¹²⁶ and reiterated them in oral evidence to us in January.¹²⁷

69. The Government did not signal any intention to close the loophole but welcomed the Committee's views on how the risk of gaming could be lessened.¹²⁸ The Minister told us that to avoid this loophole being exploited, Ofgem would have to monitor which tariffs are truly green (providing environmental benefits) and which ones are not.¹²⁹ We were concerned by Dermot Nolan's view that the "ways to check whether a tariff is green" or not were "imperfect".¹³⁰

70. **We share stakeholders' view that the Bill as currently drafted allows for unscrupulous suppliers to game the system and avoid the cap by moving customers on poor-value tariffs onto loosely-defined green tariffs. The Government should work with Ofgem to strengthen the definition, standards and checks for electricity tariffs with environmental claims so the system cannot be gamed in this fashion and undermine the success of the cap.**

71. **We recommend that the Bill be amended to make clear that attempts to circumvent the cap by offering tariffs that do not provide substantial environmental benefits and were not actively chosen by customers will be in breach of the legislation. Ofgem should be alert to and be prepared to stop any form of pricing that is designed to circumvent the cap.**

124 [Q383](#) [Chair]; Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), 11 December 2017, para.24

125 Good Energy [PLS0046](#), Rt Hon Caroline Flint [PLS0041](#); [Q283](#) [Ed Kamm]; [Qq285-286](#) [David Bird; Patrick New]

126 [PLS0045](#)

127 [Q374](#) [Dermot Nolan]

128 [Qq489-490](#) [Claire Perry]; [Q286](#) [Patrick New]

129 [Q489](#) [Claire Perry]

130 [Q374](#) [Dermot Nolan]

Green gas tariffs

72. Some stakeholders suggested that the same exemption should be extended to green gas tariffs¹³¹ as many customers on green tariffs are on dual-fuel tariffs.¹³² We understand from the evidence that in order to include green gas tariffs in the exemption Ofgem would be required to create a green gas accreditation.¹³³ We heard no valid reason not to remove this obstacle and ensure that dual-fuel and gas tariffs that are chosen actively by customers for their environmental characteristics are included within the exemption. ***The Government should explain its rationale for not exempting green gas tariffs under clause 3.***

73. ***The Government should respond to the concerns expressed by stakeholders in evidence to us on the detriment to investment in renewable generation and green gas tariff customers of not exempting these tariffs.***

74. ***The Government should work with Ofgem to create the necessary accreditations to include green dual-fuel and green gas tariffs within the price cap exemption. This should be done without repeating the gaming risks of the green electricity tariff exemption.***

131 Good Energy [PLS0046](#),

132 Good Energy [PLS0046](#), Energy UK [PLS0028](#), Co-op Energy [PLS0030](#), Ecotricity [PLS0015](#), Energy Policy Group [PLS0036](#)

133 Ecotricity [PLS0015](#), para.1.2

6 Measuring success and removing the cap

Clauses 6 and 7: the sunset clause

75. The Bill’s sunset clause is set at 2023 but the cap could be lifted as early as 2020 depending on Ofgem’s annual reviews and the Secretary of State’s assessment of whether the “conditions are in place for effective competition”.¹³⁴

76. We heard some evidence suggesting that 2023 was an arbitrary date¹³⁵ or that the Bill should not have a sunset clause and that the cap should last until the market is fixed.¹³⁶ However, the majority of the evidence, including the Government’s,¹³⁷ pointed towards a temporary intervention.¹³⁸ The Government told us the sunset clause was a guarantee that it does not end up “in the business of setting energy prices over the long term”¹³⁹ as it remains committed to market competition.¹⁴⁰

77. We support the Government’s view that the price cap should only be a temporary measure. As a result, we believe that removing the sunset clause would make removing the cap too challenging and would put the Government unduly in charge of setting energy prices for the foreseeable future. We favour a return to unbridled competition once the customer detriment is removed.

Clauses 6 and 7: the conditions for effective competition

78. The Minister told us she was wary of defining how “the conditions for effective competition” would be measured although she hoped it would be one where loyalty is rewarded, where the detriment is reduced and where vulnerable customers are protected.¹⁴¹ The Government decided to make Ofgem responsible for assessing whether changes in the market under the cap would lead to “the conditions for effective competition” because of the regulator’s expertise in matters of competition. Dermot Nolan listed some of the indicators the regulator may use for this assessment.¹⁴²

79. As previously mentioned, the evidence from many stakeholders makes it clear that “effective competition” could be measured in different ways and that this could be a point on which the Government’s policy will be challenged in the courts. However, the Minister explained that giving too strict a definition of “effective competition” could “stimulate unintended consequences, or be incredibly prescriptive about what the market should

134 [Draft Domestic Gas and Electricity \(Tariff Cap\) Bill](#), subsection 6(6)

135 Centre for Competition Policy [PLS0049](#),

136 Citizens Advice [PLS0021](#), [Q333](#) [Hayden Wood; Patrick New], [Q79](#) [Peter Smith]

137 Department for Business, Energy & Industrial Strategy, [Impact Assessment: Draft Domestic Gas and Electricity \(Tariff Cap\) Bill, 29 November 2017](#), published 11 December 2017; Department for Business, Energy and Industry Strategy [PLS0038](#)

138 Ofgem [PLS0045](#); Professor Martin Cave OBE [PLS0044](#); Energy Policy Group [PLS0036](#); ScottishPower [PLS0034](#); uSwitch.com [PLS0033](#); Co-op Energy [PLS0030](#); Confederation of British Industries [PLS0029](#); Cornwall Insight [PLS0027](#); MoneySuperMarket.com [PLS0024](#); Centrica plc [PLS0022](#); Mr John Penrose [PLS0019](#), Which? [PLS0016](#); E.ON [PLS0014](#); OVO Energy [PLS0008](#); First Utility [PLS0004](#); Bristol Energy [PLS0002](#); SSE [PLS0052](#)

139 [Q458](#) [Claire Perry]

140 [Q431](#) [Claire Perry]

141 [Qq424-427](#)

142 [Q345](#)

look like, because there is so much change and innovation.”¹⁴³ **We believe that setting a definition of “the conditions for effective competition” before setting the cap could create incentives for suppliers to game the system or treat the cap as a box-checking exercise rather than going above and beyond their obligations. It would also risk creating unnecessary opportunities for legal challenges.**

80. It is right that the decision to keep or remove the cap is left to the Secretary of State, based on Ofgem’s assessment, as the Government is responsible for introducing the legislation and setting its objectives. We believe that Ofgem have the required expertise to set and measure indicators of effective competition and make the appropriate recommendation to the Secretary of State.

81. *We recommend that the Secretary of State base the decision to keep or lift the cap on the minimum requirements that overcharging and the differential are substantially reduced, fairness is improved, and vulnerable customers are protected.*

Clause 6: Smart meters

82. The Bill’s sunset clause coincides with the sunset clause for the Smart Meters Bill currently before the House¹⁴⁴ and the first review date for the cap is 2020 — the date by which the Government also intends the smart meter rollout to be completed. The Tariff Cap Bill appears to have been timed to fit alongside the smart meter rollout and benefit from the changes it will bring to the market. In subsection 6(2) Ofgem is explicitly required to “consider the extent to which progress has been made installing smart meters for use by domestic customers” when making its assessment of the market.

83. However, the Government has acknowledged that smart meters are “an enabler, not a determinant of switching”.¹⁴⁵ The evidence cited by the Government¹⁴⁶ shows that small increases in likelihood of switching amongst owners of smart meters are linked to customers who already are more likely to be engaged.¹⁴⁷ The witnesses we heard from were also sceptical about relying on smart meters to transform customers’ likelihood of shopping for the best deal.¹⁴⁸

84. Given the slim evidence that smart meters have any substantial impact on customer switching rates, we conclude that it would be unwise to rely solely on the smart meter rollout once the cap is lifted to maintain effective competition in the market.

85. *Once the cap is lifted, the Government and Ofgem should take any necessary measures to ensure that the elimination of overcharging remains in place in the long term and that suppliers are not able to go back to their overcharging and cross-subsidising practices. Engagement measures currently rolled out should also be maintained to keep encouraging customers to switch suppliers.*

143 [Q426](#)

144 [Smart Meters Bill 2017–19](#)

145 [Q461 \[Claire Perry\]](#)

146 [Q462 \[Dan Monzani\]](#)

147 Ofgem, [Consumer engagement survey 2017 report](#), 21 September 2017, p10

148 [Q230 \[Ed Kamm\]](#); [Qq316-317 \[Hayden Wood\]](#); [Q319 \[Patrick New\]](#); [Q340 \[Dermot Nolan\]](#)

Conclusions and recommendations

The cost of inaction

1. We accept the evidence from Ofgem, consumer bodies and the Minister that vulnerable customers will benefit most from the Tariff Cap Bill and will, in all likelihood, need some form of price protection for the foreseeable future, including after the Government's price cap is lifted. *We recommend that the Government provides details on its plans to protect vulnerable customers from overcharging when Ofgem's safeguard tariff and the Government's price cap are lifted.* (Paragraph 11)
2. We agree with Ofgem that legislative obstacles to data-sharing of vulnerable customer data held by government with energy suppliers need to be removed so as to give vulnerable customers better protection. *We recommend that the Government commits to removing these obstacles by seeking to amend section 36(3) of the Digital Economy Act 2015 in time for winter 2018.* (Paragraph 13)
3. We conclude that Ofgem have failed customers, especially vulnerable customers, by being overly cautious and reactive on the issue of poor-value standard variable and default tariffs. They should have removed the obligation to move customers at the end of their fixed-term contracts on default tariffs sooner and set mandatory targets for suppliers to take customers off standard variable tariffs when it was still appropriate to do so. *We urge Ofgem to be faster and more proactive in using their extensive powers to protect customers from overcharging in the future.* (Paragraph 20)
4. *We recommend that Ofgem continues to look for creative ways to encourage customer engagement and switching, especially by working with housing associations, consumer bodies, suppliers and comparison websites to find new ways of reaching out to those who are least engaged.* (Paragraph 23)
5. Pricing practices through which some suppliers ensure that customers at the end of their fixed-term contracts do not benefit from the best available deals are fundamentally incompatible with the principle of fairness. (Paragraph 29)
6. In the absence of any appeal against the Competition and Markets Authority's findings and after review of the Authority's methodology, we were unconvinced by criticisms of the £1.4 billion annual customer detriment figure. We found no valid reason to question this figure. (Paragraph 30)
7. We share the Government's view that the energy market "is not working for all consumers" and is yet to demonstrate effective competition and fairness. We agree with Ofgem's view that in a truly competitive market that works for all consumers and is fair, the differential between the highest and lowest comparable tariffs should be smaller. (Paragraph 32)
8. We assessed the suppliers' announcements about the steps they intended to take to reduce the number of customers on poor-value tariffs and concluded that they were insufficient to address the scale of the problem. We also noted the lack of any announcements on the part of the other three Big Six suppliers (ScottishPower, EDF Energy, npower) who still have large numbers of customers on poor-value tariffs.

We believe the feebleness of these announcements shows a clear lack of will on the part of the Big Six to take the necessary steps towards redressing existing customer detriment. (Paragraph 35)

9. We conclude that the Big Six have brought this policy intervention upon themselves by raising their prices in 2017 and by failing to take effective action against the overcharging of their customers on default and standard variable tariffs. (Paragraph 36)
10. The Committee agrees with the Secretary of State's view that customers who are not able to shop for better deals should not be overcharged unfairly and that even customers who are able to switch tariffs but fail to do so should not be penalised disproportionately. (Paragraph 39)
11. Energy is "special": consumers should not be expected to constantly defend themselves from excessive prices. We conclude that government intervention is justified when markets fail to deliver fair outcomes for consumers and have a disproportionate impact on consumers who are the least able to protect themselves from overcharging. (Paragraph 40)
12. There is a strong case for the Government's Bill and the policy of introducing an intelligent, effective price control policy that will have the immediate impact of lowering the highest prices for millions of consumers and improve fairness in the delivery of an essential good. (Paragraph 41)

The case for an absolute price cap

13. We believe an absolute cap is the best price control to achieve the specific goal of removing overcharging for 12 million customers immediately and achieving greater fairness. It is right that the Bill does not allow for a relative cap to be implemented. (Paragraph 49)
14. We conclude from the Northern Ireland experience that "regulation and competition can usefully co-exist" under an absolute price cap and maintain incentives to compete on prices. (Paragraph 51)
15. We support the Competition and Markets Authority's Energy Market Investigation remedies and we acknowledge Ofgem's role in referring the domestic energy market to the Authority for investigation. However, we conclude from the evidence that the market will only deliver fairer outcomes for all consumers once it combines both stronger engagement and reduced overcharging. Thus, in our view, alternatives to price controls and the Competition and Markets Authority remedies are positive for engagement but they do not go far enough to remove the customer detriment quickly and effectively, especially for non-prepayment vulnerable customers. (Paragraph 55)
16. *The Government should provide protection to customers in time for winter 2018 by seeking to ensure that the Bill receives Royal Assent before parliamentary summer recess 2018.* (Paragraph 56)

17. We conclude that suppliers do not need appeal rights to the Competition and Markets Authority for this Bill. This could unnecessarily delay further the successful implementation of the cap. (Paragraph 57)

Recommended changes to the Bill - How the cap is set

18. We believe the Northern Ireland experience and the evidence show that it will be possible, if challenging, for Ofgem to set a cap that meets subsections 1(6)(a), 1(6)(b) and 1(6)(e). Some suppliers may struggle to adapt or challenge with judicial review how Ofgem will measure the costs of an “efficient supplier”. (Paragraph 60)
19. We support the Government’s view that the determination of “the conditions for effective competition” in subsection 1(6)(c) should be left with Ofgem. (Paragraph 61)
20. *The Government should work with Ofgem to amend the wording of the Bill to make it as resistant as possible to successful legal challenge to subsection 1(6)(d).* (Paragraph 62)
21. *We recommend that the Bill be amended to include a requirement that Ofgem review the level at which the cap is set at least every six months to keep up with changes in suppliers’ costs and consumer engagement.* (Paragraph 64)
22. We were unconvinced by the argument that the five goals in subsection 1(6) are incompatible. We acknowledge that they are challenging and may not all be achievable at once but we believe that the current wording of the Bill, with slight amendment, allows Ofgem to prioritise and weigh them carefully when setting the cap. (Paragraph 65)
23. *To deter legal challenges that would delay unnecessarily the implementation of the cap, we recommend that the Government clarify in the Bill that Ofgem will not be required to set a cap that will meet all five subsections simultaneously, though it may eventually do so. This would be consistent with the main aim of the Bill of reducing overcharging, not increasing switching.* (Paragraph 66)

Recommended changes to the Bill - The green tariff loophole

24. We accept the argument that customers should be allowed to pay more for renewable electricity if they actively decide to do so and if the tariffs in question truly encourage renewable generation. We support the exemption of green electricity tariffs from the cap. (Paragraph 67)
25. We share stakeholders’ view that the Bill as currently drafted allows for unscrupulous suppliers to game the system and avoid the cap by moving customers on poor-value tariffs onto loosely-defined green tariffs. *The Government should work with Ofgem to strengthen the definition, standards and checks for electricity tariffs with environmental claims so the system cannot be gamed in this fashion and undermine the success of the cap.* (Paragraph 70)
26. *We recommend that the Bill be amended to make clear that attempts to circumvent the cap by offering tariffs that do not provide substantial environmental benefits and*

were not actively chosen by customers will be in breach of the legislation. Ofgem should be alert to and be prepared to stop any form of pricing that is designed to circumvent the cap. (Paragraph 71)

27. *The Government should explain its rationale for not exempting green gas tariffs under clause 3. (Paragraph 72)*
28. *The Government should respond to the concerns expressed by stakeholders in evidence to us on the detriment to investment in renewable generation and green gas tariff customers of not exempting these tariffs. (Paragraph 73)*
29. *The Government should work with Ofgem to create the necessary accreditations to include green dual-fuel and green gas tariffs within the price cap exemption. This should be done without repeating the gaming risks of the green electricity tariff exemption. (Paragraph 74)*

Measuring success and removing the cap

30. We support the Government's view that the price cap should only be a temporary measure. As a result, we believe that removing the sunset clause would make removing the cap too challenging and would put the Government unduly in charge of setting energy prices for the foreseeable future. We favour a return to unbridled competition once the customer detriment is removed. (Paragraph 77)
31. We believe that setting a definition of "the conditions for effective competition" before setting the cap could create incentives for suppliers to game the system or treat the cap as a box-checking exercise rather than going above and beyond their obligations. It would also risk creating unnecessary opportunities for legal challenges. (Paragraph 79)
32. It is right that the decision to keep or remove the cap is left to the Secretary of State, based on Ofgem's assessment, as the Government is responsible for introducing the legislation and setting its objectives. We believe that Ofgem have the required expertise to set and measure indicators of effective competition and make the appropriate recommendation to the Secretary of State. (Paragraph 80)
33. *We recommend that the Secretary of State base the decision to keep or lift the cap on the minimum requirements that overcharging and the differential are substantially reduced, fairness is improved, and vulnerable customers are protected. (Paragraph 81)*
34. Given the slim evidence that smart meters have any substantial impact on customer switching rates, we conclude that it would be unwise to rely solely on the smart meter rollout once the cap is lifted to maintain effective competition in the market. (Paragraph 84)
35. *Once the cap is lifted, the Government and Ofgem should take any necessary measures to ensure that the elimination of overcharging remains in place in the long term and that suppliers are not able to go back to their overcharging and cross-subsidising practices. Engagement measures currently rolled out should also be maintained to keep encouraging customers to switch suppliers. (Paragraph 85)*

Formal minutes

Wednesday 7 February 2018

Members present:

Rachel Reeves, in the Chair

Vernon Coaker	Ian Liddell-Grainger
Drew Hendry	Rachel Maclean
Stephen Kerr	Mark Pawsey

Draft Report (*Pre-legislative scrutiny of the draft Domestic Gas and Electricity (Tariff Cap) Bill*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 85 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Fourth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Wednesday 21 February at 9.45 am

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the [inquiry publications page](#) of the Committee's website.

Tuesday 12 December 2017

Question number

Stephen Littlechild, Fellow, Judge Business School, University of Cambridge, and **Stephen Smith**, former Ofgem Board Member and Director at Flipper and Global-365 plc [Q1–43](#)

Martin Cave, Group Member, Energy Market Investigation, Competition and Markets Authority, **Simeon Thornton**, Project Director, Energy Market Investigation, CMA, and **Lesley Ainsworth**, Group Member, Energy Market Investigation, CMA. [Q44–75](#)

Victoria MacGregor, Director of Energy, Citizens Advice, **Pete Moorey**, Director of Advocacy and Public Affairs, Which?, **James Taylor**, Head of Policy, Campaigns and Public Affairs, Scope, and **Peter Smith**, Director of Policy and Research, National Energy Action. [Q76–120](#)

Tuesday 19 December 2017

Michael Lewis, Chief Executive Officer, E.ON UK; **Sarwjit Sambhi**, Managing Director UK Home, Centrica; **Ed Kamm**, Chief Commercial Officer, First Utility; **Stephen Forbes**, Chief Commercial Officer, SSE. [Q121–283](#)

Peter Haigh, Managing Director, Bristol Energy; **David Bird**, Chief Executive Officer, Co-op Energy; **Hayden Wood**, Co-founder, Bulb; **Patrick New**, Managing Director, Ecotricity. [Q224–333](#)

Wednesday 10 January 2018

Dermot Nolan, Chief Executive, Ofgem. [Q334–421](#)

Wednesday 17 January 2018

Claire Perry MP, Minister for Energy and Clean Growth, Department for Business, Energy and Industrial Strategy; **Dan Monzani**, Director of Energy, Networks and Markets, Department for Business, Energy and Industrial Strategy. [Q422–510](#)

Published written evidence

The following written evidence was received and can be viewed on the [inquiry publications page](#) of the Committee's website.

PLS numbers are generated by the evidence processing system and so may not be complete.

- 1 Adam Smith Institute ([PLS0026](#))
- 2 Bristol Energy ([PLS0002](#))
- 3 Care & Repair Cymru ([PLS0040](#))
- 4 Centre for Competition Policy, University of East Anglia ([PLS0049](#))
- 5 Centrica plc ([PLS0022](#))
- 6 Citizens Advice ([PLS0021](#))
- 7 Competition and Markets Authority ([PLS0051](#))
- 8 Confederation of British Industries ([PLS0029](#))
- 9 Consumer Council ([PLS0047](#))
- 10 Co-op Energy ([PLS0030](#))
- 11 Cornwall Insight ([PLS0027](#))
- 12 David Osmon ([PLS0006](#))
- 13 Department for Business, Energy and Industry Strategy ([PLS0038](#))
- 14 Dr Timothy Dodsworth ([PLS0018](#))
- 15 E.ON ([PLS0014](#))
- 16 Ecotricity ([PLS0015](#))
- 17 EDF Energy ([PLS0012](#))
- 18 Energy Policy Group ([PLS0036](#))
- 19 Energy UK ([PLS0028](#))
- 20 First Utility ([PLS0004](#))
- 21 Frank Field ([PLS0050](#))
- 22 Good Energy ([PLS0046](#))
- 23 Hudson Energy Supply UK Limited ([PLS0007](#))
- 24 Institute of Economic Affairs ([PLS0017](#))
- 25 MoneySuperMarket.com ([PLS0024](#))
- 26 Mr John Penrose ([PLS0019](#))
- 27 National Energy Action (NEA) ([PLS0037](#))
- 28 npower ([PLS0031](#))
- 29 Octopus Energy ([PLS0035](#))
- 30 Ofgem ([PLS0045](#))
- 31 OVO Energy ([PLS0008](#))
- 32 Professor Martin Cave OBE ([PLS0044](#))
- 33 Professor Stephen Littlechild ([PLS0003](#))

- 34 Professor Stephen Littlechild ([PLS0053](#))
- 35 Rt Hon Caroline Flint ([PLS0041](#))
- 36 Scope ([PLS0025](#))
- 37 ScottishPower ([PLS0034](#))
- 38 Smart Energy GB ([PLS0013](#))
- 39 SSE ([PLS0052](#))
- 40 TaxPayers' Alliance ([PLS0009](#))
- 41 uSwitch.com ([PLS0033](#))
- 42 Utilita Energy Ltd ([PLS0001](#))

List of Reports from the Committee during the current Parliament

All publications from the Committee are available on the [publications page](#) of the Committee's website. The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2017–19

First Report	A framework for modern employment	HC 352
Second Report	Leaving the EU: implications for the civil nuclear sector	HC 378
Third Report	The safety of Electrical Goods in the UK	HC 503
First Special Report	Industrial Strategy: First Review: Government Response to the Committee's Second Report of Session 2016–17	HC 337
Second Special Report	Corporate governance: Government Response to the Committee's Third Report of Session 2016–17	HC 338
Fourth Special Report	Leaving the EU: negotiation priorities for energy and climate change policy: Government Response to the Committee's Fourth Report of Session 2016–17	HC 550
First Joint Special Report	Apprenticeships: Government Response to the Second Joint Report of Session 2016–17	HC 450