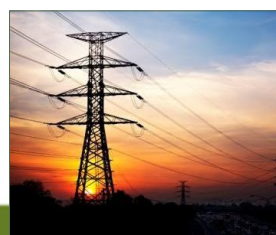


Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase II Regulatory Implications

Final Report
December 2016



About the Utility Regulator

The Utility Regulator is the independent non-ministerial government department responsible for regulating Northern Ireland's electricity, gas, water and sewerage industries, to promote the short and long-term interests of consumers.

We are not a policy-making department of government, but we make sure that the energy and water utility industries in Northern Ireland are regulated and developed within ministerial policy as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly through financial and annual reporting obligations.

We are based at Queens House in the centre of Belfast. The Chief Executive leads a management team of directors representing each of the key functional areas in the organisation: Corporate Affairs; Electricity; Gas; Retail and Social; and Water. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

Our Mission

Value and sustainability in energy and water.

Our Vision

We will make a difference for consumers by listening, innovating and leading.

Our Values

Be a best practice regulator: transparent, consistent, proportional, accountable, and targeted.

Be a united team.

Be collaborative and co-operative.

Be professional.

Listen and explain.

Make a difference.

Act with integrity.

Abstract

Protecting consumers is at the heart of the Utility Regulator's (UR) role and working to deliver sufficient effective competition in the Northern Ireland (NI) energy market to protect customers is an integral part of our focus. Phase I of our review of the effectiveness of competition in the Northern Ireland Retail Energy Market assessed the state of competition in the NI energy markets and highlighted areas which may require intervention. It endorsed the maintenance of price controls on dominant suppliers as an appropriate regulatory response to market dominance.

This second phase of the review considers the regulatory options for the NI energy supply markets which could replace the status quo should the current form of price regulation cease. Cornwall Energy was commissioned by the UR to help develop a set of options for future price regulation of the NI market which could potentially be employed in the event that the current form of regulation is changed. These were consulted upon by the UR in December 2015, with the consultation period closing in March 2016. This paper represents the final UR position at this stage of market development. Stakeholder responses have been taken into account as well as the final findings of the CMA energy market review in GB.

Audience

Consumers and consumer groups; industry; and statutory bodies.

Consumer impact

The strategic goal of this project is to ensure that consumers are, and continue to be, effectively protected in the NI energy markets. The direct consumer impact of this is likely to be on the end user price, when the current regime of price regulation on the incumbents only ends. However, a future consultation on the precise implementation of one or more of the chosen options will be carried out as well as a legal review which will be on the basis of the circumstances and state of the market at that point.

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Glossary

CMA	Competition and Markets Authority
GB	Great Britain
I&C	Industrial and Commercial
NI	Northern Ireland
Ofgem	The Office of Gas and Electricity Markets in Great Britain
REMM	Retail Energy Market Monitoring
UR	The Northern Ireland Authority for Utility Regulation or the “Utility Regulator”

CPS	Consumer Protection Strategy
EAI	Electricity Association Ireland
FSB	Federation of Small Business
PNGL	Phoenix Natural Gas Limited
NEA	National Energy Action

1. Strategic Background

- 1.1 Protecting consumers is at the heart of the Utility Regulator's (UR) role as outlined in its statutory duties. We also have duties to promote effective competition when appropriate. The UR believes in the benefits of competition, if it is effective competition and the majority of consumers are actively engaged in the market. The UR therefore operates a twin tracked approach to ensure both that NI consumers are adequately protected and that open competitive markets are actively promoted. As a result, our approach is multi-faceted, with a number of different and separate projects to help achieve these duties of consumer protection alongside the promotion of effective competition and maximum customer engagement in the market.

NI Retail Energy Market Regulation to Date

- 1.2 In Electricity, the primary statutory duty of the Utility Regulator (UR) is *“to protect the interests of consumers of electricity supplied by authorised suppliers, wherever appropriate by promoting effective competition”*¹.
- 1.3 In relation to gas the principal objective of the UR is *“to promote the development and maintenance of an efficient, economic and co-ordinated gas industry in Northern Ireland” whilst having regard to “the need to ensure a high level of protection of the interests of consumers of gas”*².
- 1.4 The electricity market was privatised in 1992. The supplier at that time was Northern Ireland Electricity Energy Supply (NIEES) now Power NI who were the monopoly supplier up until the electricity market was opened to competition.
- 1.5 Electricity retail markets were initially opened for large non-domestic consumers in 2002, with the smaller non-domestic market being opened over the following couple of years. The domestic market was opened to competition in 2007 but there was no new entrant until 2010.
- 1.6 Whilst the electricity supply market in NI is fully open to competition and there are now a number of competing suppliers in the market Power NI still retain the majority share of the domestic market. They are therefore subject to a price control.
- 1.7 Natural gas was introduced to NI in 1996. There are two distinct distribution areas for natural gas. These are the Greater Belfast area and the Ten Towns area.
- 1.8 The Greater Belfast market has been open to competition since 2007. There are approximately 178,000 customers in the market. Currently there are six active suppliers in the market. However only two companies supply to

¹ Article 12 of the *Energy (Northern Ireland) Order 2003*.

² Article 14 of the *Energy (Northern Ireland) Order 2003*.

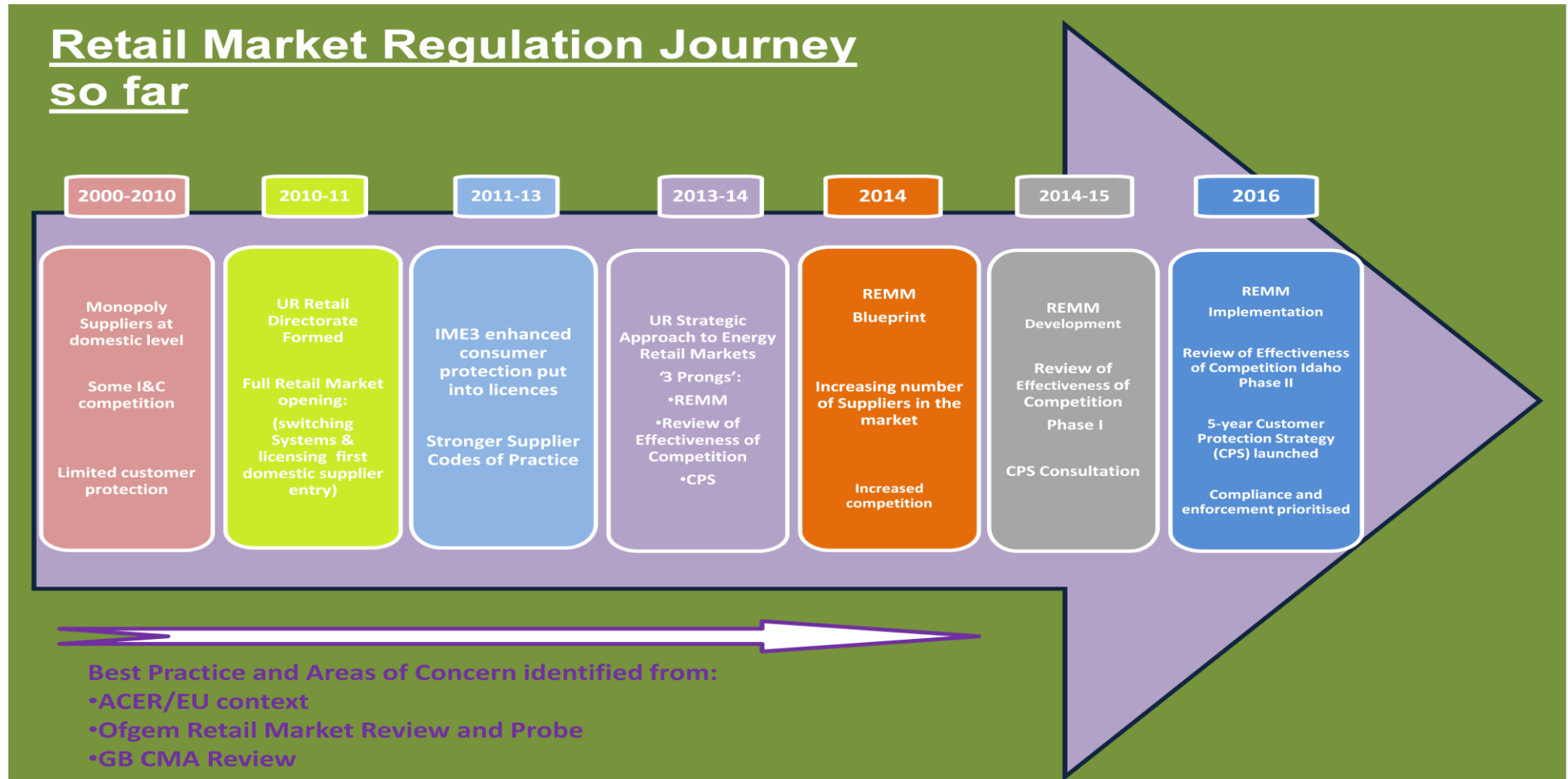
domestic consumers. SSE Airtricity is the incumbent supplier in this area and is subject to price control.

- 1.9 The Ten Towns gas market is a relatively small market; there are approximately 27,000 gas customers. The market for I&C customers using less than 732,000 kWh per annum has been open since April 2015, currently there are four suppliers operating in the market. However firmus is currently the only supplier for domestic customers.
- 1.10 This means there are three price regulated energy supply companies in NI:
- Power NI Ltd (Power NI) in the electricity supply sector;
 - SSE Airtricity Gas Supply (NI) Ltd (SSE Airtricity) in the gas supply sector in Greater Belfast; and
 - firmus energy (supply) Ltd (firmus) in the gas supply sector in the Ten Towns area.
- 1.11 These three supply companies are subject to a price control as they are deemed to be dominant in the market they operate. Where competition is not sufficiently developed or effective, the UR protects customers by regulation and this applies to the domestic electricity market and the domestic and small I&C market in gas.
- 1.12 Since the energy retail markets opened to competition and through the formation and delivery of the retail market and consumer protection aspects of the UR's Corporate Strategy, there have been a series of joined-up UR projects which have helped to shape the current competitive retail market and consumer protection frameworks. These have had the twin focus of promoting as effective a competitive retail market as we could in the NI context, whilst also having the high level of consumer protection envisaged by our statutory duties and by EU law.
- 1.13 These projects were put into place alongside the continuation of price regulation for domestic and small business customers and ongoing price control reviews. The existence of price controls on suppliers who are dominant in the domestic and small business markets protects both electricity and gas consumers from ineffective competition and has been broadly welcomed by consumer bodies, and non-price regulated suppliers, in NI. It is our view that their existence has also allowed us to avoid some of the issues and concerns that have arisen in other energy markets on price and profit transparency and charging by dominant suppliers.
- 1.14 The other consumer protection measures put in place by UR in recent years worked alongside price regulation, and are primarily "non-price" intervention measures. The projects were identified by examining best practice elsewhere and in light of EU legislative requirements and tailoring those lessons learned to the NI context to formulate a coherent policy. This set of consumer protection measures were explicitly built into the UR's corporate strategy and

annual Forward Work Plans, and extensively consulted on with all stakeholders.

1.15 This “journey” of UR retail market regulation in NI is laid out in Figure 1 below.

Figure 1 Retail Market Journey so Far



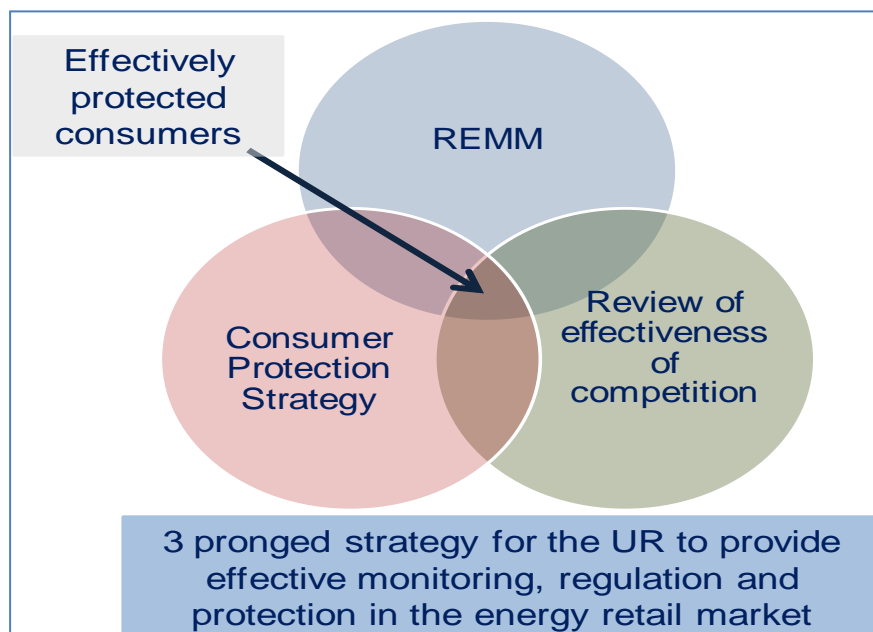
- 1.16 The period up to 2011 was categorised by largely monopoly suppliers in the domestic space and rolling de-regulation in the I&C sectors in electricity. Much of the early UR work at this time was focused on ensuring regulatory oversight and input into delivering the mechanics, processes and systems to deliver unlimited and efficient customer switching and all of the associated retail market functions.
- 1.17 These were considered to be in place by May 2012 and focus then shifted to important key customer protection building blocks such as Supplier Codes of Practice and other measures to achieve the “higher level of consumer protection” required by EU Energy Directives (e.g. tariff transparency, cost-free switching of supplier).
- 1.18 From 2014 onwards the focus, under the new 5-year UR Corporate Strategy, was the delivery of the so-called “3 prongs”:
- **Review of Effectiveness of Competition** (how do/will customers fare in our retail markets and what are the appropriate regulatory interventions);
 - **REMM** (effective retail energy market monitoring so we have good market intelligence);
 - **Consumer Protection Strategy (CPS)**: setting out a 5 year Action Plan in 2016 ensuring protection of vulnerable domestic customers and promoting consumer knowledge and engagement in the retail markets).
- 1.19 The paper “*The UR Strategic Approach to Energy Retail Markets and Consumer Protection*”³ was published in 2014. It set out UR’s strategic vision for retail markets and again emphasised the importance of our twin track approach: customer protection alongside effective competition and empowered consumers. It stated that:
- “Our overall philosophy in developing retail competition is to develop, change or maintain the regulatory framework in a way that seeks to crystallise and maximise consumer benefit from competition; whilst also ensuring consumers remain protected by an effective regulatory regime that learns from best practice elsewhere”*
- 1.20 It also set out an ‘ideal vision’ for the future electricity and gas supply customer environment. It included the goals:
- Well-informed consumers have clear and easily understood information and awareness of different suppliers, products and tariff / service choices resulting in uncomplicated, high-quality decision-making by consumers. Consumers can easily weigh up their options and switch supplier if they wish to.

³ <https://www.uregni.gov.uk/news-centre/ur-publishes-its-strategic-approach-energy-retail-markets-and-consumer-protection>

- All consumers benefit from competition as much as possible, but are also protected by ongoing regulatory action. This regulatory action is transparent, proportionate and developed through appropriate analysis and consultation.
- The UR builds on existing work to effectively monitor supplier and customer activity in the energy retail markets to ensure the market is operating effectively, and to provide information to the regulator, stakeholders and importantly to customers themselves, to allow transparent and effective decision making. (REMM).
- Customers, especially vulnerable ones, are adequately protected in the NI energy markets. There is much evidence that vulnerable customers may not be able to benefit as much as others from the benefits of competition, and may need an extra layer of regulatory protection (CPS).

1.21 This document, and the UR Corporate Strategy, laid out the projects which would help achieve this vision. They highlighted that these projects, whilst separate, are interlinked. These are shown in Figure 2 below:

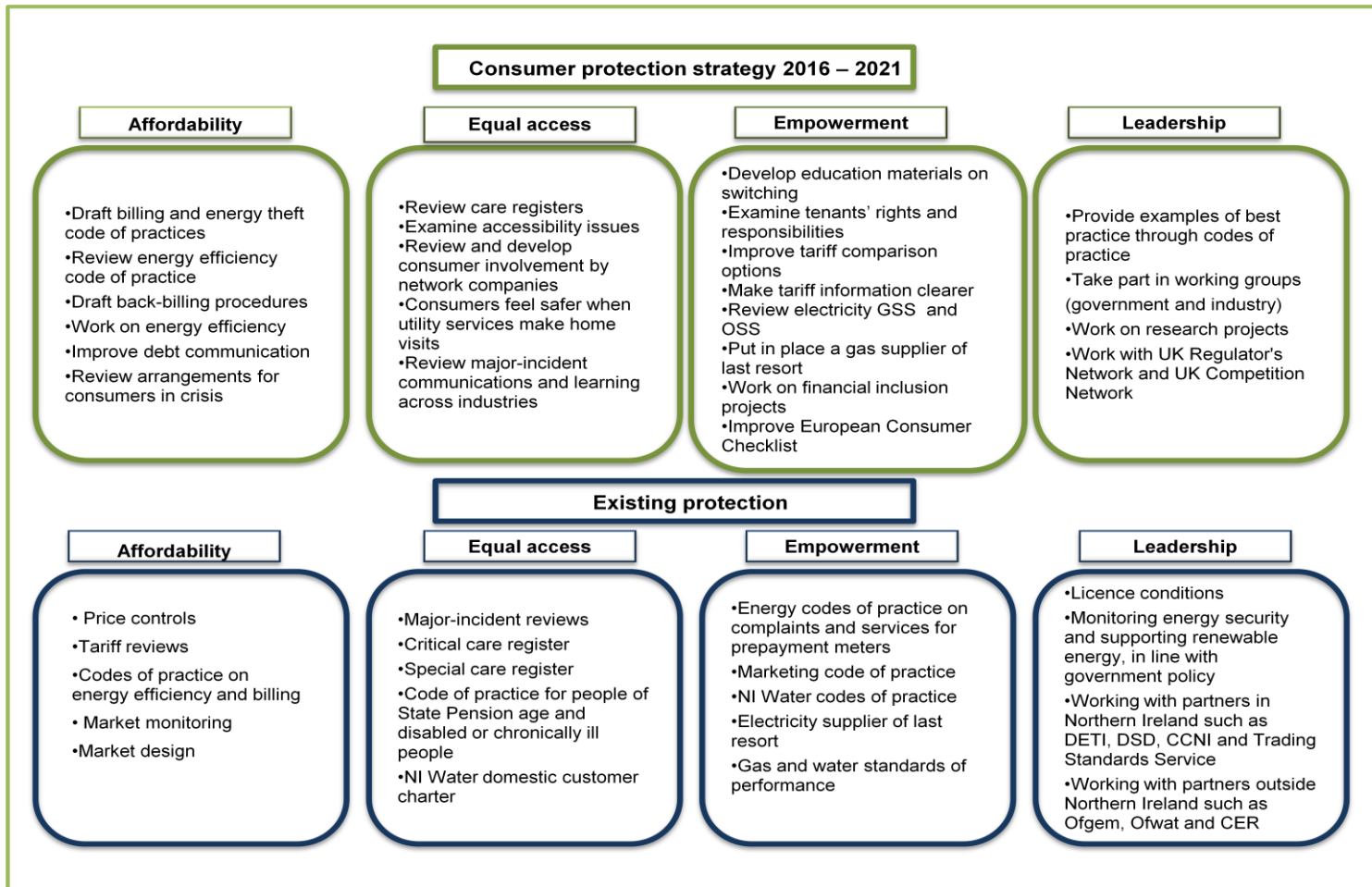
Figure 2 ‘Three Prongs’



- 1.22 Each project is important in its own right, but taken together, they form a ‘3-pronged’ strategy to allow the UR to more effectively monitor, regulate and ultimately protect consumers in our energy retail markets. The projects built on the solid foundations we already had in relation to consumer protection and delivering optimal competition in the energy retail markets, but did so in a targeted, consistent and proportionate sense.
- 1.23 The most recent delivery aspect of the three prongs came in the form of the 2016 CPS, which has a 5 year plan to put in a new layer of vulnerable domestic customer protection, and projects to enhance consumer empowerment and ability to engage actively in the market, building on the

existing foundation already in place at 2016. Figure 3 below gives an overview of CPS.

Figure 3 Consumer Protection Strategy



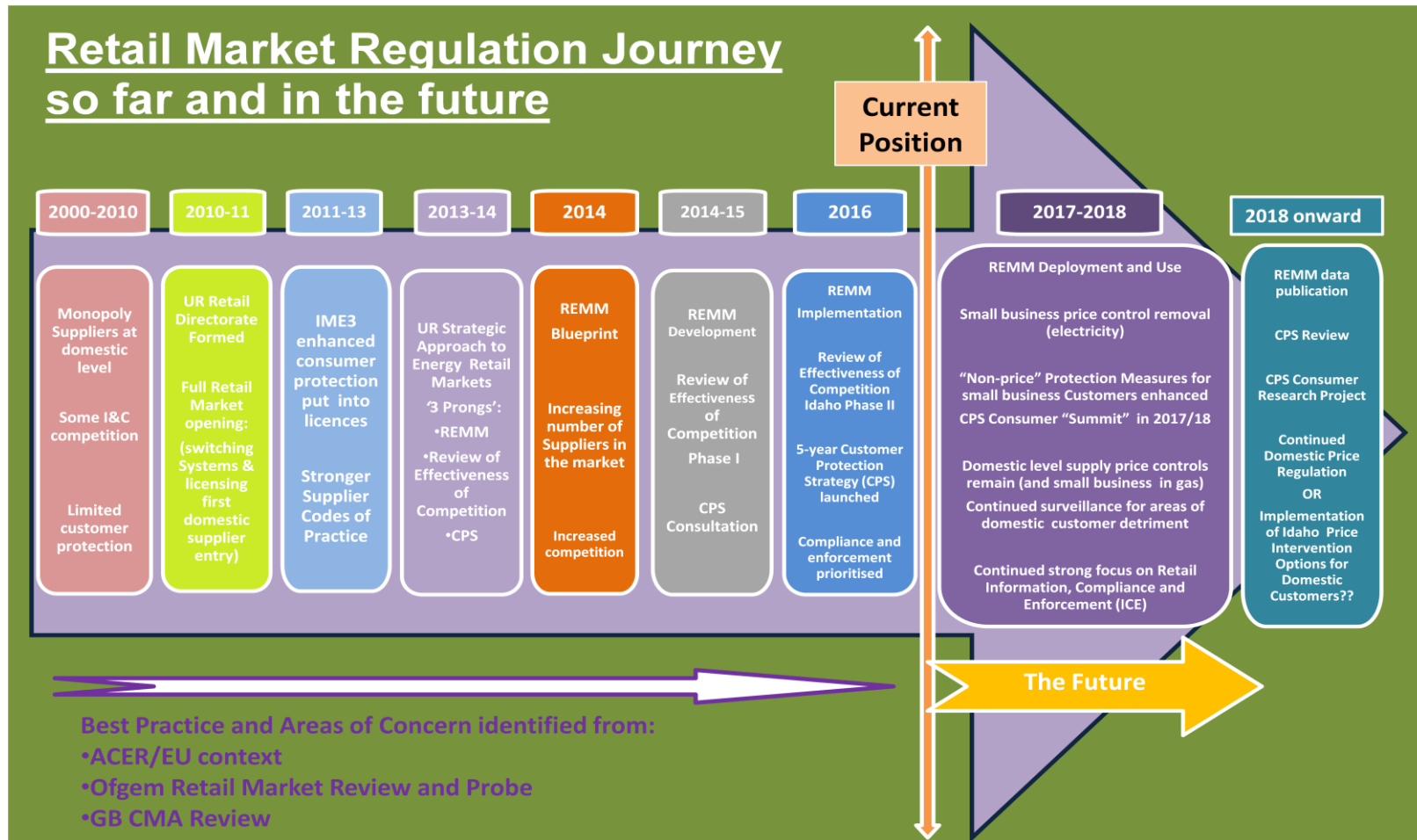
Current Position

1.24 Re-visiting this Retail market journey is important to understand the current position and next steps we are considering in terms of UR regulatory approach. Below is a summary of the current position:

- There are good customer protection arrangements in place for domestic customers, and these sit alongside ongoing domestic price regulation. Year 1 CPS projects are all underway and Year 2 projects are planned for the UR's 2017/18 FWP. We continually scan for gaps, or lessons we might learn from GB regulation and the recent CMA market investigation. Also, market issues arise constantly which require new thinking/approaches to our consumer protection model.
- Alongside this protection, we continue our work to maximise the level of competition in our energy retail markets and ensure customers have the knowledge and tools to actively engage in those markets (e.g. our current work on educational material on switching for customers; our work on a new Code of practice on the clarity of information on Bills).
- Domestic price regulation is a key benefit in NI, and has ensured we have avoided the worst issues evidenced by CMA in relation to retail market detriment to customers in GB. Consumer bodies in NI, and to some extent non-dominant suppliers, are very supportive of this approach. This Phase II of the Review of Effectiveness of Competition outlines some of the UR's options for a future regulatory approach if this current form of domestic price regulation was to be removed.
- We are continuing to develop and implement REMM. This will take time, and full deployment and use of REMM data will only commence in 2017/18. Trend and features etc will take some time to emerge. REMM also delivers substantial compliance and information benefits to UR.
- We are reaching a defining moment in the I&C market, where electricity price regulation for small businesses is being removed for the first time. We need to consider the "non-price" regulatory and customer protection consequences of this, and plan to do this in 17/18, learning from CMA experience. This will be a priority for 2017/18.

In this context, Figure 4 below shows the retail journey to this point and what we envisage it to be going forward:

Figure 4 Retail Market Journey so Far & in The Future



2. Review of Effectiveness of Competition in the NI Energy Market

2.1 The Review of Effectiveness of Competition is the third element of the ‘three pronged strategy’. There have been two phases in the Effectiveness Review project.

Phase I Findings

2.2 During 2014 the UR commissioned Cornwall Energy to review the condition of energy supply competition in NI. This project assessed the NI energy markets along similar metrics as those followed by the UK Competition and Markets Authority (CMA) and Ofgem in their *State of the market assessment*⁴, but recognising significant physical, size and market maturity differences between NI and GB supply markets.

2.3 The Cornwall Phase I report⁵ laid out the findings in relation to the state of retail competition in the NI electricity and gas retail markets. The conclusions of the Phase I report were:

- The NI market has achieved reasonable levels of switching given the context of the market and its maturity.
- The Power NI (former electricity supply incumbent) share of the domestic and small I&C market remains high, with a lot of the pricing strategies of

⁴ <https://www.ofgem.gov.uk/publications-and-updates/state-market-assessment>

⁵ <https://www.uregni.gov.uk/news-centre/competition-retail-energy-markets-northern-ireland-report-published>

competitors focused on discounting of the Power NI price; gas incumbent market shares remain similarly high, with similar pricing strategies.

- There are limited supply players in the energy supply market and it is highly concentrated.
- Given the fundamental lack of scale of the NI market, this is unlikely to change and the number of suppliers in the market is unlikely to materially increase.
- Whilst competition has been reasonably effective up to now, given the structural characteristics of the market and the lack of sufficient critical mass to attract a larger number of suppliers, relying on competition is not enough on its own to effectively protect customers. Northern Ireland has only circa 788,000 domestic electricity customers and circa 167,000 domestic gas customers in the greater Belfast Area. (NI has less than 3% of the total number of domestic electricity customers in GB and, for example, is only around 70% the size of the market in greater Manchester).
- Those customers who wish to switch have arguably already done so, and it should not be expected that switching rates will continue as they have up to now. Research indicates high levels of “stickiness” amongst customers similar to those seen in GB.

2.4 The report concluded that the requirement for some form of price regulation is likely to continue for the foreseeable future; and that this form of regulation should co-exist with the ongoing development of competition. The Cornwall paper stated *“the NI experience strongly suggests that regulation and competition can successfully co-exist”*.

Review of Effectiveness of Competition in the NI Energy Market - Phase II Objectives

- 2.5 Phase II of the project commenced in April 2015, with the publication of an information paper⁶ which represented the formal commencement of Phase II. In this paper we stated that we intend to monitor the condition of competition in all market sectors going forward. The REMM⁷ will be used as the tool to carry out this monitoring. In addition to this, there will be ongoing liaison with customers, suppliers and consumer bodies.
- 2.6 The core objective of Phase II is to assess the options for a future regulatory framework (potentially including some form of price regulation) in a market where the current regime of price controlling the former supply incumbents only may no longer be appropriate.
- 2.7 The original scope of Phase II, in terms of the development of future regulatory options, covered the NI electricity and gas domestic and small I&C retail markets only. The larger end of the I&C energy markets were not within the scope of Phase II, as these were found on balance to be sufficiently competitive in Phase I. It is also true that these larger customers exhibit none of the stickiness of small business or domestic customers and will ensure themselves that they receive the most competitive prices available by negotiating with all available suppliers in the market in a well informed and organised way. Hence price regulation is unlikely to be required for this customer group.

⁶

http://www.uregni.gov.uk/news/view/ur_publishes_information_note_on_review_of_effectiveness_of_competition_pha/

⁷ http://www.uregni.gov.uk/news/view/retail_energy_market_monitoring_remm_final_decisions_published/

2.8 The UR published its consultation paper on Phase II, along with a technical annex developed by Cornwall Energy, in December 2015⁸. This paper consulted on seven options for a future regulatory framework once the current price control regime ends. These options were developed by the UR in conjunction with Cornwall Energy, and through discussions with suppliers and other stakeholders, together with lessons learnt from international regulatory experience.

CMA Review and Findings and relevance to NI

2.9 GB energy retail market experience is also an important context to the UR's Phase II project. In June 2014, the GB regulator, the Office of Gas and Electricity Markets (Ofgem), announced that it would refer the GB energy market for an investigation by the Competition and Markets Authority (CMA). The decision followed a market assessment, conducted by Ofgem, which concluded that a number of features of the market were preventing, restricting, or distorting competition.

2.10 As part of its investigation, the CMA was required to examine whether “any feature, or combination of features, of each relevant market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the United Kingdom or a part of the United Kingdom”. If this were the case, it would represent an Adverse Effect on Competition (AEC).

2.11 The CMA focussed its market assessment on the GB market and did not consider the NI energy markets. However, the review is important in the context of this consultation for a number of reasons.

⁸ <https://www.uregni.gov.uk/consultations/consultation-phase-ii-review-effectiveness-competition-ni-energy-markets>

- 2.12 Firstly, the GB retail market has been fully open to competition for much longer than the NI markets (17 years in GB) and as such experience of market conditions and regulation provides valuable lessons for NI.
- 2.13 Secondly, notwithstanding important physical differences between the GB and NI market (such as market size and the relatively low (but growing) customer access to gas in NI), the assessment and proposed remedies in GB suggest remedies that may be appropriate for application in NI.
- 2.14 The final report of the current CMA review of GB energy markets⁹ was issued in June 2016. During the course of the review, the CMA stated that its focus and concerns were not on the wholesale energy market in GB, but rather the retail sector where they identified certain concerns on consumer harm.
- 2.15 The findings highlighted that there were a combination of features in the GB market which have an adverse effect on competition. For example, one of the areas examined by the CMA related to ‘weak customer response’. Within this area they highlighted the issue of the ability of suppliers to use their unilateral market power to charge higher prices and earn larger profits from their “inactive” or “disengaged” customers. They also pointed to the fact that energy is a homogenous product and as such customers are less interested in it as a product of “choice”, and in their ability to switch providers. This exacerbates the situation. Overall, the CMA found that GB energy customers were, and continued to be, paying billions of pounds more for their energy than necessary.
- 2.16 The measures that the CMA has decided to implement in the retail energy market include:

⁹ <https://www.ofgem.gov.uk/gas/retail-market/market-review-and-reform/state-competition-energy-market-assessment>

- obligating suppliers to provide Ofgem with details of all customers who have been on their standard default tariff for more than three years i.e. the “sticky” customers. This information will be put on a database to allow rival suppliers to contact customers by letter and offer cheaper and easy-to-access deals based on their energy usage;
- a transitional price cap for customers on pre-payment meters (PPM), from 2017-20. This is important as it represents a re-introduction of supply price regulation in the GB energy market (albeit it is a temporary measure until the introduction of smart meters). We also recognise that the reasons for it are in part due to technical barriers to switching. It should also be remembered however that re-introduction of price regulation for all standard tariff customers of the incumbents was discussed by the CMA and one panel member, Martin Cave, supported that course of action. This indicates a significant shift in policy discussion in GB around the role of price regulation despite many years of promoting active competition ;
- enabling price comparison websites to play a more active role in helping customers find the best offers for them by giving them access to meter data; and
- improving how information is relayed to customers to help engagement by using trials and testing what works in practice.

Additionally, in the non-domestic market, the CMA decided to implement measures including:

- greater transparency of tariffs for micro-businesses, with a requirement for all suppliers to publish tariffs including acquisition and retention tariffs; and
- an end to the automatic ‘rollover’ of contracts for micro-businesses and an end to exit fees if a contract not renewed;

- having Ofgem implement a programme to provide micro-business customers with different or additional information to promote them to engage in the SME retail energy markets; and
- a requirement on suppliers to provide details of their micro-business customers who have been on a default tariff for over three years to Ofgem, so this information may be used for postal marketing.

2.17 The implications in the NI context, whilst bearing in mind that the markets are different in terms of scale and maturity, are that lessons can be learned from the results of the CMA review. Of particular note is the price cap for prepayment customers. This essentially represents the reintroduction of a form of price control back into the competitive UK energy market.

2.18 In addition to this, the recommendations for micro-businesses could also be of relevance to NI. Issues such as the transparency of prices are cited by small business representative groups in NI as problematic and this lack of transparency means small businesses do not have the correct information with which to make good quality decisions. This distorts the proper functioning of the competitive market. Up to now small businesses did have the regulated Power NI tariff to use as a benchmark against other offerings, but from 1 April 2016 this will no longer be the case as the price control has been removed from Power NI in the small business market as they are no longer dominant in that space. More detail on the CMA final findings are contained in the Cornwall Energy report contained in Appendix I.

3. Phase II Findings and Recommendations

- 3.1 As previously stated in section 1, the paper published by the UR in December 2015 consulted on the potential options for a future regulatory framework. This would follow the end of the current price controlling regime in place in the NI energy market if it were to be removed.
- 3.2 The options the UR consulted upon were developed in conjunction with Cornwall Energy and engagement with the industry. Cornwall met with all suppliers and developed the options in the context of those interactions taking on board supplier concerns and advice regarding the operational feasibility and likely success of each option. The consultation period ended in March 2016, presenting stakeholders with the opportunity to give their views on the viability of the various options.
- 3.3 Seven options were consulted upon, these were:
 - **Significant Market Power:** undue preference and undue discrimination licence obligations would be switched on for any supplier deemed by the UR, under established and transparent criteria, to have significant market power (SMP);
 - **Inactive Customer Tariff:** for incumbent suppliers' disengaged customers (not all suppliers as with the default tariff). This option would only apply to the former incumbent energy suppliers. "disengaged" would need clearly defined.
 - **Default Tariff:** for those consumers unwilling or unable to engage with the market. All suppliers will offer this tariff (not just incumbents as with the inactive customer tariff) and have to clearly show and justify its constituent parts, including the margin being taken under the tariff;

- **Tariff Cap Spread:** limitation on the differences between the most expensive and cheapest tariffs of a supplier;
- **Dominance Thresholds:** setting market thresholds above which if a supplier or suppliers are deemed sufficiently dominant to be able to exert market power, regulatory solutions may be implemented;
- **Gross-Margin Cap:** where suppliers would only be permitted to put rates into the market with a maximum level of gross margin; and
- **Price-to-Beat Tariff:** offer determined by the UR that suppliers would have to match or better.

3.4 There were 12 responses to the consultation. Of these responses, nine were from suppliers or their representatives. Stakeholder responses are contained in Appendix II onwards to this paper.

UR Decision on Options to be Retained

3.5 Cornwall Energy have produced a detailed technical paper in conjunction with the UR. Stakeholder feedback was reviewed in detail by both the UR and Cornwall Energy in drawing together this paper. This review also included detailed discussion of consultee views taking into account their concerns, the implications of these and if/how they could be addressed. It also considered if the concerns were justified. This detailed consideration was used in the collation of the paper as well as assessing the options taking into account, amongst other things, the practicality of each options and the pros and cons of each. The paper also details the process of the development of the options and how Cornwall Energy has reached their conclusions and recommendations. This was done in conjunction with the UR; and the resulting recommendations discussed and approved with the UR Board. This paper is contained in Appendix I to this paper.

3.6 Cornwall Energy has made recommendations to the UR as to which options, in their view, should be retained. They have recommended that four options be retained, so that the UR can carry out a legal review and consult on the implementation of them at some point in the future, if the relevant time comes. Any policy decision made at this time, in terms of proceeding with the implementation of any of the four retained options, will take into account the market conditions at the time and will be taken by the UR.

3.7 The four options are:

- **Significant Market Power:** undue preference and undue discrimination licence obligations would be switched on for any supplier deemed by the UR, under established and transparent criteria, to have significant market power (SMP);
- **Inactive Customer Tariff:** for incumbent suppliers' disengaged customers (not all suppliers as with the default tariff). This option would only apply to the former incumbent energy suppliers. "disengaged" would need clearly defined.
- **Default Tariff:** for those consumers unwilling or unable to engage with the market. All suppliers will offer this tariff (not just incumbents as with the inactive customer tariff) and have to clearly show and justify its constituent parts, including the margin being taken under the tariff; and
- **Dominance Thresholds:** setting market thresholds above which if a supplier or suppliers are deemed sufficiently dominant to be able to exert market power, regulatory solutions may be implemented.

3.8 More detail on each of the options can be found in the Cornwall Energy Paper.

Legal Context

- 3.9 A number of respondents to the consultation expressed the view that they felt there may be legal implications with some of the options if they were implemented. However, it is our intention to consult on the implementation of the options and to carry out a legal review which will be done in the context of the market at the time. Any legal implications will be resolved at this point.

4. Implementation

- 4.1 This section of the paper sets out the scope (i.e. the customers) which the retained options will cover, if implemented, as well as the timing of the implementation of any option.

Scope of Option Coverage

- 4.2 As stated in section 1, it was previously anticipated that the potential options retained for further consideration could be applied in both the domestic and the I&C market. However, over the course of the consultation period and upon further internal consideration by the UR, we are minded to apply any of the retained options to the domestic market only. There are a number of reasons for the UR taking this position.
- 4.3 There are more suppliers in I&C market, and we have seen more aggressive customer acquisition from companies operating in it. It has also historically been the case that some suppliers enter the I&C market only, whilst others enter both domestic and I&C. As a result, it is likely that the I&C market will continue to have more active suppliers than the domestic market.
- 4.4 The UR also noted that the recently published CMA remedies for GB do not include any form of price intervention in the micro-business market, but rather a number of other measures in relation to increasing transparency of tariffs and automatic rollover of contracts no longer being allowed.
- 4.5 The EU's 'third package' included a "universal service obligation" requirement for Member States under Article 3(3) of Directive 2009/52/EC. The universal service obligation is 'the right to be supplied with electricity of a specified quality within their territory at reasonable, easily and clearly comparable, transparent and non-discriminatory prices'. In this context it could potentially be argued that price intervention may be justified to deliver

these requirements. However, when taking into account the market conditions at the time, DETI (now DfE) chose to make this EU requirement one that was applicable to domestic customers only in NI. Therefore, given that universal service is not currently transposed into our legislation to include non-domestic customers, this could make the justification for new price intervention measures more difficult for that customer group.

- 4.6 In addition to this, and as referred to in the Power NI SPC17 Decision paper¹⁰, we intend to consult on other potential non-price-intervention measures which could be put in place for small I&C customers. These may include: a duty to offer terms along with the requirement for reasonable deposits; tariff transparency for I&C customers similar to the CMA recommendation; contract rollover parameters e.g. no exit fees; letters to customers informing that their fixed term contract is coming to an end.

Timing of Implementation

- 4.7 In terms of implementation, the UR is of the view that it is important to give some certainty to the market in relation to the timing of option implementation should the policy adopted be to implement one of the options shortlisted. If the UR does, during the period running up to the removal of the current form of regulation, decide that it is in customers' interest to implement one of the options, there are two possible scenarios regarding timing of the implementation. These are :

- Immediately after the end of the current price control regime and in advance of any customer harm occurring; or
- After a period of competition and monitoring (duration of which would need to be determined).

¹⁰ <https://www.uregni.gov.uk/news-centre/utility-regulator-publishes-decision-paper-2017-power-ni-price-control>

- 4.8 After discussion, the Authority took the view that if the current form of regulation ends one or more of the retained options could be implemented immediately. This would be dependent on the policy position at that time as regards if the UR felt it was necessary, given the size and state of the domestic market to implement some form of price regulation and not rely on competition alone. This policy would be based on a view that it is highly likely that domestic customers, or a certain type or group of domestic customers are going to experience detriment if they are not protected by some version of price regulation after the current form is removed. Given a view of high likelihood of detriment a coherent regulatory response would be immediate implementation given our statutory duties on consumer protection. However, it is important to note that this would follow a full legal review which would also take into account market circumstances at the time.
- 4.9 We wish to give as much certainty to the market in relation to the timelines for implementation as possible but can only commit to a minded to position based on our assessment of the market today. The decision on whether price regulation is required could be two, three or more years away and the UR will need to take the facts at that time into account.
- 4.10 The UR current position however is that we believe that is likely that customer harm could occur if we did not have an immediate implementation of one or more of the options. The harm referred to is the natural market progression post price controls where suppliers charge their 'sticky' customers significantly more than those customers who are engaged.
- 4.11 In other similar markets the experience has been that the Standard Variable Tariffs (SVTs) given to inactive customers are substantially higher than the suppliers acquisition tariffs which are offered to new customers.

- 4.12 The NI market size coupled with this customer 'stickiness' prevalent in other markets would suggest that there is no reason to believe that NI suppliers/market would behave differently to those in GB or ROI.
- 4.13 If the UR did not implement immediately there is a real risk of customer harm. We are of the view that the protections should be in place **before** this harm can take place.
- 4.14 We believe that the retained options are compatible with and will not hinder competition. This has been demonstrated in the 'hybrid' model which we currently have in NI, and which has been widely welcomed by consumer groups and a number of non-dominant suppliers. The UR is of the view that the retained options will either benefit all customers by general protection for the whole market or protect those who are inactive (and potentially vulnerable) in the case of the 'inactive tariff' or 'default tariff' options.
- 4.15 Our eventual decision on what option/s (if any) will follow the removal of the current price controls will be taken in the context of our legal framework which includes our statutory objectives under Articles 12 and 14 of the Energy (NI) Order 2003, noting that these are different as between gas and electricity.
- 4.16 In the interim it is important to allow the market to develop. The UR will continue to monitor and promote competition. Any policy decision taken to implement the options will be in this context

5. Next Steps

- 5.1 This paper and the attached Annex represent the final paper on the Review of Effectiveness of Competition project. Four options have been retained which may be implemented if the current form of price regulation ends. The UR current view is that one should be implemented immediately if the current form of price regulation ends.
- 5.2 The UR will continue to monitor the market in terms of market shares and any other issues which may arise. This will be carried out through the REMM framework. We will continue to support and promote the development of competition.
- 5.3 A full legal review will be carried out in advance of the implementation of any of the options.
- 5.4 As indicated in this paper and the Power NI SPC17 Decision Paper, we intend to initiate a piece of work which will examine potential non-price intervention measures for the protection of small I&C customers. This is in the context of the scope of the price regulation options developed as part of this project covering domestic customers only.

Appendix I

**Cornwall Energy – Review of
Effectiveness of Competition
Phase II final Report**

Date: September 2016

**Review of the Effectiveness of Competition in the
Northern Ireland Retail Market – Phase II
Final Report**

Prepared by: Robert Buckley, Ed Reed, and Colin Magee
Cornwall Energy

About Cornwall Energy

Cornwall Energy's team of independent specialists have experience of liberalised energy markets and their regulation since their inception in Great Britain and elsewhere in the late 1980s. We provide consultancy, intelligence and training, and are a trusted and reliable partner whether you are a new entrant or a large, established player.

Specific areas of our expertise include:

- wholesale and retail energy market competition and change;
- regulation and public policy within both electricity and gas markets;
- electricity and gas market design, governance and business processes; and
- market entry.

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I Executive summary

I.1 Consultation purpose

This assessment of the effectiveness of the Northern Ireland (NI) retail markets for electricity and gas was commissioned by the Utility Regulator (UR).¹ It is part of a wider programme of interlinking work to deliver the regulator's corporate strategy ambitions for the period 2014-19. In November 2014, Cornwall Energy published the *Review of Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase I*², which concluded—among other findings—that given the inherent oligopolistic tendencies of the supply markets “the NI experience strongly suggests that regulation and competition can successfully coexist. Some form of direct price regulation is often necessary to deliver and sustain competitive entry until it is well-established”.

Now in the second phase of the project, an options paper was published on 21 December 2015, which set out for consultation a series of retail market regulatory options that could be introduced (in isolation or combination) to the Northern Ireland (NI) gas and electricity retail markets if and when the current retail price controls are no longer required. The timeframe in which any of the options might be implemented following the removal of the current retail price controls is something the UR will consider.

The options presented sought to provide regulatory protection if market conditions at the time suggested that consumers generally were not or may not be adequately protected through competition alone—or that specifically disengaged customers could experience material detriment through supplier pricing practices.

This paper will be accompanied by a UR policy decision paper.

I.2 CMA review linkages

The investigation by the Competition and Markets Authority (CMA) into the GB market commenced in June 2014, and announced its final decision on remedies on 24 June 2016. There are several key overlaps between the investigation and this project on the NI retail markets, as was highlighted in Phase I.

I.2.1 Domestic

The CMA's proposal for a “transitional price cap” for prepayment customers mirrors the concept of an “inactive customer tariff”. Many of the GB stakeholders commented specifically on this option and their concerns should be taken into account when making a decision for NI, especially considering the concerns raised by a number of suppliers. It is however reasonable to assume that certain generic features of customer response will emerge in NI just as they have in GB (and RoI). The most prominent of these is customer stickiness, and we see that many customers in GB and RoI have remained with the former incumbent suppliers.

On this issue, Citizens Advice's commented that there was too much focus on informational remedies in GB. Whilst the NI market has not been open as long—or to the same degree—as GB, there is still evidence suggesting an ingrained consumer stickiness that may need to be combatted with more pro-active prompting or interventions.

I.2.2 Non-domestic

In the GB non-domestic market, the CMA announced several measures that had overlapping principles of those put forward for NI. The Authority's requirement for micro-business suppliers to publish their prices could resemble outputs of a default tariff, should the UR decide to publish the prices. The NI options (through the inactive customer tariff) and the CMA (through the targeted marketing for microbusiness who've been on a default tariff for longer than three years) both sought to mitigate the risk faced by disengaged micro-businesses.

¹ In this report we use the term UR to refer to the executive and supporting team. The term NIAUR, which is the board of the regulator, is not specifically referenced.

² http://www.uregni.gov.uk/news/competition_in_retail_energy_markets_in_northern_ireland_report_published

1.3 Responses

There were 12 responses to the consultation from a variety of NI stakeholders. There was a largely negative response from energy suppliers who responded. Many commented that the options were overly burdensome and would have a negative impact on innovation and operations. There was some support for what were considered to be the less invasive options, such as Significant Market Power and Dominance Thresholds. On the question of whether there should be a period of no price controls, half those who responded to the question were in favour.

1.4 Recommendations to UR

Based on the consultation responses as well as our own independent assessment of the options, we made recommendations on each option based on their suitability for the NI market. Of the seven options considered in this consultation, we have decided to refer four to the UR for further consideration. These are:

- Significant Market Power;
- Inactive customer tariff;
- Default tariff; and
- Dominance thresholds.

The remaining three options are deemed to be unsuitable for the NI market, primarily due to issues related to implementation or being unlikely to have a net beneficial impact.

2 Background and CMA Linkages

2.1 Phase I review

In November 2014, Cornwall Energy published the *Review of Effectiveness of Competition in the Northern Ireland Energy Retail Market*³. This represented the completion of Phase I of a project that was one of the Utility Regulator's (UR's) "flagship" projects highlighted in its Forward Workplan 2014-15. The report laid out the state of retail competition in the NI electricity and gas retail markets. It also made a number of secondary recommendations (e.g. around measures to improve customer switching rates), which are being dealt with separately by the UR outside of this consultation.

The primary findings of the Phase I report were:

- the NI market had achieved reasonable levels of switching given the context of the market and its maturity, and this has resulted in limited competition in the market;
- Power NI (the former electricity supply incumbent) retains a high share of the domestic and small I&C market, with a lot of the pricing strategies of competitors focused on discounting of the Power NI price;
- gas incumbent market shares remain similarly high, with similar pricing strategies as above;
- there are limited players in the energy supply market;
- given the small size of the NI market in both an absolute and a relative sense, this situation is unlikely to change materially and the number of competitors in the market is unlikely to increase; and
- whilst competition has been reasonably effective (up to November 2014), given the characteristics of the market and the lack of sufficient critical mass to attract a larger number of suppliers, relying on competition alone to protect customers may not be sufficient.

The report concluded that the requirement for some form of price regulation was likely to continue for the foreseeable future; and that this form of regulation should coexist with a competitive market. The report stated: "The NI experience strongly suggests that regulation and competition can successfully coexist. Some form of direct price regulation is often necessary to deliver and sustain competitive entry until it is well established."

However, the present price control mechanism remains only on the former incumbent suppliers in the domestic and small I&C sectors and is justified by their ongoing dominance in these price-controlled sectors. This dominance may erode gradually, and could potentially lead to a situation where an incumbent's market share falls to a level where it can no longer automatically be deemed to be dominant in either the domestic or small I&C market. At that point, it may no longer be tenable or desirable in terms of customer protection automatically to retain price regulation on only the incumbent supplier in isolation. Given the tendencies of the NI supply markets described in the Phase I report, the UR is keen to examine its regulatory options going forward in the medium term.

2.2 CMA energy market investigation in GB

On 26 June 2014, the GB regulator, the Office of Gas and Electricity Markets (Ofgem), announced that it would refer the GB energy market for an investigation by the Competition and Markets Authority (CMA). The decision followed a market assessment, conducted by Ofgem, which concluded that a number of features of the market were preventing, restricting, or distorting competition.

As part of its investigation, the CMA was required to examine whether "any feature, or combination of features, of each relevant market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the United Kingdom or a part of the United Kingdom". If this were the case, it would represent an Adverse Effect on Competition (AEC).

³ http://www.uregni.gov.uk/news/competition_in_retail_energy_markets_in_northern_ireland_report_published

The CMA focussed its market assessment on the GB market and did not consider the NI energy markets. But the review is important in the context of this consultation for a number of reasons.

Firstly, the GB retail market has been deregulated for much longer than the NI markets (17 years in GB) and as such experience of market conditions and regulation provides valuable lessons for NI.

Secondly, notwithstanding important physical differences between the GB and NI market (such as market size and the relatively low (but growing) customer access to gas in NI), the assessment and proposed remedies in GB suggest remedies that may be appropriate for application in NI.

2.2.1 Publication of final decision on remedies

The CMA announced its final decision on remedies on 24 June 2016. The measures that the Authority decided to implement in the retail energy market include:

- Obliging suppliers to provide Ofgem with details of all customers who have been on their standard default tariff for more than three years. This information will be put on a database to allow rival suppliers to contact customers by letter and offer cheaper and easy-to-access deals based on their energy usage;
- a transitional price cap for customers on pre-payment meters (PPM), from 2017-20; and
- enabling price comparison websites to play a more active role in helping customers find the best offers for them by giving them access to meter data.

Additionally, in the non-domestic market, the Authority decided to implement measures including:

- requiring micro-business suppliers to publish their prices and no longer allowing them to lock their customers into rollover contracts;
- having Ofgem implement a programme to provide microbusiness customers with different or additional information to promote them to engage in the SME retail energy markets; and
- requiring suppliers to provide details of their microbusiness customers who have been on a default tariff for over three years to Ofgem, so this information may be used for postal marketing.

A more detailed breakdown of the CMA decisions can be found in Annex A.

2.2.2 Reaction to the CMA's provisional decision

Major suppliers

All the Big Six suppliers except EDF Energy opposed the proposed transitional price cap for prepayment meters.

Centrica said it strongly objected to the principle of introducing price regulation for any segment of the retail market as it was inconsistent with the promotion of competition. It said there would be “severe unintended consequences” from the cap, particularly at the unsustainably low price level proposed, which was derived from a “deeply flawed” benchmarking methodology.

Centrica argued that if the cap was set at the low level proposed, it would mean prepayment customers had little incentive to engage in the market to search for better offers. It was said that the effect could also be compounded as suppliers and PCWs will have little incentive to compete with each other or drive engagement with prepayment customers due to “unsustainably low revenues”, and may even force some suppliers out of business.

SSE said the CMA’s assessment of detriment was “not robust, fails to address the available evidence correctly or at all, disregards important factual matters and makes unreasonable assumptions based on no or little evidential support”. This had resulted in significant overstatement of the alleged detriment within the domestic energy market.

Centrica similarly suggested that the introduction of a new detriment methodology at a late stage had raised a number of procedural concerns. The company said the CMA’s plans to include an alleged level of detriment in the final report split by supplier and fuel type was unjustified, and that it would severely damage the suppliers concerned.

Other domestic energy suppliers

Many smaller domestic energy suppliers found room for improvement in CMA remedies. First Utility expressed concern that the CMA's proposals were focused on those parts of the market that were already active and better served by developing competition, and provided too little support for the standard variable tariff (SVT) customers of the Big Six.

Ovo Energy said it felt that the level of consumer detriment in the market justified protections for consumers beyond those on prepayment meters. It called for the introduction of a "social tariff cap"—a price cap that would apply to all vulnerable customers, calculated in the same way as the prepay cap.

Consumer bodies

Citizens Advice said that, in general, it backed the CMA's proposals, but it had concerns that a minority of the recommendations could have unintended consequences. However, the organisation said that the CMA was depending heavily on informational remedies, and that past experience suggested that these did not materially improve levels of engagement. Given that the retail energy market had been open to competition for 15 years, it was likely that consumer behaviour was highly ingrained.

2.2.3 Implications for NI

There are several key overlaps between the CMA's GB market investigation and UR's project, as was highlighted in Phase 1. In particular, the CMA's proposal for a "transitional price cap" for prepayment customers mirrors the concept of an "inactive customer tariff". Many GB stakeholders commented specifically on this option and their concerns should be taken into account when making a decision for NI, especially considering the concerns raised by a number of suppliers.

However, we are mindful that the NI market is fundamentally different from that of GB. This is true in terms of scale, access to gas, role of PCWs, number of suppliers and potential for new entry. We advise that the findings and final decisions taken by the CMA be evaluated in an NI context. For example, marketing codes of practice and the presentation of bills in standardised form have been adopted in NI, to help avoid some of the difficulties that had been observed in the GB market despite its record of longer and deeper competition.

Citizens Advice's view that there is too much focus on informational remedies in GB is also relevant. Whilst the NI market has not been open as long—or to the same degree—as GB, there is still strong evidence suggesting an ingrained consumer stickiness that may need to be combatted with more pro-active prompting or interventions.

2.3 Phase 2 consultation

The options paper published by the UR on 21 December 2015 set out for consultation a series of retail market regulatory options that could be introduced, in isolation or combination, to the Northern Ireland (NI) gas and electricity retail markets if and when the current retail price controls are no longer in place. The timing of the implementation of these options following any removal of the current retail price controls is yet to be decided. This is an important issue, which is dealt with in the accompanying UR policy decision paper.

The options presented in the paper were drawn from desk-based research of energy retail market regulatory approaches in other jurisdictions, which have been introduced to provide protection to some or all customers where competition is judged to have been insufficient to deliver effective outcomes. These included the Australian, US and European markets where initiatives have been introduced with a view to allowing competition and regulation to coexist.

During the development of the options paper we met with a number of NI stakeholders. This was primarily to provide suppliers and consumer representatives with an early view of the work stream and options that are considered in this paper. The stakeholders were introduced to a high-level design of each option, on which they provided feedback. Some of the options are open to all market segments, whilst others could only realistically be implemented in the domestic market. The scope of any option implementation is also dealt with in the accompanying UR policy decision paper.

On 22 December 2015, the UR published a consultation asking specific questions regarding the options provided in the options paper, and views were sought up to 18 March 2016.

2.4 Options overview

The following seven options were put out to consultation:

- **Significant Market Power:** undue preference and undue discrimination licence obligations would be switched on for any supplier deemed by the UR, under established and transparent criteria, to have significant market power (SMP);
- **Inactive customer tariff:** for incumbent suppliers' disengaged customers (not all suppliers as with the default tariff). This option would only apply to the former incumbent energy suppliers- "disengaged" would need to be clearly defined;
- **Default tariff:** for those consumers unwilling or unable to engage with the market. All suppliers (not just incumbents as with the inactive customer tariff) will be responsible for setting their own "fair/reasonable" default tariff and have to clearly show and justify its constituent parts, including the margin being taken under the tariff;
- **Tariff Cap Spread:** limitation on the differences between the most expensive and cheapest tariffs of a supplier;
- **Dominance Thresholds:** setting market thresholds above which if a supplier or suppliers are deemed sufficiently dominant to be able to exert market power, regulatory solutions may be implemented;
- **Gross-Margin Cap:** where suppliers would only be permitted to put rates into the market with a maximum level of gross margin; and
- **Price-to-Beat Tariff:** offer determined by the UR that suppliers would have to match or better.

A more in depth in description of each option can be found in Annex B.

3 Summary of responses

This section details the views expressed by the respondents during the consultation. It begins by summarising the initial thoughts of the suppliers regarding the options presented prior to the consultation. This is followed by a breakdown of the formal responses to the consultation from all respondents. The responses regarding each question and option are followed by Cornwall Energy’s evaluation of them.

3.1 Respondents

Following the publication of the options paper, but prior to the commencement of the formal consultation, Cornwall Energy contacted the suppliers operating in NI to seek their initial opinions on each option in order to inform its approach. Below are summarised the views that the suppliers expressed during our interviews with them. As these were not part of the formal consultation, they are presented anonymously and for indicative purposes only.

There were then 12 stakeholders that responded to the consultation:

- Budget Energy;
- The Consumer Council for Northern Ireland (CCNI);
- Electricity Association of Ireland (EAI);
- Electric Ireland;
- Energia;
- Firmus Energy;
- Flogas;
- Federation of Small Businesses (FSB);
- Phoenix Natural Gas Limited (PNGL);
- National Energy Action (NEA);
- Power NI; and
- SSE Airtricity.

Responses were framed in different ways, which we have endeavoured to reflect without presuming the respondents’ intentions. Some answered each consultation question in turn; some addressed each option; others did both, and a few instead offered more general opinions.

3.2 Considerations

Due to the scope of the research, several of the respondents raised concerns that have not been fully addressed in this paper, such as and legal issues and directives from the EU Third Package.

3.3 Respondents’ views on questions

The paragraphs below set out specific responses from respondents to the questions posed.

Q1. Whether each option strikes a fair balance between the rights of customers and the rights of any supplier which would be subject to that option?

Six responses were received to this question, of which four were from supply companies. There was a general consensus among suppliers that the UR should ensure its decisions are based on firm evidence and that, where possible, adopt a less interventionist approach.

In its response Power NI questioned if the UR was best placed to set tariffs in relation to the options where it would take that role. The company asked if, where the options were “forcing choices on a customer”, the UR was “comfortable assessing an individual’s requirements and deciding what is best for them”. Power NI emphasised that the UR should “focus on enhancing competition rather than considering

measures which will stifle it” and provide an incentive for suppliers to be competitive in terms of price and service, with the penalty for failure being the loss of market share.

SSE Airtricity argued that if the UR has seen fit to remove the current price controls, it could “be assumed that incumbent suppliers no longer hold dominant positions in the market and/ or there is a sufficient level of competition”. However, it said this was contrary to how some of the options are aimed at the incumbents, saying: “There are no longer any incumbent suppliers so there should be no reason to target them specifically.”

Budget Energy responded to this question with reference to each option in turn (See section 3.4).

Electric Ireland agreed that all the options struck a fair balance between the rights of customers and suppliers.

The Consumer Council for Northern Ireland (CCNI) said the current “hybrid” model of price regulation is already acting in consumers’ best interest and called on the UR to ensure that its decisions in regards to the options presented were based on “firm evidence”. Electricity Association Ireland (EAI) took this stance also and said “insofar as all options directly or indirectly interfere with a supplier’s right to engage with customers and in the absence of evidence that prices are unfair or unreasonable, then a balance is not struck between the respective right of suppliers and customers”.

Cornwall Energy response

When looking at the issue of disengagement, we agree that it is important to differentiate, where possible, between those consumers who cannot engage, and those who choose not to do so. A household may never have switched supplier because it is happy with the service it receives, especially given that the omnibus survey in Phase I of this project revealed quite a high level of consumer satisfaction in the NI energy market. However, we feel a balance needs to be found in order to protect vulnerable consumers, and as a result it is possible that some consumers that are happy with their supplier are classified as disengaged.

Addressing SSE Airtricity’s comments, whilst a significant portion of an incumbent’s customer base still consists of those who have never switched supplier, there will be a need for additional regulatory scrutiny.

In terms of evidence for the options, we accept that there is an inherent risk in implementing options without primary evidence of how NI markets will behave after the removal of price controls. In order to minimise risk, we analysed a range of mechanisms implemented in other markets after the removal or relaxation of price controls, with a special focus in those markets closest to NI in size.

Q2. Whether each option strikes an appropriate balance between the protection of customers and the promotion of competition?

This question received responses from seven organisations. While all respondents agreed that consumer protection was of utmost importance, the suppliers raised concerns that some of the options presented could be detrimental to consumers.

SSE Airtricity commented that none of the options allowed competitive forces to reach their full potential, and this in itself was harmful to consumers. It argued that suppliers in NI “already have stringent obligations set out in their codes of practice which ensure customers are protected”, and that these would presumably continue in any future market. At the same time, it said that none of the options facilitate competition, and those regarding sticky customers would “only inhibit competition and could potentially reduce the level of competition and choice for customers”.

Similarly, Power NI noted that “the UR should also be cognisant of the distortive effect of regulated prices [...] on the effective operation of the market”. It also questioned whether further protections were necessary given consumer protection is already governed by consumer protection law, provisions within the Competition Act and the role of Trading Standards.

Energia did not address this question directly, but raised concerns that “some of the tariff controls put forward by the Cornwall Energy report are likely to be punitive to engaged customers by limiting the

products that suppliers are able to offer [and] may result in a market devoid of innovation and competition”.

Electric Ireland took the view that all but one of the options did not appropriately balance customer protection and competition. It said that the “central challenge currently facing the electricity market is to create a level playing field for all suppliers through establishing market conditions for greater competition and choice”, which would be achieved by “reducing the dominance of the incumbent”. Since more than 70% of credit meters were still with the incumbent, it said that this segment should receive particular attention.

Budget Energy responded to this question with reference to each option in turn (See section 3.4). However, its general view echoed that of SSE Airtricity: that the options mostly distorted competition and therefore harmed customers.

However, consumer bodies expressed a contrasting view. CCNI said price regulation protects customers by “ensuring the price they pay reflects the cost of supply, and they do not subsidise cheaper tariffs which are designed to attract more engaged consumers”. It raised concerns that, while many of the options presented would protect consumers to some extent, some options could have a detrimental impact. “Now is not the time to move away” from price regulation, it concluded.

FSB did not raise any specific concerns around consumer protection, but said small businesses should be granted the same level of protection as domestic energy users.

Cornwall Energy response

We do not agree that these options will unduly restrict supplier innovation. Many of these options ensure that suppliers are acting in a fair manner, such as having justifiable final prices and not mistreating specific customer groups or having unjustifiable prices for specific groups, even inadvertently. We would expect that suppliers currently act in this manner, and there would be little to no impact on their ability to innovate. Certain options that would involve restrictive elements could have mechanisms to ensure innovation was not stifled. For example, in the case of a tariff cap spread exceptions would be made to allow suppliers to offer green tariffs or additional services, as was highlighted in the options paper.

In response to Power NI and SSE Airtricity’s comments about existing protection/ legislation, these options would work alongside the Competition Act, ensuring its principles are implemented in an energy context. If a supplier is already fully adhering to consumer law, then these options should not add any significant burden.

Whilst it is true that not all of these options will “facilitate competitive forces to operate at their maximum”, when assessing the options we must again find a balance that ensures consumers are protected. Competition alone may not meet the needs of consumer protection, especially in a market as small as NI, and thus it is important to consider what mechanisms can be implemented alongside a competitive framework.

Q3. Whether each option is likely to protect vulnerable customers (including, in particular, persons who are chronically sick or disabled, of pensionable age, on low incomes or residing in rural areas)?

Six responses were received to this question, of which four suppliers said that the UR should not assume that the options put forward would put an end to fuel poverty or reduce risk to vulnerable consumers.

Electric Ireland was a proponent of a reduction in the dominant market share of the incumbent as a way of leading to greater customer benefit through added choice and value, particularly in the credit meter segment. It took the view that “robust arrangements for the protection of vulnerable customers are already well-embedded in the market arrangements and we do not believe that any of the options would dis-improve this situation”; indeed, it would be reasonable to expect that vulnerable customers would benefit from better pricing outcomes in a more competitive market.

SSE Airtricity took the view that it was “impertinent to assume that vulnerable customers are not in a position to shop around or switch or are in a financially unviable situation”. It added that the current obligations set out for suppliers in the codes of practice already offer vulnerable customers a high level of protection, and so none of the options were likely to affect them any worse than other customers.

Budget Energy said: “fuel poverty among vulnerable customers will unfortunately continue regardless of the level of competition and this issue should mainly be tackled by direct intervention or through the provision of subsidies for those groups most at risk.” For that reason, it took the view that both suppliers and regulators should insist on greater monitoring and enforcement of consumer protection, especially for the most vulnerable group.

Power NI argued that every option represented a “risk to consumers regardless of their vulnerability”, so the least interventionist ones are “best placed to result in a competitive outcome”. It said that the Retail Energy Market Monitoring (REMM) framework already facilitated robust monitoring and could allow the UR to request information from suppliers to justify their actions. This, it said, would be a “more efficient, transparent and cost reflective” option than price control, ensuring the market can operate and enhancing the enforcement of competition law through the availability of information.

The EAI was in agreement that, “given a universal service obligation is in place, measures aimed at regulating prices will affect both general and vulnerable customers equally”.

NEA said the price control applied to the regulated companies “can give us some trust in the market, and that the current mixture of regulation [...] and competition goes some way in protecting consumers”. But it also called on the UR to “play its role in protecting vulnerable consumers by supporting the targeting of energy efficiency schemes to the vulnerable”.

Cornwall Energy response

Whilst we accept the comments that these options will not put an end to fuel poverty in NI, they should provide a level of protection for those who cannot engage in the market, ensuring they are not unduly penalised. The potential benefits for vulnerable consumers, combined with the risks associated with inaction, are great enough to warrant further consideration of the options.

We agree with Electric Ireland’s comment suggesting that added choice and value could stimulate market engagement. However, we maintain that this alone will not be enough to ensure vulnerable consumers are protected, and that there is little evidence to suggest that competition alone will drive this behaviour in suppliers.

Q4. What are the burdens that are likely to be placed on suppliers made subject to each option?

This question received five responses, four of which were from supply companies. There was consensus that any regulatory intervention in the market had the potential to place additional burdens on suppliers, and price setting in particular would require considerable resources from the UR.

Budget Energy said that when prices are fixed, suppliers were always burdened by concerns “over the Regulator’s facility to read the market”, as any mis-judgements could force them to charge the maximum allowed to maintain their profits. Furthermore, Budget Energy argued that “There is no simple – or even complex - way to determine a ‘right level’” for a fixed price, and there will be continual pressure to set and reset a tough price control, ultimately “conditioning the market to be inflexible and unresponsive to dynamic market conditions.”

Similarly, Power NI said that “any option which involves a regulatory price or ex-ante review places a disproportionate burden and regulatory risk upon suppliers.” It noted that price reviews typically take 18-24 months, and warned that as the UR further sub-divides regulated/non-regulated thresholds the processes “only become more complicated and open to error.” It concluded, stating: “Removing the commercial decision making process from the business in question relies on the UR’s ability to get all decisions right.”

Electric Ireland argued that all but one of the options (Inactive customer tariff) brought with it new regulatory conditions, which “would place additional burdens on those suppliers in the form of expanded costs”. These included process design, operation and monitoring, and system change. There may also be an unintended constraint on innovation in the market as a result, it said.

SSE Airtricity answered this question with reference to each of the options (see section 3.4), but overall argued that several burdens were common between the options, saying that under most of them,

“suppliers would no longer be in control of their own business and therefore would not be free to meet commercial needs”. This would result in a “restriction in the activity of affected suppliers and impact on their ability to innovate and compete”, negatively impacting competition, presenting a significant barrier to entry, and potentially leading to market exit.

In its response EAI also raised concerns that dominance and market power obligations were deliberately discriminatory, while the remaining options limited innovation and added system and/ or administrative costs which ultimately would be borne by customers.

Cornwall Energy response

All interventions, to varying degrees, are likely to carry with them some additional burden for suppliers and the regulator. However, as highlighted in a previous response, many of the options being considered are to ensure the market is operating in a fair and appropriate manner. Therefore, those already pricing fairly and acting in the interest of their customers will have little to no additional burden. We will assess in section 4 whether any individual option has an undue burden.

We would disagree with SSE Airtricity’s statement that under most options suppliers would no longer be in control of their own business. Some of the options should have little to no impact on the company’s market activity. For those options that are more interventionist, should they be taken forward, all feasible steps will be taken during the option design to ensure suppliers still have the ability to compete effectively and innovate.

We also disagree with EAI’s comments that the dominance and market power obligations are “deliberately discriminatory” in respect of the suppliers to which they might apply. Neither of these options targets a specific supplier, and the aim of both is to ensure that no supplier(s) has the ability to abuse an advantageous market position. Such interventions are commonplace in several markets.

Q5. Are those burdens disproportionate to the benefit secured and, if so, is there a less intrusive or onerous measure that could be implemented by the UR?

Six responses were given in total, of which four were from suppliers and two from business support organisations.

Power NI was of the opinion that the burdens associated with any form of regulatory pricing, default tariff, price control or margin cap were “excessively onerous”, and advised the UR to look more at competition, active monitoring and step-in measures as better means of facilitating positive consumer outcomes.

Airtricity agreed, saying that most of the options presented a significant burden to the industry while not offering “much in terms of benefit in a market where competition has developed”. However, Dominance Thresholds was seen as the “most realistic” and would probably be “required” in a post-price regulation market.

Electric Ireland did not comment generally but voiced its support for the Inactive Customers option (see section 3.4), specifically if it was focussed on the domestic credit meter customer segment. This, it said, would “deliver the least disruption to current market arrangements with clear customer benefits”.

Budget Energy argued that any setting individual margins would result in a resource drain and risk the UR being “seen to engage in explicit market structuring”, which Budget said was “inherently too far towards protecting customers away from competition.” Reintroducing price controls would also “significantly increase regulatory uncertainty”, and hence the cost of capital, which would be passed on to customers.

The EAI felt that it was not possible to address this question without significantly more detail regarding implementation costs and the impact of reduced competition.

The FSB was in favour of tightening the rules on auto-rollover of tariffs in order to “reduce the risk of exploitation of the smallest businesses by suppliers”.

Cornwall Energy response

SSE Airtricity is correct in saying that “the burden varies on the option”. Many options would be fairly straight forward to implement, as much of the data required will be made available through REMM. We would disagree with Power NI’s comment the additional burden placed by a default tariff would be “excessively onerous”, as under the assumption that tariffs are currently priced fairly then there will be little additional requirement placed on suppliers.

However, we accept that the other options controlling price, such as a margin cap, would place a significant burden on suppliers and the regulator. The aspect of implementation and operational resource requirements is examined in more detail in section four, and whether any additional burden is outweighed by the potential benefits.

Should any option be taken forward, more analysis of the costs and impacts would be required, as EAI suggested. However, at this stage we feel that the potential impact of each option can be gauged through assessing the outcomes of similar actions taken in other markets.

Q6. Do consultees have any other comments on the options put forward?

Five suppliers wished to make additional comments, of which over half were in relation to increasing competition.

SSE Airtricity commented that the “reintroduction of price controls could only be justified if designed in a manner to fix a real issue impacting on competition”. This was because it could risk de-incentivising customer engagement and undermine customer trust. It also highlighted that several of the options were “based on assumptions that are contrary to the current situation in the market”, such as the assumption that prices are comprised of a unit and a standing charge. Finally, Airtricity argued that while the UR had acknowledged that option 7 (price to beat) would be resource-intensive, in fact, almost all the options would be due to the ongoing updates they would require, as well as the need for clear guidance to reduce the impact uncertainty could have on costs to suppliers.

Budget Energy wanted to see more time given to the REMM reporting mechanism to develop before the UR introduces further measures. This would help the UR determine whether the mechanism “provides the required oversight, scrutiny and control of market suppliers”. Additionally, it suggested that “I-SEM and smart meter innovation could increase engagement both by suppliers and customers”, and that this too should be given time to show results.

Firmus acknowledged that the Ten Town Licenced Area had been outside the scope of the consultation, but drew attention to how not one other supplier had emerged to challenge it in the region after a year. It cited a number of different explanations for this, such as the current UR regulated retail margin of 1.5%; high fixed costs for suppliers entering the domestic market; and unfavourable acquisition costs relative to market share possibilities. Firmus inferred that the regulated margin meant no other supplier could justify entering the market for the area, which raised questions of “whether regulation and competition can co-exist in a hybrid state.”

Energia made a general point that the UR’s proposed interventions were premature in attempting to head-off predicted issues rather than addressing known problems, as the CMA’s recommendations for GB had done. Energia said that, “While there is a balance to be struck between reactionary interventions and trying to ensure the market is functioning, designing remedies before any problems have been identified or even begun to surface is counterproductive.” Additionally, it advocated encouraging further competition and customer engagement, rather than “introducing complex tariff rules that have been largely discontinued elsewhere”.

Phoenix Natural Gas Limited (PNGL) noted the importance of continued support to the growth of the gas distribution network by encouraging the “maximum number of connections”.

Of the groups representing suppliers or customers that responded to this question the FSB noted the importance of considering of “how to best protect small business consumers” when evaluating the seven options. The EAI argued that the continuation of price regulation “is contrary to the intent of EU legislation

and the effective functioning of the energy only market.” In its view, price deregulation in Ireland is positive and “should be given consideration” for further progress on this issue.

Cornwall Energy response

Addressing comments about the need for proof of detriment before some options can be considered, we would argue that behaviour in other markets can give a good indication of potential risks NI could face should price controls be removed. Following the removal of price controls it is possible we could see the price discrimination against sticky customers, as is the case in the GB energy market which we have taken as a base case. Given this experience, the implementation of options to mitigate and deter such pricing strategies before they materialise may be appropriate.

We agree with those who commented that increasing competition is an important aspect of improving the market. The scope of this project focuses on options that could be introduced in the period following any removal of retail price controls, and whilst enhancing competition is critical, specific programs for increasing competition fall under a separate work stream within the UR.

Budget Energy’s suggestion that the REMM reporting mechanism be allowed more time to determine whether there is a need for intervention is fair. However, should any of these options be implemented, we believe it will be at a point in the future when the REMM reporting will have been fully embedded and will be able to provide insight into supplier activity at that future point.

PNGL’s comment on the gas network and Firmus’ comment on the Ten Towns area, whilst valid, are outside of the scope of this project.

Q7. Are there any other options not included in Cornwall’s list?

Four suppliers offered additional options to those in Cornwall Energy’s list.

Power NI expressed surprise that Cornwall Energy did not explore EU requirements or “the likely outcomes of a liberalised market with enhanced market monitoring as a base case”. It also pointed out that there was also no indication of a time limit on intervention, which is a European requirement too.

SSE Airtricity recommended that the UR focus on removing barriers to competition, such as through promoting switching via campaigns, and addressing the small size of the market through extending the gas network. Establishing a single gas market would reduce complexity for market entrants, and potentially also cut costs to customers by reducing duplication of processes. Other issues it highlighted included energy theft and greater information availability for customers, such as monitoring of price comparison websites to ensure their impartiality.

Budget Energy would like to see an advertising campaign that focussed on increasing awareness of energy costs and provided information on suppliers and the range of tariffs on offer. It also advocated the creation of independent price comparison websites and the launch of a consultation on “easier switching”. Additionally, Budget Energy suggested that there should be discussion on the benefits of possibly extending “Inactive customer” price controls to all suppliers, for when a customer had remained inactive for a set period of time, such as two years.

Electric Ireland advocated continued deregulation and called for specific criteria to be set out that aimed for “full deregulation of incumbents within a short, defined timeline of not more than 2-3 years”. This, it said, would deliver the basis for an optimal enduring outcome for customers.

The FSB said it would support measures that will tighten rules on auto-rollover of tariffs, to reduce the risk of exploitation of the smallest businesses by suppliers. Additionally, it held up the 2003 *Communications Act* a model of best practice for the way it has the regulator treat the smallest businesses like domestic consumers other than where there are clear reasons not to. This, the FSB said, “would give a much fairer level of consumer protection to these firms.”

Cornwall Energy response

We do not believe that Budget Energy’s suggestion about the possible extension of “Inactive customer” price controls to all suppliers is feasible or necessary. We believe the focus of such an option should be on incumbents as that is where the majority of inactive consumers are situated. An extension of this option

could place a significant additional burden on emerging suppliers, as well as on the regulator who would be required to oversee all the tariffs. Budget's other suggestions to boost switching and competition fall outside of scope of this project.

The suggestion of a period of full price deregulation from Electric Ireland is something which could be considered, and received support from other suppliers in Question eight.

The point which Power NI raised in relation to time limit on intervention is reasonable and it is envisaged that any option (if implemented) would be under continuous review in terms of its requirement.

Q8. Feedback is sought as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring.

Four suppliers responded to this question in total, with mixed support for a period with no price controls. They stressed that if it was to go ahead, monitoring would be crucial.

Power NI said that it “strongly believes that the electricity market should be allowed to operate without price controls”. In its view, the UR has taken significant steps to implement retail market monitoring and enhanced Codes of Practice, so it should now “implement a regulatory framework which is consistent with other markets and thereby align with both European and national objectives.”

Electric Ireland also voiced its support, but said that “critically”, such a period should be subject to a “defined trial period during which target market share expectations [...] for dominant incumbents were set as outcomes of the trial.”

Budget Energy, however, was much more cautious. It argued that the NI market was still fairly immature and more competition would be needed before retail markets could be “allowed to operate with no price controls, subject to enhanced monitoring.” In Budget Energy’s view, price deregulation requires a developed market, warning that “an immediate move to any of the options presented would be not just impulsive at this stage but also counterproductive”.

SSE Airtricity argued that the key issue was certainty, saying that if the UR is serious about removing price controls, it should “set out the criteria that must be met for price deregulation to take place in each market”. It highlighted that the UR had stated in the consultation that the criteria set out for the non-domestic electricity market indicated not the point at which price regulation was no longer required, but the point when further consultation would take place. It concluded: “This does not provide certainty to market participants or customers. Without clear direction from the UR, the future of the market is unclear.”

The EAI said that it would “strongly support” a proposal for a period during which the energy retail markets are allowed to operate with no price controls. It took the view that retail market monitoring measures currently being implemented “would be sufficient to actively monitor the market response.”

CCNI was strongly opposed to the removal of price controls on account of the “significant risk” to disengaged and vulnerable consumers.

Cornwall Energy response

Responding to SSE Airtricity’s call for certainty and clarity, we would argue that it is difficult for the UR to take definitive decisions that would need to be adhered to in the future, when market circumstances may have changed and the decisions are no longer be appropriate.

We believe that implementing a period of no direct retail price intervention following the removal of the current retail price controls comes with a degree of risk. As evidenced in neighbouring markets such as GB, periods of unfettered competition can lead to pricing strategies that result in higher prices for disengaged consumers. Also was stated in Phase I review, given the characteristics of the NI market and the lack of sufficient critical mass to attract a larger number of suppliers, relying on competition alone to protect customers may not be sufficient.

3.4 Respondents' views on specific options

Significant Market Power (SMP)

Key concerns

- Potentially contravenes the EU competition law;
- Concern around returning to price control; and
- Lack of clarity around the option.

Initial informal discussions

In preliminary discussions, suppliers felt that—if implemented—this option should be for all suppliers, not just the biggest, as they all have the same commercial risks.

It was seen as having advantages: it could be effective as a way of transitioning from price regulation to deregulation, and could encourage cost reductions through innovation. However, there was a strong view that it would be difficult and expensive for suppliers to provide the necessary granularity of data for this option to work.

REMM was already seen as overly-burdensome, some suggested, and it was thought that further factors like existing price controls and guaranteed service standards would compound the issue, making it necessary to streamline the processes. It was suggested that additional monitoring should only be on a targeted basis, based on the suspicion of malpractice.

Consultation responses

Of the five organisations to respond directly on this option, four were suppliers. They were moderately positive about the potential for a mechanism like this to be implemented in the NI market.

Budget Energy took the view that the SMP option “boils down to essentially restating in the licence the obligations that are already pre-existent under competition law”. It considered that if the UR chose not to follow the European Commission’s *Competition Guidance Paper*’s dominance thresholds, it would have to select them carefully. Budget Energy also argued that price controls for suppliers who are deemed to be dominant potentially contravened the EU’s competition law review of 2013, which emphasised the distinction between dominance and the abuse of dominance. Such price constraints would, therefore, distort competition, and careful modelling would need to be used so that suppliers are penalised just for “merely experiencing a transitory increase in market power due to a particular innovation or efficiency - to which other suppliers have not caught up.”

Firmus Energy did not express a specific opinion due to the uncertainties surrounding the implementation of this option, which would “depend on the competitive context and on the specific way in which the option is implemented”. However, it did state that it had a “preference for less interventionist approaches to be used where possible”.

Flogas noted that it “seems reasonable that additional licence obligations would become effective” if SMP was identified. However, it said a return to price regulation would not be “appropriate”, since this would “distort competition and potentially discourage switching.”

SSE Airtricity said the option “could potentially strike a fair balance between the rights of suppliers and customers” and assist in the development of competition. It could also prove to be “a less intrusive method of intervention”. However, SSE questioned how the distinction would be made between SMP and market dominance and said the UR would have to set out a clear definition of what it is, when a supplier would be considered to hold it, and what intervention would take place in response.

Several concerns were raised about the effectiveness of the option, or the potential for unintended negative consequences. CCNI agreed that, if SMP was identified, prompt and robust intervention would be required, but argued that the option would “provide limited protection to the customers”.

Cornwall Energy response

We believe this option would constitute a low level intervention and place little additional burden on suppliers, as much of the data will be obtained through REMM, and detail of any additional monitoring requirements would be communicated to the market in advance of implementation. Unlike some of the other options, it is not a price control as such, and could operate alongside a period of open competition.

Whilst we accept Flogas and Budget Energy’s comments that the threat of action could distort competition, we would view this as a small risk that is outweighed by the level of protection that it will provide the market and consumers. Also the removal of price controls without subsequent intervention on tariffs could encourage greater price competition if market conditions suggest high consumer engagement levels.

Addressing Budget Energy’s point on dominance, we agree that having SMP does not mean a supplier will abuse its position. However, given the potential for consumer harm should abuse occur, we believe the additional requirements placed on a supplier would be acceptable.

As legal questions are outside of the scope of our research, we have not addressed Budget Energy’s comment that this option could contravene EU law. Should the UR choose to take this or any option forward, we would suggest a full legal review be performed.

CCNI’s comments are correct in terms of the option providing little specific protection for vulnerable consumers, but more information will be available to assess market conditions and ensure vulnerable customers are not being disadvantaged. Also, any subsequent regulatory intervention could address any specific concerns regarding vulnerable consumers.

Inactive customer tariff

Key concerns

- Inactive does not mean disengaged or disadvantaged;
- Creates confusion in the market; and
- Could actually hinder switching.

Initial informal discussions

Initial views from energy companies were not positive. In the round they considered that any sort of “refuge tariff” would have to be variable, and that customers might not want this due to valuing stable monthly costs. It was thought that suppliers would naturally try and set this as high as permitted, not only from the perspective of profits, but also potentially to try to discourage unattractive customers.

Some questioned if there was actually a legal basis for the introduction of this option, and that it could prove to be a price control in all but name. Further clarity would also be needed on what constituted cost-reflectiveness, and how a fair price would actually be determined.

Consultation responses

Five responses were received regarding this option, with several suppliers questioning the need for such a mechanism and the implications of a customer being “inactive”.

Flogas argued that it was wrong to assume that inactive customers were not getting a fair deal from suppliers, saying “some customers are not interested in switching for a variety of reasons”. It emphasised that having different customers of a particular supplier paying different rates “should not be seen in itself as a problem or evidence that the market is not working”; indeed, it is to be expected that customers who shop around get better deals. Flogas did acknowledge that incumbents with large sticky customer bases may effectively use them to subsidise cheap offerings for new customers, and therefore price-out rivals, but the re-introduction of price regulation was not an appropriate response as it would “distort competition and potentially discourage switching.”

SSE Airtricity was similarly concerned that this option was predicated on the assumption that disengaged customers are being exploited. The company said this option did not support switching and “could have detrimental impact on competition in the market”. SSE also suggested that this would create high levels of

confusion and uncertainty in the market, and “does not strike a balance between the rights of customers and suppliers.”

Budget Energy echoed these views, saying that in “such an immature market” it was “vital to fully understand” the differentiation between customers who choose not to engage, and those who are not capable of engaging, such as due to social or financial circumstances. It also argued that the regulation of Power NI’s prices could be hindering switching, with customers encouraged to trust Power NI’s brand, potentially to their detriment. While customers cannot be forced to switch, education on how the NI electricity market now works should be explored before authorities become convinced that “NI has a market reflective of consumer preference”. Budget Energy suggested the price regulation could be potentially encouraging sticky customers.

Firmus Energy again highlighted the lack of competing offers in the Ten Towns area (which was out of scope for this project), calling the suggestion that a “subset of consumers are in some way inactive and insufficiently protected by competition” was “premature”. Firmus Energy suggested that rather than inactivity being a symptom of competition not working, “existing regulation of margins have been such as to frustrate the emergence of competition”.

However, CCNI felt the option did not go far enough, saying that whilst it would protect some customers while also promoting competition, many customers who had switched in the past but were now disengaged would not be protected.

Cornwall Energy response

Without the granularity to differentiate between those consumers who are disengaged and those who haven’t switched because they are happy with their supplier, a small subset of consumers are likely to be switched tariffs unnecessarily. To a similar extent, we agree it is wrong to assume that customers who are inactive/disengaged are therefore being disadvantaged. These drawbacks would need to be accepted in order to ensure as many disengaged customers are captured as possible, and to limit the potential for abuse, whether or not it currently exists. Additionally, any inconvenience brought about by moving tariffs will be mitigated by the fact that all customers on an inactive customer tariff will benefit financially.

Responding to Flogas and Budget Energy’s comments surrounding engagement, there is a small risk of exacerbating disengagement for some consumers if they feel reassured they are receiving a fair price through price controls. However, we believe that in order to ensure that vulnerable consumers are still protected, interventions on final prices may still be necessary.

Addressing SSE Airtricity’s comment, such a significant shift in the market will undoubtedly cause a degree of confusion, but this can be mitigated by effective communication from the suppliers.

We accept Firmus Energy’s comments that this option has some potential to frustrate competition. In our view new entrants would need to beat inactive tariff price to win customers. Competitors are also less likely to gain inactive consumers as the customer has less reason to engage with the market. These would need to be addressed by ensuring that tariff was set at the correct level i.e. low enough to ensure vulnerable customers are protected, but not so low as to inhibit price competition.

We agree with CCNI’s comment suggesting some consumers who have already switched may have since become disengaged. Those who have never switched should be the UR’s highest priority.

Default tariff

Key concerns

- Potentially contravenes the EU competition law;
- Stifle innovation; and
- Potential barrier to entry.

Initial informal discussions

Preliminary attitudes to this option were particularly negative, with suggestions that it bordered on re-nationalisation, may not have a legal basis, and was essentially the opposite of competition. Some commented that it would not necessarily help vulnerable customers and would cut switching. Furthermore, it could prove costly, as not only would the system have to be set up, but suppliers would need to be compensated for the loss of customers. Suppliers considered that a better solution would be targeted education for sticky customers.

Consultation responses

Of the five respondents who commented on this option, four were suppliers who held mostly negative views on a default tariff.

SSE Airtricity said that this option “in effect is price regulating all suppliers” and questioned its legality. It held that this option would have serious negative consequences for suppliers and may mean that new entrants find they will “never be profitable”. Enforcement would also be difficult given the definition of the “reasonability” of a default tariff, as suppliers “need certainty and clear guidance in order to undertake their business”.

Budget Energy took the view that if a default tariff was to be assessed individually for each supplier on an ex-post basis, then it would be the “least onerous of the price control options” proposed and had the least potential to “stifle further competition”. That, however, did not mean that it would be easy. One risk with a default tariff was the possibility that suppliers would be wary of presenting any sort of innovative tariff “beyond the pricing norms expected” as a default in case they failed to meet the UR’s criteria. Budget Energy also highlighted that under an ex-post regime, default tariffs carry a “spectre of uncertainty” due to the possibility of disputes and penalties over whether or not they are fair. The costs of these will ultimately impact customers.

Flogas argued that domestic suppliers “do currently set their own default tariff, frequently called their Standard Variable Rate”, which reflects their hedging position. The concept of an Industry wide default tariff is therefore “unworkable”, as suppliers have “different cost structures and different attitudes to risk”, and therefore different hedging positions. That said, Flogas thought it would be reasonable for the UR to review default tariffs under the REMM process, so long as sensitive data is not published. Business suppliers, it said, should have the choice of whether to offer a default tariff or not, and they need the opportunity to be innovative in developing products and tariffs.

Firmus Energy addressed this option together with the inactive customer tariff (see above).

However, CCNI was in support of the option, saying it provided a “good balance between protecting the interests of consumers and promoting competition” and provided a “safety net” for disengaged customers.

Cornwall Energy response

We would disagree with the comments that a default tariff is likely to stifle innovation and have negative consequences. For this option, suppliers would set their own default tariff, and the price will be set a level that will be fair and, where requested by the UR, justifiable. Therefore, if suppliers are already pricing their standard tariff fairly, there would be little to no additional burden. Suppliers can still offer a range of other tariffs and thus can innovate. However, clarity will need to be provided around what is meant by “fair”, but this will not equate to the UR setting prices.

For the same reasons, we disagree with SSE Airtricity’s comment that this option would mean that new suppliers would never be profitable. However, we could see this possibly deterring entry if new entrants believe a consequence is insufficient margins can be achieved, and if there is uncertainty on UR’s approach to “fair” tariff pricing. The same is true for what Budget Energy described as a “spectre of uncertainty” due to the possibility of disputes and penalties. These are issues of market perception rather than actual problems with the option, and would need to be resolved by ensuring there is a robust framework and clear communications from the UR.

Responding to the comment from Flogas, we restate that this will not be a market wide tariff. Each supplier will set the price of its default tariff based on its own costs.

Tariff Cap Spread

Key concerns

- Likely to be ineffective;
- Some consumers could end up paying more; and
- Confusing for consumers.

Initial informal discussions

Initial engagement with energy companies had shown this to be one of the more popular options, as it still utilised competitive markets, allowed suppliers to make price decisions, and should prevent price gouging. However, they still raised issues: it was thought that price gouging should otherwise be apparent from REMM data; and that a wide range of price differentials was just the natural result of competition. Setting the tariff spread was also seen as difficult, with a fear that the regulator may assess other markets and choose the lowest spread from them.

Consultation responses

Of the five respondents who commented on this option, several suppliers highlighted what they felt to be some issues with a tariff cap spread.

SSE Airtricity argued that a tariff cap spread already exists as a result of suppliers having to “strike a balance between the option of pricing below cost and above competitor prices.” The UR would have to assess a spread for each supplier based on analysis, it said, and this would have to be highly responsive to changes in market conditions, or else suppliers might not be able to change prices when commercially required. This option therefore “has the potential to confuse customers and may result in a reduction in the number of offers available”.

Budget Energy said that, rather than pinning non-switching customers to the lower prices induced by competition for switchers, this option might have the opposite effect, meaning engaged customers “would potentially be tied to the high prices maintained for disengaged customers”. It also felt it was possible that this option may reduce incentives for suppliers to offer engaged customers attractive fixed priced tariffs, due to “fear that a need to raise the standard variable tariffs [...] due to cost increases would take them outside the allowed spread.”

Firmus Energy addressed this option together with the inactive customer tariff and default tariff (see above).

Flogas was somewhat more positive about this option, saying it “could be of some use” regarding disengaged customers of incumbent suppliers or those with SMP, but otherwise it could hinder fair competition and switching.

CCNI’s considered this to be a useful option for encouraging suppliers to seek innovative means of reducing costs. This, it said, would enable them to “offer cheap tariffs and attract new customers, while protecting disengaged customers from unfair high prices.” It added though that any cap on the spread between cheapest and most expensive tariffs should protect vulnerable customers and households in fuel poverty.

Cornwall Energy response

Responding to Budget Energy’s comment about engaged customers on more expensive tariffs as a result, we would agree that there is a potential for suppliers to increase the price of their cheapest tariff, rather than reduce their most expensive. As a result, inactive vulnerable consumers could see no change in price.

We disagree with SSE Airtricity’s comment that the option would be confusing to consumers. The tariff spread cap would limit how supplier’s set their tariffs, but should be invisible to consumers. The supplier suggests that there will be a reduction of tariffs as a result, which we accept is possible, which could actually reduce confusion in the market (without the negatives brought about by the four tariff cap in GB).

Dominance Thresholds

Key concerns

- Concern about automatically returning to price control;
- Dominance does not mean disadvantaged; and
- Too mechanistic and inflexible.

Initial informal discussions

From preliminary talks with suppliers, a persistent view emerged that this option would punish success, as a dominant position did not indicate guilt of poor practice or abuse of market power. It would also make suppliers wary of being the Supplier of Last Resort as they might gain customers through a market exit and then be penalised.

As with other options there were also potential legal issues highlighted, as price controls cannot be re-introduced without evidence that consumers are being harmed. Suppliers said that instead, implementing a price floor or forced divestment would make more sense than a price control. Alternatives would be limits on marketing spending, or the preparation of a roadmap to determine how dominance could be reduced.

Consultation responses

Dominance thresholds were looked on more favourably than some of the options, though support among suppliers was qualified.

Flogas said it was appropriate to set thresholds as they provided a “safety net”. However, it also argued that full re-regulation of the dominant supplier’s prices should be a last resort, with the Tariff Spread Cap being “a preferred alternative.”

SSE Airtricity felt that this option had “merit” and would have been an option had the market been fully price de-regulated. However, it was effectively “re-regulation” of prices. SSE said that customers “may not necessarily be negatively impacted by the dominance”, but it has implications on competition and suppliers, and will be quite onerous after the current price regulations have been removed. SSE concluded that the reintroduction of price controls could only be to fix a “very real and serious” adverse effect on competition. It added that this option “achieves customer protection and can protect competition, but only if it is clear to all what the dominance threshold is.”

However, Firmus Energy felt an option such as this could result in the “mechanistic application of a test that does not adequately capture the relevant market context”. The company added that it would prefer a more principle based approach that required assessment of the particular market context, rather than “hard wiring” metrics.

Other respondents also commented on the idea of reintroducing price controls as part of this option. CCNI said a conventional price control once a supplier had become dominant “may prevent the exertion of market power, and protect its disengaged and vulnerable consumers from that stage on”.

Cornwall Energy response

Rather than punishing the successes of a supplier, as some market stakeholders suggested, we believe the option mitigates concerns with market power for all suppliers and prospective new entrants, and also sends clear signal to market on how dominance is determined.

Similar to the comments we made for SMP, we agree that being dominant does not mean a supplier will abuse its position. However, given the potential for consumer harm should abuse occur, we believe the additional requirements placed on a dominant supplier would be acceptable.

The UR’s action to tackle dominance would depend on market conditions at time, and it would need to communicate at early stage as it become apparent a supplier(s) may become dominant. This would not necessarily be a return to price controls, and could be a combination of one or more of the options discussed in that paper. However, the intervention may be a return to price controls for the dominant.

Firmus Energy’s comment is one that should be taken under consideration. We still feel that the threshold should be a fixed series of metrics that equate to dominance, but there should be some flexibility, and an investigation or consultation should be triggered that takes in account market conditions.

Gross-Margin Cap

Key concerns

- Difficult to implement;
- Stifles innovation; and
- Barrier to entry

Initial informal discussions

Perhaps the least popular option from initial talks, this was seen as both difficult to implement and anti-competitive. There were concerns that it lacked a legal basis, and would be hard to set due to the unpredictability of the commodity market. It was described as just another form of price regulation, and could hurt both investment and market entrants through its restrictions. Should it be pursued, a lot of aspects would need to be firmed up, such as how it would work with brokered prices, what would happen with over- and under-recovery, and how long each review period would have to be

Consultation responses

No respondents said this would be a suitable option should price controls be lifted in NI.

Budget Energy suggested that, since this option has largely been drawn from current regulation active in Australia, “it may be instructive to further explore the Australian experience”; particularly the fact that the Independent Pricing and Regulatory Tribunal has reached the view that price regulation is no longer necessary in New South Wales and that measures targeted at customer groups were a better option. Budget Energy added that while price controls had been successful in Australia, this was in the context of a move away from price regulation, and it was therefore illogical “to steer towards a means of regulation that is currently being steered away from in the area in which it is currently implemented.”

Firmus Energy again saw this option in the context of the Ten Towns, where regulated margins were—in its view—extinguishing any interest in competing in the region. Furthermore, it noted that gross margin takes into account operational expenditure, so the fixed market entry and start-up costs “may also be frustrating competition.”

Flogas opposed an industry-wide Gross Margin Cap due to it being intrusive, failing to account for different hedging strategies, and potentially restricting competition and innovation.

SSE Airtricity agreed, saying that the purpose of this option was unclear in an interim or post-price regulation market since it is “reminiscent of price regulation”. The company explained that it could not see how this would support competition or protect consumers in a competitive market, and echoed the view of Firmus that the current low margin cap in the domestic gas market was not attractive for new entrants. It added that “Clear guidance would need to be provided to new entrants as to when price regulation will be applied to them.”

While the CCNI believed that consumers would be protected by this option, it would require “significant additional work” for the UR, and customers would be unlikely to understand the process due to its complexity.

Cornwall Energy response

We accept comments that this option could have some drawbacks, particularly around implementation, which will need to be taken into consideration when choosing whether or not to take it forward. As highlighted by several respondents, there is a significant risk associated with setting the cap. Should the cap be set too low suppliers struggle to cover costs (particular “shocks”) and deter entry as margin could be deemed insufficient for a viable business. Conversely, if cap is set too high the intervention may deliver no

material benefit to disengaged customers. This onus would be on the UR to ensure the cap is set at the correct level, which would pose a significant additional burden on the regulator, as CCNI commented.

Addressing comments around competition and innovation, we agree such an option could have a negative impact. Should the cap be set too low, there would be less incentive to compete and win customers, and thus less need to innovate. This could lead to market where supplier's commercial decisions are guided by the regulatory framework rather than a competitive market.

Flogas' comment about taking into account hedging strategies is one that should be considered should this option reach the design stage. The outcome of such a mechanism should not be to impede how a supplier chooses to hedge its wholesale position, or restrict it from investing the company.

Price-to-Beat Tariff

Key concerns

- Resource intensive for regulator and suppliers; and
- Difficult to set at the correct level.

Initial informal discussions

Initial reactions to this option from energy companies were also largely negative for the same reasons as the gross margin cap: it would be complicated, with a lot of risk borne by the regulator, and prolonged disputes between them and suppliers. It would also restrict longer term deals, failed to account for the composition of a supplier's customer base, and was not providing clear protection for any customer types.

Consultation responses

No respondent was clearly in favour of a price-to-beat tariff being implemented.

Flogas described this option as "counterintuitive", as the public would see it as price regulation for all suppliers, with the UR as the price setter. It would be "very complicated and time-consuming and potentially open to error", as well as not accounting for variation in hedging.

In addition to the issues it had raised that were common to all price-fixing options, Budget Energy's singular main concern was that the 'price-to-beat' "potentially provides a higher focal point for default prices to settle".

SSE Airtricity and CCNI had similar comments, both saying the implementation of price-to-beat tariff would be "resource intensive" for both suppliers and the UR due to the need for constant updating. SSE considered that it would be "very difficult for the UR to develop a 'reasonable price' which takes account of all supply costs and reasonable margin"; some suppliers would probably benefit considerably and others not at all. This too was price control, to all intents and purposes, and supported neither customer protection nor the promotion of competition.

In a similar vein, Firmus Energy agreed with the view of Cornwall Energy that it would "lead to consumer confusion and extensive levels of monitoring and analysis". Firmus argued that such an option would do nothing in the Ten Towns region due to the lack of alternative suppliers, and would not adequately reflect the market context.

The CCNI had mixed views on this option, arguing that to ensure protection of vulnerable consumers the charge to cover fixed costs "should be levied in relation to the amount of energy used, rather than as a flat rate for all customers", as otherwise it would inhibit the ability of customers to keep bills low by minimising their energy use. It deflected claims that this option might lead consumers to think that the UR endorses the highest-priced tariff in the market, arguing instead that "the current Power NI price control effectively sets a price for competing suppliers to beat [...] The Consumer Council has not encountered evidence suggesting consumers regard UR as endorsing the highest priced tariff in the market."

Cornwall Energy response

We accept that there would be some issues with this option. The option would likely place a significant resource burden and risk on the regulator to establish a methodology that adequately represents supplier costs that results in all suppliers being able to beat the price and ensure the market remains competitive.

We agree that many of the risks discussed for the gross margin cap are applicable here. Should the price-to-beat be set too low, it could hinder market entry and competition, and if it is set too high it could create a higher focal point for default prices, as Budget Energy suggested.

As CCNI commented, any price-to-beat tariff would need to be based on consumption (such as a capped unit rate) rather than a fixed cost per year. This would ensure customers of all consumption levels would be protected.

4 Conclusions and recommendations

Based on the consultation responses as well as our own independent assessment of the options, we have made recommendations on each option based on their suitability for the NI market. Each recommendation can either be:

- *No further action* - Given the evidence available, we do not believe this option would be suitable in an NI context; or
- *Refer to the UR* - This option has been potential to operate effectively in an NI context. We recommend the UR consider implementation after removal of price controls. The exact timing of any implementation would be decided closer to the point of the removal of the current controls.

4.1 Significant Market Power

4.1.1 Ease of implementation

The option itself should be relatively easy to implement through a licence condition. As described in the December 2015 consultation paper, the licence approach also provides regulatory latitude to determine SMP in the context of the market environment at the time.

4.1.2 Risks

As was suggested by some respondents, the threat of action could distort competition. We believe this to be a minor risk that is outweighed by the level of protection that it will provide the market and consumers.

The outputs of REMM are still unproven, and for such an option to be effective the UR and stakeholders need to ensure it is providing meaningful and timely data. The UR also needs to clearly define SMP and implement a robust framework so as the market is not left in uncertainty for the future.

4.1.3 Benefit

Several respondents agreed that a mechanism such as this would be of benefit in a market where price controls had been lifted. We see it as an important tool to signal to all market participants that there is a mechanism to monitor market power. The enhanced monitoring would allow UR to react to emerging issues more rapidly where SMP is found, as opposed to have only Competition Act powers to call upon. This is also an option that could sit alongside a period of competition and monitoring following the removal of current price controls. The removal of price controls without subsequent intervention on tariffs could encourage greater price competition if market conditions suggest high consumer engagement levels.

All suppliers would know that where SMP was determined by the UR, the supplier(s) would be required to refrain from undue discrimination, undue preference, predatory pricing and unduly onerous terms. In practice, the REMM framework should provide early indications of where a supplier's market power could begin to give rise to consumer and competitive detriment and therefore enable dialogue to commence at an early stage.

The removal of price controls without subsequent intervention on tariffs could encourage greater price competition if market conditions suggest high consumer engagement levels.

Whilst there is little specific protection for vulnerable consumers from this option, increased information will be available to assess market conditions and could be used to help ensure vulnerable customers are not being disadvantaged. Also, any subsequent regulatory intervention could address any specific concerns regarding vulnerable consumers.

4.1.4 Supplier burden

The implementation would be unlikely to add any significant burden to suppliers, as much of the data required would be available through REMM. Detail of additional monitoring requirements can be communicated to the market in advance of implementation.

4.1.5 CE recommendation

Refer to UR

We believe this is a “light touch” form of regulation, and any potential distortions to competition that were highlighted by some respondents, are outweighed by the protection it would provide domestic and business consumers.

4.2 Inactive customer tariff

4.2.1 Ease of implementation

In our view, which is shared by a number of respondents, there would be a number of difficulties implementing such a tariff, and it could be particularly challenging for incumbent suppliers and the UR to maintain. In essence this option would see the continuance of price controls for the currently price controlled suppliers’ inactive customers.

As highlighted by several respondents, one of the difficulties with implementing this option is that any reasonable means to define “inactive” will inevitably capture some customers that do not require direct regulatory protection and miss some that do. In addition, the resources required to establish (and change) the inactive tariff would likely be significant and be incurred by a decreasing fraction of the incumbent supplier’s customer base.

4.2.2 Risks

We would have a concern that such a tariff could act a barrier to entry, depending on how low the price is set, as new entrants would need to beat inactive tariff price to win customers.

We accept the comments from stakeholders that this may further dampen the incentive for such customers to seek out better offers. However, this may be an issue that reduces over time as the market matures and consumer proficiency, knowledge, and access increases over time. Also, a consumer on an inactive tariff is likely have the same mentality as in the current price controlled market, which has recently experienced in increase in switching facilitated by new supplier entry.

4.2.3 Benefits

Where implementation issues can be tackled, the outcome should be a net benefit for inactive customers through lower bills.

The key benefits for this option would be ensuring disengaged consumers are receiving fair terms. An indirect impact of this could be an increase in engagement prompted either by:

- the supplier – incumbents may choose to contact customers before forced to move them; or
- consumers –notification of the movement onto an inactive tariff may prompt consumers to engage. We feel the wording of the tariff name to be very important in this regard, and should be standardised across all suppliers.

4.2.4 Supplier burden

In our opinion, this option would come with a fairly high burden for suppliers. The process of identifying applicable customers and then migrating them to the inactive tariff is likely to be relatively resource intensive.

4.2.5 CE recommendation

Refer to the UR. Consider the learning points from the proposed transitional safeguard price cap for GB from the CMA

We note that the CMA’s transitional price cap for the GB prepayment market has similarities to this option. Both are measures that seek to address acknowledged disengagement from customers, many of whom will be vulnerable. However, there are some key difference in the markets and options that detract from its suitability in an NI context. For example in GB:

- the focus is only on prepayment consumers;
- the market size is considerably larger; and

- the intervention is transitional until the smart meter roll out is complete (currently expected for December 2020), and is not considered a long-term option.

Despite these differences, we believe such an option would function well in the NI market, if the above points were taken into account when it is being developed. In addition, the fact that a similar mechanism is being implemented in a neighbouring market will provide a good learning experience. The option could mitigate the potential abuse of unilateral market power, which in GB the CMA determined is a position only held by former incumbent suppliers.

4.3 Default tariff

4.3.1 Ease of implementation

A default tariff would need to be implemented through licence condition. The UR would also need to develop methodology to determine how to assess if default tariffs are justifiable. Suppliers would need to put in place management process and systems to ensure prices can be justified

4.3.2 Risks

The regulatory risk noted in consultation responses will need to be carefully considered. Any third party determination of a “fair price” introduces commercial risk. It may be possible to ameliorate this risk through guidance (which, for example, recognises that supplier costs are incurred/ change over different timescales or each has different competitive strategies) and acknowledgement that the overriding consideration is that the customer on a default tariff is not exposed to undue detriment.

4.3.3 Benefits

The benefit of this specific approach is that in the NI market context it can provide assurance that as the relatively small retail market matures and current price controls lapse, consumers can always access a tariff that is deemed to be fair. We favour this option as it puts the onus on suppliers and is therefore less resource intensive than some of the other options. With the establishment of REMM, the UR will also have a significant basis of information in order to question suppliers on their default tariffs.

The approach would allow the UR to gain better insight and knowledge of how supplier costs are factored into very different business models (e.g. new entrants compared to ex-incumbents) and so, over time, improve its own view on what is deemed to be fair. This would provide a level of transparency as suppliers would need to be forthcoming about the margins they earn from the default tariff—either publically or privately with the UR.

Provided the implementation of this option was undertaken in a consultative and constructive manner between industry and the UR it should ensure all suppliers (existing and new entrants) can continue to offer innovative services and keenly priced tariffs outside of their default tariff (if they so wish). The introduction of the default tariff should also be a spur for greater competition between suppliers for customers on such tariffs (e.g. Supplier X offers the cheapest default rate which could induce a switch) and to test the market with new tariffs.

4.3.4 Supplier burden

This option would place a fairly low burden on suppliers as it works much like the market at present. The biggest additional burden would be putting in place management process and systems to ensure prices can be justified.

4.3.5 CE recommendation

Refer to the UR. Consider the learning points from the proposed transitional safeguard price cap for GB from the CMA

The strength of this option lies in its similarity to the market at present, whilst still sending a clear message to suppliers around fair pricing. Suppliers would have to offer a “default” tariff that would be open to all consumers, and then have to be able to, if necessary, justify this price to the UR. Under the assumption that suppliers are currently pricing fairly, we would foresee little impact on pricing strategy or regulatory requirements, with ensuring transparency of the tariff being the main additional burden.

It would also need to be decided whether the concept of a “fair” price is a licence binding obligation. If enshrined in licence, the UR could take action on supplier’s who cannot justify their price, or have been found to be “unfair”. Alternatively, “fair” could be principle put forward by the UR, and whilst still providing the same transparency, the onus is on suppliers to meet the requirement without potential regulatory reprimand. This would be more in line with Ofgem’s move toward principles based regulation.

As evidenced by many of the responses to the consultation, there is some confusion amongst stakeholders around what exactly a default tariff would entail, and many of these misconceptions form the basis of much of the criticism. Should this option be implemented, we would recommend further stakeholder engagement to ensure there is sufficient clarity amongst stakeholders. Without clear boundaries of what is considered “fair”, a degree of uncertainty could deter entry if new entrants believe a consequence is insufficient margins can be achieved.

4.4 Tariff Cap Spread

4.4.1 Ease of implementation

The implementation of the option would be complex, given the need to determine on the basis on which the cap was based. The UR would require significant resource to determine an appropriate spread and put in place a methodology that was sufficiently responsive to cost changes and did not introduce unnecessary commercial risk for suppliers (which we assume would ultimately result in higher charges for customers). As highlighted in the December consultation paper, customer annual consumption levels would result in very different actual spreads between low and high consuming customers and could lead to consumer confusion.

4.4.2 Risks

We find that if a tariff cap spread were implemented, it would possibly result in no overall benefit to customers. Depending on the level of the cap spread, the option would see a narrowing of tariff offers (on the assumption suppliers offer more than one tariff) which in turn could reduce engagement as the benefits of switching would be lower. It may also, as was seen with a similar intervention in the GB to reduce regional price differences, result in supplier pricing behaviour that increases the cheapest offers more than expensive offers are decreased. Therefore, inactive vulnerable consumers may see no change in price as active customer offers rise so that a supplier is compliant

A tariff cap spread could also limit introduction of multiple tariffs, depending on how the cap is defined (e.g. for average tariff, by consumption levels etc.). The option would need to be designed in such a way that it does not impede a supplier’s ability to innovate, such as with green tariffs.

Despite the complexity, there could be various workarounds for suppliers (e.g. provision of rewards, inducements, vouchers etc.)

4.4.3 Benefits

A potential reduction in price gouging could result.

4.4.4 Supplier burden

This would place little additional burden other than the restriction on how suppliers price their tariffs.

4.4.5 CE recommendation

No further action

This would be a complex option to implement that may have little or no overall benefit, and could result in the cheapest tariffs increasing in price.

4.5 Dominance Thresholds

4.5.1 Ease of implementation

The option itself could be implemented relatively easily through a licence condition. It also has a relatively low regulatory burden for suppliers, and the UR could monitor it through REMM data. However, there may need additional system requirements for suppliers and UR.

4.5.2 Risks

Several respondents commented that dominance thresholds risk being too mechanistic if no qualitative measures are considered alongside the quantitative metrics. Despite this, we feel that for this particular option it important to have a fixed series of metrics (market share, Herfindahl-Hirschman Index, number of suppliers in the market, etc.) that denotes dominance in order to a send clear signal to existing and prospective suppliers and the wider market.

4.5.3 Benefits

In our view this option would send clear signal to market on how dominance is determined, and would mitigate concerns with market power for all suppliers and prospective new entrants. In a potential future where price controls are lifted due to the incumbents no longer dominant, this option would provide a “safety net” against the re-emergence of dominance.

4.5.4 Supplier burden

This option is unlikely to add any significant burden, as much of the information for monitoring will be obtained through REMM. However, should a dominance threshold be exceeded, then the specific supplier burden is likely to increase.

4.5.5 CE recommendation

Refer to the UR

If this option were implemented, it would need to be determined whether action would be taken when dominance materialises, or when there is actually evidence of harm as a result of the dominance. We would also suggest that there would need to be a considered approach as to what happens in the event of the dominance threshold being breached. Reinstating price controls may not be in the best interests of the market and consumers, and we would suggest that a dominant supplier could be subject to one or more of the options in this paper, depending on the circumstances at the time.

However, we feel it important that when dominance is observed, an investigation / consultation be triggered rather than the` automatic implementation of another option. In this circumstance, the competitive landscape can be assessed before any action is taken, if at all.

4.6 Gross-Margin Cap

4.6.1 Ease of implementation

The option would require significant resource from the UR to determine an appropriate cap (and to ensure the methodology is sufficiently flexible to adapt to changing market costs and conditions) and has the potential to introduce regulatory risk to the market and reputational risk for the regulator.

Gross margin caps for individual suppliers would be possible, but more complex. They would also run the risk that competitors could infer more easily supplier operational costs and approach to trading. A market wide cap would be set such that more efficient suppliers would more easily price offers that were competitive and retained reasonable margins.

4.6.2 Risks

In our view, the option is unlikely to have a net-beneficial impact on the market. As highlighted in some of the responses, the primary difficulty with this approach (as has been evidenced in other markets) is that the UR would need to set the cap at a rate (for all suppliers or, as significant extra resource cost, individual suppliers) that it deemed sufficient to allow companies to maintain sufficient profit to grow and adapt, while keeping end prices reasonable.

Many suppliers highlighted they have different costs that they are exposed to over differing timeframes, and in some instances will incur unexpected costs that they have little or no initial sight of.

If the cap is set too low it could deter new entry and/ or result in suppliers paring costs down to a point service levels also fall. Where it is set too high (and on the assumption switching levels and engagement are

deemed unsatisfactory) it would allow suppliers to price above costs and what they may have independently determined to be the desired margin.

4.6.3 Benefits

It is possible that this option would reduce risk of price gouging of disengaged consumers, and ensuring they are on fairly priced tariffs.

4.6.4 Supplier burden

This option is likely to place a significant burden on suppliers; due to the negotiations with the UR when the cap is being consulted on, as well as the additional processes for subsequent tariff calculations. The obligation itself would be audited against financial accounts and REMM data submissions.

4.6.5 CE recommendation

No further action

This would be very complex to implement and maintain, and is unlikely to have a net-beneficial impact for consumers.

4.7 Price-to-Beat Tariff

4.7.1 Ease of implementation

Similar to several of the respondents, we would have concerns around this approach as it requires the UR to take a view on what price it deems necessary for suppliers to beat. This in turn would place significant resource burden and risk on the regulator to establish a methodology that adequately represents supplier costs that results in all suppliers being able to beat the price (without jeopardising their businesses) and ensure the market remains competitive. For example it could reduce incentive to switch if all prices in the market are very close to the price-to-beat tariff rate

4.7.2 Risks

A price-to-beat tariff could drive a price-centric market that encourages suppliers to reduce operating expenses by cutting investment in customer service and innovation.

Even where the option could be implemented reasonably it may result in suppliers pegging their tariff to the price-to-beat tariff rather than in response to competitor offers and their own cost base. Conversely where the price-to-beat is swinging it could deter new entry and encourage supplier cost cutting to the detriment of service levels.

4.7.3 Benefits

It is possible that this option would be to reduce risk of price gouging of disengaged consumers, and ensuring they are on fairly priced tariffs.

4.7.4 Supplier burden

This option is likely to place a significant burden on suppliers; due to the negotiations with the UR when the price to beat is being consulted on, as well as the additional processes for subsequent tariff calculations.

4.7.5 CE recommendation

No further action

This would place a significant resource burden on the regulator, and the potential benefits are outweighed by the risk to suppliers should it be set at an incorrect level.

4.8 Recommendation summary

Based on the consultation responses as well as our own independent assessment of the options, we made recommendations on each option based on their suitability for the NI market. Of the seven options considered in this consultation, we have decided to refer four to the UR for further consideration. These are:

- Significant Market Power;
- Inactive customer tariff;
- Default tariff; and
- Dominance Thresholds.

The remaining three options are deemed to be unsuitable for the NI market, primarily due to issues related to implementation or being unlikely to have a net beneficial impact.

5 Annexes

Annex A – The Competition and Markets Authority Final decision on remedies

Overview

In June 2014, Ofgem announced its decision to refer the UK energy market to the Competition and Markets Authority (CMA) for a market investigation. After an extended investigation, the CMA announced its final decision on remedies on 24 June.

The measures that the Authority has decided to implement in the retail energy market include:

- obligating suppliers to provide Ofgem with details of all customers who have been on their standard default tariff for more than three years. This information will be put on a database to allow rival suppliers to contact customers by letter and offer cheaper and easy-to-access deals based on their energy usage;
- a transitional price cap for customers on pre-payment meters (PPM), from 2017-20; and
- enabling price comparison websites to play a more active role in helping customers find the best offers for them by giving them access to meter data.

The retail markets

The CMA explained that gas and electricity prices had increased significantly over the past decade. Average domestic electricity prices have increased by around 75% in real terms between 2004-14, while gas prices were up by 125% over the same period.

The report reaffirmed the CMA's view that consumers were continuing to fail to take advantage of the significant benefits of switching suppliers. It found that the savings available to customers have risen substantially over the past couple of years, and reached an equivalent of £330 in the second quarter of 2015. This was deemed evidence of weak customer engagement in the retail markets—a problem that was seen as particularly pronounced among PPM customers.

The CMA remained of the view that the Big Six exercised unilateral market power over their inactive customer base, and that they had the ability to exploit this position through pricing their standard variable tariffs at a level that could not be justified by cost differences. It did, however, reject the idea of tacit coordination between suppliers in relation to pricing announcements.

The detriment to domestic customers of the Big Six was estimated to be £1.4bn/ year on average between 2012-15—and this was on an upward trend, reaching £2bn in 2015.

Prepay customers

The CMA reaffirmed its view that competition was significantly weaker for prepay customers compared to other customer groups. Gains available to prepay customers who switched to a credit meter roughly doubled between 2013-15, reaching between £290-£370 in the second quarter of the year.

Price cap

Acknowledging that it would take some time for the remedies to have a significant impact, the CMA has decided that it will, as proposed, introduce a transitional price cap for prepayment customers—lasting from 2017 to the end of 2020.

The measure will take a “reference price and cost index approach”—an initial level of the cap will be set based on the CMA's competitive benchmark analysis, and this will then be allowed to change over time according to movements in cost indices.

The cap will not apply to SMETS2 meters when these are rolled out to prepay customers as they will have access to a wide range of tariffs.

Retail Market Review

The report's evidence on the impact of the regulator's Retail Market Review (RMR) reforms found that customer engagement did not appear to have improved materially, and fundamental doubts were raised about the point of the four-tariff rule. The rules had also been harmful in their impact on price comparison websites.

The CMA has therefore decided to make a recommendation to Ofgem to remove a number of standard licence conditions relating to the "simpler choice" component of the RMR rules—including the ban on complex tariff structures, the four-tariff rule, the restrictions on the offer of discounts, and the restriction on the offer of bundled products.

Remedies to improve engagement

On the back of its criticisms of the impacts of RMR, the CMA is seeking a more evidence-based approach to developing engagement-related interventions in the future. Ofgem will be recommended to establish an ongoing programme to test measures to promote engagement in the household retail markets, and introduce a licence condition requiring suppliers to participate.

The CMA has also confirmed suppliers will be required to disclose details of customers who had been on their standard variable tariffs for three or more years, to be stored in an Ofgem-controlled database. The regulator will be advised to retain and disclose this information to rival suppliers, and disengaged customers would have the option of opting out of the disclosure process.

In order to strengthen the incentive of price comparison websites to engage customers, the CMA is planning to recommend to Ofgem that it remove the Whole of the Market Requirement in the Confidence Code, and that it introduce a requirement for websites to be transparent over the market coverage that they provide.

DECC will be advised to make several changes to the Midata Programme to give price comparison websites increased access to customer data and consequently monitor the market on behalf of customers so as to advise them of savings.

Seeking to place emphasis on principles rather than detailed rules, the CMA will recommend to Ofgem that it introduce an additional "standards of conduct" into SLC 25C that would require suppliers to take account, in designing their tariffs, the ease with which customers could compare value for money with other offerings in the market.

Microbusinesses

The report's analysis suggested that the Big Six had, in supplying energy to SME customers, made profits in excess of the cost of capital amounting to approximately £220mn/ year from 2007-14. Around £180mn of this related to microbusiness customers.

Suppliers will, under the CMA's plans, be required to disclose the prices of their available acquisition and retention contracts to a large proportion of their microbusiness customers. Suppliers will also need to disclose their out-of-contract (OOC) and deemed contract prices on their websites. Not only will this improve microbusiness customers' ability to compare price information, it should support the development of price comparison websites catering for these customers and accordingly reduce high search costs. The remedies will further prohibit termination fees for evergreen and OOC contracts.

Additionally, the CMA recommended that suppliers should have to disclose to Ofgem details of their microbusiness customers who have been on default tariff for three or more years, and regularly update this. The information will be held securely by Ofgem and—unless microbusinesses opt out—be made available to rival suppliers (subject to safeguards) so that they may target marketing materials at the disengaged customers.

Next steps

The changes will be delivered through a combination of CMA Orders and recommendations to Ofgem and the government. The CMA will shortly publish a timetable detailing this remedies implementation process over the next six months.

Annex B – Option descriptions

1. Identification of Significant Market Power and consequent licence conditions

The starting point to this option is in the current licence conditions (condition 14 in current electricity supply licences and condition 2.5.5 in Firmus's gas supply licence for the Ten Towns) which state where a supplier is deemed dominant in any market it must not show undue discrimination or undue preference to any customers in that market where it is deemed to be dominant, or set prices that are unduly onerous or predatory in that market.

Terms in respect of particular consumers shall be taken to be “unduly onerous” if the revenue from supply on those terms: significantly exceeds costs in respect of those consumers; and exceeds such costs by significantly more than in the case of the generality of consumers supplied in the same market. However (unless the converse is manifestly the case) terms shall not be taken to be unduly onerous if other suppliers have more onerous terms.

2. “Inactive customer” price controls for Power NI, Firmus and SSE Airtricity Gas Supply

This option would apply only to former incumbent suppliers at the point the UR determined that current retail price controls were no longer tenable. In its place Power NI, Firmus and SSE Airtricity Gas Supply would be subject to a price control for their customers that had never switched i.e. “inactive customers”.

As the suppliers in the market with by far the highest number of customers that have never switched, the incumbent suppliers would be in a position where, compared to their competitors, in a future where current price controls lapse, they could raise their disengaged customer prices to fund cheaper offers to more engaged customers. This could potentially result in the following detriment:

- disengaged/inactive customers pay significantly more for their energy, with the potential that an element of their bill is used to offer engaged customers “loss leading” tariffs; and
- other suppliers without a large rump of customers that have never engaged with the market are unable to compete against the lower tariffs offered by incumbents.

This type of concern is real, and this behaviour has been highlighted by the CMA in its energy market investigation—Summary of provisional findings report where it states “weak customer response gives suppliers a position of unilateral market power concerning their inactive customer base and that suppliers have the ability to exploit such a position through their pricing policies”.

The incumbent supplier would be allowed to offer any tariffs and offerings it liked to customers in the market, except those identified as disengaged. For the disengaged customers it would have to supply under a tariff agreed with the UR. The setting of this tariff would mirror the tariff setting process of today.

In effect this would divide the incumbent suppliers’ retail businesses into price regulated and price unregulated parts, as is the case today for NI price regulated suppliers who have price regulated and unregulated I&C sections within the one business. The change would be that the domestic sectors within these incumbent businesses would be split into price regulated and unregulated, following removal of the current form of price control frameworks whereby now the domestic sectors of these businesses are totally price regulated.

3. “Default” tariff

Suppliers would be obliged by licence condition to offer a set of “default” tariffs that would be open to all customers. These default tariffs would be variable tariffs and be set by the individual supplier. There would be three default tariffs, one for each payment type of Direct Debit, Prepayment and Credit in Arrears. Each default tariff would be shown including any discounts for the payment type included so customers could easily compare the default tariffs of each supplier. Customers that were not being supplied through a tariff that was cheaper than the default tariff (for that payment type) would be migrated to the default tariff for their payment type at the end of their fixed term offer (unless they chose another cheaper tariff or to switch to another provider). Also where a supplier’s customers are supplied via a variable tariff they would

be switched to the default tariff for their payment type unless their current tariff was cheaper than the default tariff of that payment type.

The default tariffs would be set by the supplier with the company moving customers to them in the circumstances outlined above. The tariffs would be variable and this would ensure that prices can be changed as the supplier's cost base moves and that customers are not exposed to a termination fee typically associated with a fixed term tariff.

The default tariffs would be offered for prepayment and credit meters. The UR may mandate the titles of all NI suppliers default tariffs (these titles to be used by all suppliers) so as to avoid customer confusion when comparing the default tariffs of various suppliers. The three default tariffs must also be shown with any discounts for payment type. Any further discounts a supplier may want to offer would need to be via other variable or fixed tariffs not the default tariffs.

The terms of the tariffs would be such that it would ensure that disengaged customers would not be exposed to tariffs with unduly high margins that could be used to offset that supplier's other offers to attract engaged consumers—e.g. prevent the possibility of disproportionate cross subsidy between sections of a supplier's customer base.

It is important to note that while the UR would oblige the creation of default tariffs, it would be for the individual supplier to set the prices. The UR would monitor the tariff rates as part of the REMM process and expect all suppliers to clearly and transparently justify their cost elements (wholesale, network, supply, policy/tax, margin) to the UR in a manner to be determined by UR. This obligation to justify the tariff rate as fair would also be a licence obligation. The UR would have the right to ask any particular supplier to give further details justifying the cost elements or have those costs audited by a third party. The UR would pay particular attention to the cost elements which the supplier has some or complete control over: wholesale, operating costs and profit margin.

The UR may also require that suppliers publish all or some of the cost elements of their default tariffs. This would also need to be enshrined in a new licence obligation and the UR would consult with stakeholders on the form and content of any such publication obligation at the time of modifying supply licences to include default tariff obligations.

4. Tariff cap spread

Licence conditions would require all suppliers (including new entrants) to price offers within a defined spread to ensure that disengaged customers are not subject to charges that are not cost-reflective and could enable a supplier to offer a "loss leading" cheaper tariff to consumers that can and/ or choose to interact with the retail market. The licence condition would take effect the moment current price controls were removed and would apply to all new offers from that point forward. It would also be necessary for the licence condition to give the UR the ability to alter the spread in response to changing evidence and market conditions.

The rules would apply to tariffs a consumer could avail of by meter and payment type. The tariff cap spread would need to be defined as a maximum price difference between cheapest and most expensive expressed as a percentage of a typical annual bill. This would be for *all* tariffs. Provisions could be introduced for "green" tariffs where a supplier could justify additional costs as a consequence of the customer willing to pay a premium for an additional environmental benefit. The situation in the industrial and commercial market would be complicated where some customers would take a bespoke contract rather than tariff.

5. Dominance thresholds

Where a supplier or suppliers hold in isolation or combination a high proportion of the overall market share the UR would take action to ensure that the supplier(s) could not use dominance to exert market power.

This option differs from others presented here insofar as regulatory action would only be invoked once a predefined threshold had been crossed. It is worthy of inclusion though as it could work in conjunction or isolation with other proposals and is framed to ensure consumers are protected where the market tends to monopoly/ oligopoly.

The fact that dominance reappears in a market (on the assumption that the transition to retail competition has been successful insofar as original incumbents have had their market share competed away to a point the retail price controls are no longer deemed necessary to protect consumers and facilitate competition) presents a challenge for regulators.

On the basis that the newly dominant supplier(s) has reached a position through fair means in an effective market it suggests that its prices and services are the most attractive to consumers and so preventing it from offering the same to a greater number of consumers could be seen as resulting in detriment. Moreover these concerns with dominance would differ from those related to a previously public entity operating in a newly created market as all (as opposed to some in the case of an original incumbent) consumers would have, at some point, actively engaged in the market.

Nonetheless market dominance in any market could give rise to outcomes that are to the detriment of consumers, other competitors, other markets (i.e. wholesale markets) and wider socio-economic considerations.

It is important to note that, where a supplier is dominant it will be subject to Chapter II of the Competition Act 1998 and will be precluded from abusing its dominant position. Under Articles 42(5A) and (5B) of the Energy Order, before taking licence enforcement action against a supplier for abusing a dominant position, the UR is required to consider whether it is more appropriate to use its concurrent powers under the Competition Act. It would only be after this consideration that the licence conditions required to implement this option would be put in place.

6. Gross margin cap

Suppliers would be obliged to provide offers to customers within a maximum gross margin (as defined below). It is expected that tariffs with a lower gross margin would be available and the cap set to ensure that no customers, particularly those that have not or choose not to switch suppliers, are exposed to unreasonably high tariffs.

The obligation would be enshrined in supply licences and audited against financial accounts and REMM data submissions.

7. Price-to-beat tariff

The regulator would determine a tariff rate that all suppliers would have to match or better. The price to beat tariff would represent a reasonable price that took account of all supply costs and a reasonable margin. To give effect to the option it would be necessary to underpin the obligation in licence or possibly secondary legislation. Mechanisms would be in place to change the tariff rates in response to changing market conditions.

The tariff would comprise two elements: a standing charge to recover suppliers' fixed costs and unit rate to cover volume based charges. This would ensure an equitable approach for all consumers with different consumption levels.

Appendix II
Budget Energy Consultation
Response

Budget Energy’s response to the specific questions set out in the UR Consultation paper “Review of Effectiveness of Competition Phase II” regarding the options provided in the Cornwall Energy paper. These responses apply to both Domestic and I&C Customers where appropriate.

Q1. Whether each option strikes a fair balance between the rights of customers and the rights of any supplier which would be subject to that option?

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Q2. Whether each option strikes an appropriate balance between the protection of customers and the promotion of competition?

Budget Energy would respond to the above questions by outlining their thoughts on each option as follows:

Option 1) SMP + Option 5) Dominance Thresholds

As the Northern Irish electricity market is relatively immature, a market participant with an SMP position in Northern Ireland could give rise to it becoming the “price setter” and in turn preventing competition. Significant Market Power as defined in the Cornwall Report lifts its definition from the Directive 2002/21/EC which is:

“if, either individually or jointly with others, it enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers.”

The Cornwall Report states that this isn’t quite dominance – which is inaccurate. The core components of SMP match the definitions of dominance as set out in:

- 1) *Hoffmann-La Roche & Co v Commission*, Case 85/76 [1979] ECR 461 paras 38-39
- 2) Paragraph 10 of The Guidance on the Commission’s enforcement priorities in applying Art 102 to abusive exclusionary conduct by dominant undertakings (Guidance Paper).

The 1998 regulatory framework within telecommunications National Regulatory Authorities could designate as having SMP where they possessed 25% market share per Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C 165/03) para 3. However, from this guideline document it is clear that SMP is being further aligned with dominance to the point where they are largely the same thing.

We would advise that Budget Energy, and all suppliers, already have obligations under:

- 1) Article 102 (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions; (TFEU) and
- 2) The Competition Act 1998, in particular section 18(2)(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions.

The SMP option therefore boils down to essentially restating in the licence the obligations that are already pre-existent under competition law. Thus this option might be dealt with alongside Option 5 regarding dominance thresholds.

In terms of dominance thresholds careful thought would be required as to what the thresholds would be if they were different than the above EU Commission Competition Guidance Paper. We welcome however that an assessment of dominance would be a multifaceted approach rather than a pure market share threshold.

The re-imposition of price controls upon presumptively dominant suppliers based on market thresholds raises the issue of *“dominance is not prohibited, dominant activities are not prohibited. Only certain activities are abusive activities.”* (Prof Diarmuid Rossa Phelan as stated in the European Competition Law Review in 2013)¹. See also para 34 of the Competition Authority’s response to CER Review of the Regulatory Framework for the Retail Electricity Market.² To impose price constraints based on dominance that will presumptively arrive from a non-incumbent given the context of the options could be perceived as punishing success. Thus the threat of pre-emptive action could distort competition. This is a point raised again the aforementioned Irish Competition Authority Response to the CER Consultation stating that re-imposition of price control could seriously damage the competitive process.

The risk is also run if proper and full market assessment is not conducted, then onerous price regulation may be placed on suppliers that are merely experiencing a transitory increase in market power due to a particular innovation or efficiency - to which other suppliers have not caught up. In this scenario competition will be unreasonably distorted. Fortunately, REMM may be able to aid in preventing this by providing historical market data. Ultimately this falls under the issue of dynamic economic modelling which is discussed in response to our response to Question 8. Thus there is further consideration required for CMA involvement if this option is implement to ensure accurate market share assessment and correct economic modelling of the potential detriment to consumers upon the occurrence of transitory dominance.

¹ Diarmuid Rossa Phelan “The Dynamic Unprohibited Nature of Dominance”, 2013 34(6) ECLR

² [http://www.cer.ie/docs/000818/cer10058\(e\).pdf](http://www.cer.ie/docs/000818/cer10058(e).pdf)

We note that the Cornwall Report raises the concern about *“the potential for oligopolistic pricing and associated customer detriment if price controls are removed too quickly.”* There is the potential for Competition Law to prevent as tacit collusion in oligopolistic markets is covered within abuse of dominance per *Impala v Commission* Case T-464/04.

It must also be considered that the various Telecommunications Directives and Regulations put in place regimes and mechanisms integrating relevant National Regulatory Authorities and the EU Commission as regards competition. Thought would need to be put about whether and how these should be integrated into the NI electricity market with consideration given to the current deliberate overlap between the CMA NIAUR.

Option 2) Inactive customer tariff for incumbent supplier

Budget Energy would be of the opinion that there is a good argument to suggest the effect of a large block of incumbent inactive customers has been to create two retail markets: one is competitive, comprising of active switchers; and the second group is likely to be less able to engage in the market.

We believe it's important to distinguish between customers who are unable to engage for either their social, or financial circumstances and those who choose not to for various reasons. We would propose that analysis on the differentiation is vital to fully understand this situation in such an immature market. There is also an argument that Power NI's price regulation could potentially be encouraging sticky customers and therefore hindering switching. In the immature Northern Ireland market, it is reasonable to assume that customers may not be switching for a misinformed reason: it is likely that customers in Northern Ireland still associate PowerNI with NIE who have “always been there”, who “own” the grid and will therefore always be able to provide the service. In this way they are trusting a brand – but perhaps to their detriment. It is important to note that customers cannot be forced to switch, but education surrounding the Northern Irish electricity market could be communicated more proactively by the Regulators and CCNI. We would suggest this option is explored before we truly can believe NI has a market reflective of consumer preference. Notwithstanding, the situation remains that the existence of too many inactive customers will be damaging for both consumers and competition.

Option 3) “Default Tariff”

Budget Energy appreciates the issues that the Cornwall Options paper have outlined with regards to, amongst other things, *ex ante* consideration of the tariff or having the default tariff priced the same across the market so that disengaged market customers. As noted in the Options Paper these issues are open to consideration with regards to this option but also directly relate to the other options proposed and thus in depth discussion of these considerations will take place within those further options. However, at this stage the point is made that if the default tariff is assessed on an *ex post* basis and individually for each supplier that it is considered by Budget Energy to be the least onerous of the price control options put forward in terms of the burdens it places on suppliers and its ability to stifle further competition. Several concerns may be expressed however even on the aforementioned provisos and these are dealt with in turn:

- 1) We believe that an assessment of Ofgem’s regulation of the GB market shows that attempts to correct perceived market inefficiencies or address aspects of the market which are having an adverse effect on competition have been largely ineffectual and have actually had unintended consequences in limiting competition. This is clear from the CMA’s approach and provisional conclusions in assessing the market after its referral from Ofgem. Illustrative of this is that with regards to the ‘simpler choices’ component of the Retails Market Review (which was aimed promoting more customer involvement through banning complex tariffs and placing a maximum limit on the number of tariffs), has actually had an adverse effect on competition.³ Further illustration of this is the approach taken in the Notice of Provisional Remedies asking for responses on the potential of unintended consequences regarding price regulations, this is an implicit recognition of the likelihood that regulation of this sort will be highly likely to have unforeseen consequences which may adversely impact the competitive of the market and customers.⁴
- 2) One of these unintended consequences is likely to be to stifle innovation on the part of suppliers in terms of the tariffs they offer to customers. This can occur through concern on the supplier’s part that any tariff that it offers to be a default beyond the pricing norms expected will not fit UR assessment methodology even if it would better suit those not engaged in the energy market. In this regard take the example of the now

³ https://assets.digital.cabinet-office.gov.uk/media/559ad883e5274a155c00001b/EMI_PFs_Summary.pdf - para 87

⁴ https://assets.digital.cabinet-office.gov.uk/media/55a908c3e5274a6fea000013/Stephen_Littlechild_-_Submission_to_PFs_and_notice_of_possible_remedies.pdf paras 95 (c and m)

defunct E. ON 'staywarm' tariff which allowed a set amount to be paid regardless of consumptions. There will be a burden, regardless of whether real or perceived, likely or unlikely, to defend which may ultimately deter the supplier from introducing the tariff innovation in the first place. Furthermore, whilst the issues surrounding *ex ante* assessment of tariffs have been partially outlined in the Cornwall Options Paper and are discussed further below it must be acknowledged that default tariffs under an *ex poste* carry with them the spectre uncertainty with regards the potential regulatory burden of either defending the tariff as 'fair' or enforcement action as a result of an assessment that the default tariff is unfair. This increase in regulatory uncertainty directly results in increased cost which will ultimately be placed on customers at their detriment. Thus there is the potential for consequences averse to competition and to customers in that innovation serving customer needs is deterred.

- 3) Innovation and serving customer needs is also likely to chill somewhat due to default tariff as it is likely to deter switching behaviour due to the potential of these tariffs being seen as backed by the UR. In this case, any savings incurred by the customer in terms of hunting out a better deal is unlikely to be seen as valuable, as the perception could be that as the tariff they are on is UR backed it must not be too far outside the 'best deal' available under current market conditions. If switching lowers from its already low rate or calcifies at its current rate there will be little incentive for suppliers to innovate or bring new tariff types to the market. This will ultimately be to the detriment of customers as it is not unlikely that business models will refocus on being able to extract the largest margin from the default tariffs whilst avoiding regulatory action which will therefore turn this soft price regulation into a hard price regulation similar to the other options below and the difficulties they present.

Given the above concerns and potential outcomes Budget Energy would submit that when viewed alongside the wish that the UR refrain from setting out explicitly what margins would be acceptable or be seen to giving informal guidance on price setting customers may be placed 'between a rock and a hard place'. Whilst not explicitly setting out pricing guidance this increases regulatory burden and as a result increased costs whereas setting prices means reducing switching and a refocusing on extracting the most amount of margin. Furthermore, it is the opinion of Budget Energy that the reticence of the UR to give informal guidance won't totally be avoided by *ex ante* as informal or indirect guidance may accrue over instances of enforcement or assessment or margin creep without enforcement.

As a follow up given already low levels of switching it is likely given predisposition to default tariffs, given customers a UR sanctioned tariff would potentially reduce incentive for them to switch. As a result of the reduction in switching in combination with a lack of clarity on acceptable pricing it may be that this makes the market conducive to oligopolistic pricing with suppliers looking to each other to set an acceptable tariff that avoids regulatory enforcement. This would then further reduce the incentive to switch and would again cause a refocus of business model as above.

Budget Energy acknowledges that the aim of the default tariff would be at least in part to prevent price discrimination, that is to say prevent those disengaged customers from being exposed to tariffs with high margins to offset offers made to attract engaged consumers. However, Budget Energy would point towards the growing economic view that this may be a competitive market outcome and not one that should necessarily be regulated to avoid per se. In this regard please see the following quote from William J Baumol (emphasis added):

*“... in a broad range of market types and conditions, where consumers can be separated into distinct groups with different demand elasticities and in which the market’s commodity cannot easily be resold by one group to another, market pressures will prevent any equilibrium in which the product price is uniform. Not only will each firm be forced to adopt discriminatory prices, but each firm is likely to be forced to adopt a unique vector of prices, each of which is dictated by the market. Thus this paper seeks to show why price discrimination may occur – and may occur frequently - not despite relative ease of entry (of other competitive pressures) but because of it. **In fact, I will show that in highly competitive markets, firms may have no choice. Competition can force them to adopt the vector of profit-maximizing discriminatory prices.**”⁵*

Thus the imposition of a default tariff to avoid discriminatory pricing may be considered to be the undue imposition of the UR’s concept of ‘fair’ outcome to the detriment of competition. It is also worth noting that the CMA in their Notice on Possible Remedies have decided not to pursue the introduction of price non-discrimination provisions and would direct the UR to the reasoning of the CMA for this.⁶

⁵ William J Baumol, Regulation misled by misread theory, Perfect competition and competition-imposed price discrimination, 2005 Distinguished Lecture, AEI-Brookings Joint Center for Regulatory Studies, Washington DC, 17 March 2006, pp 2-3,

⁶ https://assets.digital.cabinet-office.gov.uk/media/559aac8eed915d1592000023/EMI_Remedies_Notice_-_Final.pdf - para 48 - 50.

4) Tariff Cap Spread

The core concern to be expressed by Budget Energy is that rather than protecting those disengaged in the market by tying them to the lower prices induced by the competition for those customer who are engaged in the market rather tying potentially reduce incentives to switch for engaged customers, due to the potentially limited differences between each end of the tariff spectrum. Thus as a result rather than the disengaged customers benefitting by being pinned to the engaged customers' lower rates, the engaged customers would potentially be tied to the high prices maintained for disengaged customers. Another potential unintended outcome might be that suppliers would not be have any incentive to offer engaged customers attractive fixed priced tariffs due to the fear that a need to raise the standard variable tariffs that many disengaged customers due to cost increases would take them outside the allowed spread. Additionally, there are issues detailed below with prospectively set price regulations due to inadequate economic modelling.

6) Gross Margin Cap

We note that this option is lifted from current regulation active in New South Wales and several other Australian States. Thus it may be instructive to further explore the Australian experience as a means to review this option. To that end Budget Energy would draw the attention to the UR to the following submission from the Independent Pricing and Regulatory Tribunal to the Australian Energy Market Commission, a view that the Commission largely agreed with:

"We consider that electricity and gas price regulation is no longer necessary in NSW given that the retail electricity and gas markets now protect customers against market power by offering more choices and better price and service outcomes. We consider that the removal of retail price regulation is likely to:

- Improve customer engagement in the market by removing the confusion in relation to the difference between regulated and market prices*
- Remove the risk that price regulation distorts the competitive market, particularly given the dynamic nature of energy markets. This will encourage retailers in to the market and thereby deliver better customer outcomes in the long term, including better 'value for money' service through reduced costs and/or innovation.*

Retail price regulation cannot protect customers from price increases driven by regulatory policy and market factors, nor can it protect vulnerable households that may be experiencing affordability problems. Rather, it is important to ensure that any specific groups of customer that cannot readily access the competitive market, or require financial assistance, are specifically considered and targeted responses are developed."

What is clear from the implementation of price regulation in Australia is that it was successful as a part of a process away from price regulation, there is an important point to be made that the end goal was the removal of regulations and that as price regulations has been removed competition was stimulated. Moreover, the price regulation was not wholly successful in protecting all customers rather it seems from an analysis of the price setting that some customers ultimately ended up paying more than the estimated efficient prices however this was deemed as necessary to allow development of the market ultimately inducing longer-term efficiency. Therefore, we would suggest that the model of Australia and New South Wales does not support the imposition of price regulation as an end in itself. At the very least it seems illogical to steer towards a means of regulation that is currently being steered away from in the area in which it is currently implemented.

7) Price-to-beat

The singular main concern particular to the ‘price-to-beat’ option is that it in the words of the CMA in the NPR (para 93) it “*potentially provide a higher focal point for default prices to settle.*” However further general issues applicable to this option are set out in our answer to Q4&5.

Q3. Whether each option is likely to protect vulnerable customers (including, in particular, persons who are chronically sick or disabled, of pensionable age, on low incomes or residing in rural areas)?

In addition to Budget Energy’s answer to Q2, the detriment to all customers would be especially reflective when considering vulnerable customers. We would draw your attention to the comments made to the AEMC Review which Budget Energy supports:

“Retail price regulation cannot protect customers from price increases driven by regulatory policy and market factors, nor can it protect vulnerable households that may be experiencing affordability problems. Rather, it is important to ensure that any specific groups of customer that cannot readily access the competitive market, or require financial assistance, are specifically considered and targeted responses are developed.”⁷

Budget Energy believes that fuel poverty among vulnerable customers will unfortunately continue regardless of the level of competition and this issue should mainly be tackled by direct intervention or through the provision of subsidies for those groups most at risk. We note that the CMA is exploring the possible contributions of smart meters to assisting vulnerable customers. However, some vulnerable customers may have difficulty with changing technology. Vulnerable customer will

⁷ IPART submission to AEMC Review, 2013 p2

need more personal contact, advice and assurance. This raises the question of face-to-face marketing.

There is a necessity, and obligation, for both Suppliers and Regulators to insist on ongoing monitoring and enforcement of consumer protection when introducing competition, this is particularly imperative when dealing with the most vulnerable group. In the UK consumers experienced a number of problems with energy suppliers using aggressive techniques and misleading information – especially with doorstep selling. Budget Energy believes that regulated price setting with the intention of ‘protecting’ vulnerable consumers could instead provide a focal point for price coordination between suppliers, which is adversative to competition. Furthermore, as regulated prices tend to discourage innovation in tariff design, there is an argument that vulnerable consumers could be robbed of new products that best suit their needs and preferences.

Q4. What are the burdens that are likely to be placed on suppliers made subject to each option?

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Q5. Are those burdens disproportionate to the benefit secured and, if so, is there a less intrusive or onerous measure could be implemented by the UR?

Additional to Budget Energy’s concerns in relation to the burdens highlighted for each option in answer in Q2 we would outline that the core concern with price setting in a wider sense, whether it take the form of a direct price-to-beat, tariff spread capping or gross margin cap is that core to their success is some form of prospective market analysis.

Markets and competition are necessarily dynamic and alter over time, this is a basic concept that is clear and appreciated even in core concepts of competition law. For instance, see the EU Commission’s competition guidance on market definition, paragraph 12 acknowledging how different time horizons may impact market definition,⁸ or explicitly set out in para 16 of the Commission guidance on article 102 TFEU enforcement priorities⁹. Accepting competition as a dynamic process means that a premium is put on innovation as a competitive driver over more static concerns such as price or output. Put succinctly *“dynamic competition models entail the prediction of future competitive outcomes”*.¹⁰ Key to a dynamic concept of competition is the innovation of

⁸ **Commission Notice on the definition of relevant market for the purposes of Community competition law, Official Journal C 372 , 09/12/1997 P. 0005 – 0013.**

⁹ **Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, (2009/C 45/02)**

¹⁰ Douglas H. Ginsburg & Joshua D. Wright ‘Dynamic Analysis and the Limits of Antitrust Institutions’ (2012) 78(1) 1.

products and processes over and above more static concerns such as price or output. The issue however is that dynamic modelling is prospective modelling and any enforced reduction in present tariffs will make a rival supplier's offerings less attractive. In so doing, the ability of new entrants to compete and reduce the incentives for customers to engage will be reduced. This could send the message that customers are thereafter to be protected by regulation, not by competition or their own action. Thus, reintroducing price controls will not merely protect customers while the CMA's other remedies take effect and these customers gradually become more engaged. Rather, by actively restricting the growth of competition, it will militate against the working of these other remedies, and defer the day when (in the CMA's view) customers are fit to be allowed to engage in the market unsupervised.

There is a dichotomy between 'one size fits all' and the resource drain of setting individual margins which runs the risk of the UR being seen to engage in explicit market structuring which is inherently too far towards protecting customers away from competition. Artificially keeping suppliers in the market is not the way to obtain customer benefit. The Cornwall Paper does acknowledge the risks in setting prices on a market wide basis rather than taking account of each supplier's individual situation and costs. Reintroducing price controls will also significantly increase regulatory uncertainty, hence the cost of capital. In short, customers will pay for this higher cost.

The IEA's views are worth citing explicitly on this point:

"Regulated prices can significantly delay the timely development of dynamic and innovative retail markets, with significant economic costs for consumers and the potential to substantially reduce effective customer choice and demand response. They can serve as policy-induced 'focal points' for standardisation of competitive behaviour, with the potential to induce tacit collusion in the market. Standardisation of prices, whether resulting from the actions of cartelists or regulators, has the potential to undermine new entry, reduce choice and discourage innovation. They can seriously distort supply-side incentives, which might also distort efficient and timely investment responses needed to ensure future reliability and affordability."

If the restrictions are set too tightly it will have a damaging impact on competition, undermining incentives for customers to switch, which will in itself chill any innovation on the market and the undermine the ability of suppliers to best serve customer's needs. Essentially both set out a pricing formula that must be followed which deters any deviation to a creative product which may better

suit customers. If set too loose then it provides no protection for customers with the option to simply price to ceiling.

In price fixing there is always a burden for suppliers in a market place to be concerned over the Regulator's facility to read the market – if a Regulator is incorrect with regards to tariffing it would mean that suppliers will be forced to price the maximum allowed i.e. price to beat or the gross margin and then when the market's prevailing conditions allow them to lower the price away from these thresholds, they will further reticent to do so as they may ultimately be forced to make up any losses incurred. In that situation, the UR could be at risk of fundamentally conditioning the market to be inflexible and unresponsive to dynamic market conditions.

The proposal ignores the practical and political considerations associated with price controls. There is no simple – or even complex - way to determine a 'right level'. There will be great pressure to set and reset the price control toughly, to demonstrate that it is of benefit to customers. The existence of prices in the market lower than the default price will be taken as a sign that the regulator has not been tough enough. There will be pressure to continue and tighten the control with little or no pressure to remove it.

Q6. Do consultees have any other comments on the options put forward?

Budget Energy would suggest that the increased information provided to the UR through the REMM reporting mechanism should be allowed some time to develop to determine if this provides the required oversight, scrutiny and control of market suppliers to achieve the objectives of the UR before additional measures are sought to be introduced.

We believe that both I-SEM and smart meter innovation could increase engagement both by suppliers and customers in the market and that appropriate time should be allowed in the market for these to develop.

Q7. Are there are any other options not included in Cornwall's list?

A lot of the initiatives proposed in the various options centre on trying to engage 'inactive or unwilling' customers. And a general focus on customer engagement. Budget Energy would suggest that some measures that could be adopted to try and engage the sticky customers are:

1. A concentrated advertising campaign undertaken by the UR (TV/Radio/Social Media/Print) on behalf of the suppliers in Northern Ireland and funded by the suppliers to make

consumers aware of all the various suppliers in the market, that different tariffs exist and the benefits of switching supplier

2. A campaign focused on increased awareness of energy costs and suppliers carried out in schools to begin to educate the next generation
3. Encourage creation of independent price comparison sites with the ability to switch customers, again through a concerted advertising campaign and some funding by suppliers
4. A consultation by the UR on ways of making the switching process easier for consumers
5. Discussion over whether it may be beneficial to extend 'inactive customer' price controls to all suppliers where inactive customer is one who has been inactive for a period of time, say more than two years.

Q8. Feedback is sought as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring. This consultation seeks views on whether there should be a period of deregulation or an immediate move to any of the options presented.

Budget Energy would advise that the ideas presented in answer to Q7 are 'soft' awareness options to promote customer engagement therefore switching therefore a more competitive market. We believe that a more competitive market in Northern Ireland would be required before it is possible to have a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring.

We would reiterate that the Northern Ireland electricity market is in its immature phase and customers not switching is not necessarily indicative of an uncompetitive market. Although Cornwall puts forth that switching is good for market maturity, it is premature to see the Northern Ireland market as having reached its peak switching figures. Budget Energy's view is that price deregulation requires a developed market and an immediate move to any of the options presented would be not just impulsive at this stage but also counterproductive to the developing competition which is at an early stage.

Appendix III

CCNI Consultation Response



**Review of the Effectiveness of Competition in the Northern
Ireland Energy Retail Market – Phase II Regulatory
Implications: Options for Consultation**

1. Introduction

- 1.1. The Consumer Council welcomes the opportunity to respond to the Utility Regulator's (UR) consultation on the review of the effectiveness of competition in the Northern Ireland Energy Retail Market – Phase 2 Regulatory Implications.
- 1.2. The current system of pricing for domestic and small business electricity and natural gas consumers in Northern Ireland (NI) is a combination of price regulation and unregulated competitive pricing. The Consumer Council believes this 'hybrid' model is currently delivering benefits for consumers. As such we would not advocate a transition from the system at present.
- 1.3. While the current system is broadly delivering benefits to consumers in terms of overall cost, UR must be sure all consumers are benefitting. The Consumer Council has worked with UR in preparing its Consumer Protection Strategy (CPS). This document has an action plan to ensure all consumers, in particular vulnerable consumers, receive the full benefits that the current 'hybrid' system offers. We will continue to work with UR, the energy industry and other stakeholders to help deliver proposals within the CPS.
- 1.4. While price is the most important issue for energy consumers, other factors such as innovation, new technology and customer service are also important. UR is continuously monitoring the market, identifying

the benefits and detriments to all consumers of the current system and considering options to deal with problems that arise.

- 1.5. The current review is welcome because it sees UR looking forward and recognising the existing system may not always be appropriate for NI. UR is quite rightly preparing for a market that may change and considering the options if it does. Before it comes to making significant and possibly irreversible changes to the domestic energy market, UR must ensure its decisions are based on firm evidence.

2. The current benefits of price regulation in NI

- 2.1. Currently price regulation is providing NI domestic and small business consumers with the following benefits:
 - Lower prices than GB or RoI;
 - Transparency that provides confidence the price is a fair one;
 - Significant savings when switching electricity supplier; and
 - Price protection for disengaged (non-switching) consumers.

3. Comparison with the GB market

- 3.1. It is a clear policy aim of the European Union to liberalise the energy markets of member states and at supply level remove price regulation. When considering the merits of the current 'hybrid' system in NI, it is useful to compare the situation in other markets. Most EU countries still have some form of price regulation for domestic consumers. Meanwhile,

the GB electricity and gas markets are the most liberalised in Europe, having had no price regulation since the 1990s.

4. Prices

4.1. NI has recently seen a round of price cuts averaging around 10% from both electricity and gas suppliers. In GB a number of the largest suppliers have reduced their prices by around 5%. With all these changes in place by 1 April 2016, NI domestic natural gas and electricity prices will be significantly lower than GB.

Region	Electricity comparison	Natural gas comparison
Great Britain	NI is 16% cheaper	NI is 23% cheaper
Republic of Ireland	NI is 25% cheaper	NI is 22% cheaper

4.2. This has not always been the case, for example, during 2009, NI domestic electricity prices were on average 13% higher than GB. However, regulatory scrutiny in NI has ensured consumers can be confident the price they pay reflects accurately the overall cost of supplying the energy. Hence the recent decreases in regulated tariffs in NI reflect the substantial and sustained falls in the wholesale gas and electricity markets over the last 18 months.

4.3. For example, in the case of gas, between February 2015 and February 2016, 'within day' wholesale gas prices reduced by around 40%. Following the most recent tariff decrease, consumers will have

experienced an overall reduction of 25% in their gas bills over the same period. As wholesale gas prices represent 39% of the whole tariff, and as the other costs are fixed, the final price reduction is broadly in line with the reduction in the wholesale price.

5. Transparency

5.1. The transparent nature of the NI price regulation model provides confidence and trust to consumers. The Cornwall Energy Phase 1 Report found 74% of NI electricity customers and 69% of NI gas customers trust their supplier. Contrast this with GB, where the energy market has no price regulation. Ofgem has found that in GB only 30% of customers trust their energy supplier.

5.2. Furthermore, in GB, concern is being expressed that prices are not reflecting the cost to supply and current wholesale price drops are not being reflected in customers' bills. In January 2016, Dermot Nolan, Chief Executive of Ofgem said of the GB market, "Energy companies are 'overcharging in many cases' with prices failing to fall in line with dropping wholesale costs"¹.

6. Competition

6.1. In the NI electricity market, price regulation of Power NI effectively creates a 'price to beat' for other suppliers. In recent years this has

¹ <http://www.bbc.co.uk/news/business-35321723>.

benefited domestic consumers with significant savings to be made by switching supplier and/or changing billing and payment method.

- 6.2. Competition in the NI domestic electricity market is developing gradually. Two new electricity suppliers² recently entered the market and new products, tariffs and offers extended choice for consumers with savings of over £100 per year available at one point to some domestic electricity consumers³. Currently, a Power NI customer with average consumption who receives paper bills and pays by a method other than direct debit can save over £142 a year by switching⁴.
- 6.3. During 2015, the Consumer Council continued its 'Switch & Save' campaign to raise consumers' awareness of the benefits of shopping around for all domestic fuels. We have so far carried out 41 public events within communities across NI.
- 6.4. As a result of all of these developments, domestic electricity switching rates showed an increase in 2015, after three years of decline. In 2014 the rate of switching in the NI electricity market was 5.7%, and in 2015 this had increased to 11.3%. By comparison, in 2015 GB had a switching rate in electricity of 12.2%.

² Click Energy and Open Electric.

³ Consumer Council, Electricity Comparison Table, 11 January 2016.

⁴ A Power NI standard rate customer consuming 3,800 kWh per year at a unit rate of 16.38p pays an annual bill of £622. By switching to SSE Airtricity's Home Electricity 24 tariff, receiving e-bills and paying by direct debit the customer will save £112 per year. The customer will also receive a £30 welcome bonus.

6.5. Currently in NI there are five electricity suppliers undercutting by up to 23% the price regulated and cost reflective incumbent tariff. The question that arises is whether this is a sustainable.

7. Consumer protection

7.1. While switching is increasing in NI, we recognise many electricity and even more gas consumers, have not yet engaged with the market. The experience of GB suggests there is a significant group of 'sticky customers' and these consumers are more likely to be vulnerable or on a low income. Price regulation protects these customers by ensuring the price they pay reflects the cost of supply, and they do not subsidise cheaper tariffs which are designed to attract more engaged consumers.

7.2. In this way price regulation in NI provides protection to consumers which is not enjoyed by their counterparts in GB. The value of this approach is demonstrated by the Competition and Markets Authority's (CMA) recent recommendation concerning the introduction of a temporary safeguard price control to protect customers on prepayment meters⁵.

7.3. Below we consider each of the seven options presented in the paper.

8. Option 1 – Identification of Significant Market Power and consequent licence conditions

⁵ CMA, *Energy Market Investigation: Summary of provision decision on Remedies* March 2016.

8.1. This option will provide limited protection to the customers of supply companies that are deemed to have Significant Market Power (SMP). The application of this option would present challenges to UR in a price deregulated market. These would be:

- Monitoring the market to identify SMP and consumer detriment;
- Switching on and off regulation for a company deemed to have SMP; and
- There is no protection for sticky customers of non-SMP suppliers.

8.2. It is an absolute prerequisite to the removal of the current price control system that no supplier has SMP. If in a deregulated market the existence of SMP emerges, it will be a clear sign competition is not working. However, we would agree if SMP is identified, prompt and robust intervention would be required.

9. Option 2 – “Inactive customer” price controls for Power NI, Firmus Energy and SSE Airtricity gas supply

9.1. The Consumer Council recognises this option would provide protection to some customers while also promoting competition. By requiring incumbent suppliers to set a tariff for inactive customers, subject to approval by UR, many disengaged customers and customers who have never switched would be protected from being charged high prices.

9.2. However, the ability of the option to protect the interests of consumers is limited by the view outlined in the options paper that any consumer

who has ever switched supplier is an active consumer. The option will not protect customers that have switched at some stage in the past but are now, for one reason or another, disengaged from the market.

- 9.3. While a customer who has switched in the past may be aware they can switch supplier, they may lack the information or confidence in the market needed to motivate them to switch. For example, they may be unaware of the amount of money they could save by switching. Secondly, as the consultation acknowledges, the option will not protect customers that move to a property supplied by an incumbent supplier. For example, an individual could move from a property supplied by a non-tariff regulated supplier to a property supplied by Power NI / SSE Airtricity / Firmus Energy and not be protected by the inactive customer price control.
- 9.4. Despite the option's shortcomings it would likely have a positive impact in terms of protecting many vulnerable customers. This is because vulnerable customers are more likely than others to be inactive in the energy market and the incumbent suppliers have the largest number of inactive customers⁶.

10. Option 3 – “Default” tariff

- 10.1. The Consumer Council believes the option of a default tariff provides a good balance between protecting the interests of consumers and

⁶ CMA survey evidence shows there is a somewhat higher proportion of those with some of the characteristics of vulnerable customers among the most disengaged and inactive domestic customers. CMA - *Energy market investigation Notice of possible remedies* July 2015.

promoting competition. The default tariff would act as a safety net for disengaged customers. It would also protect customers who reach the end of a fixed term tariff offer and do not switch to a cheaper tariff or supplier. It is appropriate that the terms of the tariff would ensure disengaged customers do not subsidise lower tariffs that are used to attract new customers.

10.2. The Options Paper explains it would be the responsibility of each supplier to set the price of its default tariff and UR would monitor the tariff rates. There is, however, a need for further information to explain what action UR would take if costs are considered unjustifiable.

10.3. The Options Paper explains consideration would need to be given regarding how the default tariffs are constructed. For example, the tariff could have a low standing charge with a high unit rate, or a high standing charge and a low unit rate. If this option is chosen for introduction following removal of the existing price controls, the protection of all vulnerable consumers should be prioritised when designing the tariff.

10.4. The Consumer Council believes it would be reasonable for UR to take an ex-post approach to assessing default tariffs. However, it would be essential for mechanisms to be established by which suppliers will discount customers' future bills if tariffs are found to have been set too high. This would be similar to the K factor aspect of the tariffs currently subject to price control.

10.5. The Consumer Council believes the default tariff option would provide a degree of protection to consumers disengaged from the energy market.

It also recognises setting the default tariff at the same price for all suppliers would provide benefits in terms of consistency for consumers. However, there is a danger uniform default tariff pricing could have the unintended effect of reinforcing consumer disengagement.

10.6. Permitting suppliers to price their own default tariff, subject to approval by UR, could protect disengaged consumers while encouraging consumer engagement, as prices would vary. If the default tariff option is to be considered further it would be helpful for UR to conduct a cost benefit analysis comparing the impacts of uniform and variable default pricing.

10.7. The Options Paper notes new entrant suppliers could possibly be exempted from being required to have a default tariff until they reached a predefined number of customers or percentage of the market. However, there is a risk an individual may switch from an established supplier to a new supplier and later be transferred onto a higher tariff. At the same time the new supplier may introduce a lower priced tariff to attract new customers. To avoid such a scenario occurring it would be preferable to require all new entrants to provide a default tariff from the outset.

11. Option 4 – Tariff cap spread

11.1. The Consumer Council understands the aim of the tariff cap spread model is to require all suppliers to price tariffs within a defined spread. This would ensure disengaged customers are not subject to non cost-

reflective charges and stop suppliers subsidising cheaper tariffs for engaged consumers.

- 11.2. The Consumer Council considers this a useful option for encouraging suppliers to seek innovative means of reducing costs, enabling them to offer cheap tariffs and attract new customers, while protecting disengaged customers from unfair high prices. It is important, however, that any cap on the spread between cheapest and most expensive tariffs protects vulnerable customers and households in fuel poverty.
- 11.3. The example presented in Table 5.4 of the Options Paper indicates a 29.6% tariff spread at a consumption level of 1,000kWh/yr, 2.5% at 2,500kWh/yr and 9.7% at 5,000kWh/yr. Permitting the largest spread at the lowest level of consumption will mean consumers on expensive tariffs who are unaware they can switch, but are trying to minimise their energy use, will lose out. This is because the higher price they are paying at their low level of consumption may be subsidising a lower tariff for an individual consuming a larger amount.
- 11.4. The Consumer Council acknowledges UR stipulating a percentage spread that is the same for all suppliers would provide clarity for consumers. However, permitting suppliers to determine their own range of spread, subject to approval by UR may be more conducive to development of the market. For example, enabling new entrants with a high proportion of engaged customers a larger spread than incumbents with a high proportion of sticky customers would facilitate the growth of competition in the market. This would be to the benefit of consumers.

12. Option 5 – Dominance thresholds

- 12.1. The Options Paper explains if dominance was found to be present in the energy market UR would have recourse to a number of options. These could be used to ensure the dominant supplier cannot abuse its position through pricing policies, frustrating entry, or lessening innovation opportunities. It is stated that the options include those outlined in the Options Paper, or a return to a conventional retail price control.
- 12.2. The paper explains if a dominant supplier has reached a position through fair means in an effective market, this suggests its prices and services are most attractive to consumers. It asserts that preventing the supplier from offering the same to a greater number of customers could result in detriment. However, this fails to recognise that in the absence of a price control a supplier could become dominant by offering low rates to new customers, subsidising these tariffs at the cost of disengaged and vulnerable customers.
- 12.3. The Consumer Council does not accept having switched supplier at one stage is an indicator of ongoing engagement in the energy market. An individual who has at one time switched may subsequently become disengaged. The absence of any regulatory measures could result in the growth of a supplier's market dominance at the expense of its disengaged and vulnerable customers.
- 12.4. Introducing a conventional price control, or an alternative measure once a supplier has become dominant, may prevent the exertion of market

power, and protect its disengaged and vulnerable consumers from that stage on. However, it will not rectify any harm the consumers have incurred up to that point. It would be preferable to retain some form of regulatory instrument to ensure if any company grows to a position where UR needs to consider recourse to Competition Act powers, the growth has occurred without harming disengaged consumers.

13. Option 6 – Gross margin cap

13.1. It is the Consumer Council's perception that while the gross margin cap option would provide protection for consumers, it appears in comparison to other options that it would result in significant additional work for UR. Furthermore, while consumers would benefit, it is unlikely they would understand the process due to its complexity. This may result in the potential adverse effect of sustaining disengagement from the energy market for sticky and vulnerable consumers.

14. Option 7 – Price-to-beat tariff

14.1. The Consumer Council notes the suggested price-to-beat tariff would comprise two elements: a standing charge to recover suppliers' fixed costs and a unit rate to cover volume based charges. To ensure protection of vulnerable consumers the charge to cover fixed costs should be levied in relation to the amount of energy used, rather than as a flat rate for all customers. Charging a flat rate would inhibit the ability of customers to keep bills low by minimising their energy use.

14.2. The Options Paper notes the price-to-beat tariff would be resource intensive for UR, and could be open to significant error if UR did not have sufficient expertise to continually appraise the price. It also suggests consumers may consider UR endorses the highest priced tariff in the market. The Consumer Council disagrees this view would be held by consumers. The current Power NI price control effectively sets a price for competing suppliers to beat. The Consumer Council's energy market monitoring indicates Power NI has consistently had the highest prices for domestic consumers in NI. The Consumer Council has not encountered evidence suggesting consumers regard UR as endorsing the highest priced tariff in the market.

14.3. It is suggested an independent third party could be assigned the role of setting the tariff rate to overcome the perceived difficulties mentioned above. The Consumer Council believes this is unnecessary, particularly because it will result in additional costs. Given UR has extensive experience in setting price controls, further information would be required to justify transferring responsibility for setting the price to beat tariff rate to a third party.

15. Additional issues

15.1. Question 7 asks *"are there any options not included in Cornwall's list?"* The Consumer Council notes UR is sufficiently concerned about ineffective competition for small I&C customers that it may adopt one of the options contained in the Options Paper. The Consumer Council

supports the CMA's initial proposal⁷ for the GB energy market that suppliers should publish price lists for micro-businesses on their websites, and make the information available to price comparison websites. This would promote transparency and benefit competition. The Consumer Council believes the publication of micro-business tariffs should be required in NI regardless of UR's chosen way forward.

15.2. Question 8 seeks feedback as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring. As discussed in response to Option 5, the Consumer Council believes there is significant risk to disengaged and vulnerable consumers inherent in the operation of the energy retail markets with no price controls. The Consumer Council therefore would not at this stage support a period of deregulation.

15.3. The current price controls provide protection to disengaged and vulnerable customers of the incumbent gas and electricity suppliers. However, under the current arrangements if the Retail Energy Market Monitoring project finds evidence of significant numbers of sticky customers associated with any of the non-incumbent suppliers, there may be a need to introduce additional protection. The Consumer Council would suggest some form of default tariff or tariff cap spread for non-incumbent suppliers may be required to protect their customers.

15.4. The seven options are quite complex, potentially resource intensive for both UR and the industry, and the impact on the market is difficult to

⁷ CMA - *Energy market investigation Notice of possible remedies* July 2015.

predict. An example of this is the four tariff rule in GB. This aimed to simplify the market for consumers. However, the CMA is currently proposing removing the rule on the grounds that it limits competition and innovation.

16. Conclusion

- 16.1. It is the Consumer Council's view that the 'hybrid' model of price regulation is currently acting in consumers' interests, and now is not the time to move away from it. However, it is important to anticipate and be prepared for changes in the market. The Cornwall paper is a welcome exercise in assessing the possible options available to UR if changes in the market require a change in regulation. In considering potential changes to the regulation of the NI energy markets UR must ensure consumers do not lose any of the protection provided by the current system of price regulation.
- 16.2. The seven options set out by UR offer an interesting insight as to actions it may consider if a deregulated market fails to benefit all consumers. This is the scenario the current CMA inquiry is tackling.
- 16.3. When it comes to making significant and possibly irreversible changes to the domestic energy market, UR must ensure its decisions are based on firm evidence and consumer feedback about other models, while addressing the unique features of the NI market.

16.4. If you require further information or you wish to discuss any aspect of this response please contact Richard Williams on 02890 251649 or richard.williams@consumercouncil.org.uk.



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Appendix IV
EAI Consultation Response



18th March 2016

Nicola Sweeney,
The Utility Regulator,
Queens House,
14 Queen Street,
Belfast,
BT1 6ED.

Via email

EAI response to Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase II

Dear Ms. Sweeney,

The Electricity Association of Ireland (EAI) reiterates its support of the Utility Regulator's (UR's) review as noted in our letter dated 28th January 2015 regarding the initial Cornwall report on the "Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market". In addition to providing commentary in respect of the questions raised we wish again to recall key points raised in our original letter.

Legality Context

We welcome the additional reference given to EU law in the current document (Paragraphs 1.8 to 1.10). Directive 2009/72/EU on the internal market in electricity is designed to facilitate a competitive internal market and, through this and a number of other measures, provide protection to consumers. Consumer protection measures are principally addressed under Article 3 and Annex 1 of the Directive. However no explicit provision is made for price regulation, contrary to the inference which might be drawn from the comment made in Paragraph 1.10 of the document. In respect of prices, the Directive (Art 3.3) provides that member states must ensure households and, where provided for, small enterprises "*enjoy universal service, that is the right to be supplied with electricity of a specified quality within their territory at reasonable, easily and clearly comparable, transparent and non-discriminatory prices.*" In respect of Paragraph 1.10, we would note that European Court of Justice rulings¹ permit regulation under very limited circumstances, including that such regulation must be time limited.

¹ For example Case C-265/08, *Federutility and others v Autorità per l'energia elettrica e il gas*.

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It is not unsurprising that the Directive makes no reference to regulated pricing, other than in respect of specific public service obligations on universal tariffs, given that price controls fundamentally undermine the basis of the current, energy only, market design. The effective operation of this market requires that prices reflect scarcity at all times, in the absence of which no new investment will arise.

We would also reiterate the comments of ACER on the position of regulated prices: *“Regulated end-user prices are not compatible with the objective of establishing liberal competitive retail markets. Therefore, CEER will develop guidance, based on experiences at national level, on the approaches to be used to facilitate the phasing out of regulated end-user prices, as soon as practicable, whilst ensuring that customers are properly protected where competition is not yet effective”*². We note that the UR recognises competition exists within the retail electricity market.

The EU Commission has consistently emphasised the need for all member states to remove wholesale and retail price regulation at the earliest opportunity. We wish again to highlight the Commission’s statement in its Communication on *“Making the internal energy market work”* (COM(2012) 663) which states that regulation of prices should cease. In particular, in section 3.2.1 it states that *“Member States should seek to cease regulating electricity and gas prices for all consumers, including households and SMEs, taking into account universal service obligation and effective protection of vulnerable customers. Suppliers should clearly spell out the different cost elements in the final cost for their customers, to encourage well-informed decision-making. The Commission will continue to insist on phase-out timetables for regulated prices being part of Member States’ structural reforms.”*

It is our understanding that the Commission will seek to make provision in this regard in its proposal later this year for a revision of Directive 2009/27/EU.

Justification

Imposing price regulation in pursuit of consumer protection must be justified as reasonable and evidence based. In this context we would question why reference is made exclusively to the GB market given its significantly different characteristics in terms of market size (a factor of approx. 25), regulatory framework and proportionately lower number of market participants. By comparison, the Republic of Ireland is more closely aligned in terms of market size (a factor of approx. 3), regulatory framework (the same wholesale market which constitutes some 60% of the customers’ bills), and an equivalent number of suppliers with 3 of the 7 being the same in both jurisdictions.

Price regulation ended in Ireland in 2011 without disruption of the market or negative impact on customers. On the contrary, vulnerable customers were provided with additional protection through the launch by electricity and gas suppliers of a voluntary industry code “Energy Engage Code” which committed to never disconnecting a customer that engaged with their supplier when facing financial hardship. Market engagement, as measured by customer switching rates, has been consistently higher than in Northern Ireland and no significant divergence in relative prices for domestic and small enterprises has arisen.

² ACER - Energy Regulation: A Bridge to 2025 Conclusions Paper (19 September 2014), and in particular, para 51

Response to the Questions raised

Question 1:

Insofar as all options directly or indirectly interfere with a Supplier's right to engage with customers and in the absence of evidence that prices are unfair or unreasonable then a balance is not struck between the respective right of suppliers and customers.

Question 2:

The question conflates two separate objectives. The Directive specifies that prices must be reasonable (in the context of the underlying cost structure) and that customers be protected through effective competition and measures identified in Annex 1 of the Directive (transparency, appropriate contract conditions, price comparators etc.). In that all options aim to regulate prices then competition is not promoted nor, as a consequence, protection provided to customers in the long term. Further, price regulation must be justified and temporary if applied to achieve an overarching economic good to comply with European law. It is not clear that evidence exists to support such a justification under any of the listed option.

Question 3:

Given a universal service obligation is in place, measures aimed at regulating prices will affect both general and vulnerable customers equally.

Question 4:

Dominance and market power obligations are deliberately discriminatory in respect of the Suppliers to which they might apply and are best addressed through active competition. The remaining options limit innovation and add system and/or administrative costs which ultimately will be borne by customers.

Question 5:

It is not possible to address this question without significantly more detail regarding implementation costs and the impact of reduced competition.

Question 6:

As noted above, continuation of price regulation is contrary to the intent of EU legislation and the effective functioning of the energy only market. It is possible that legislation revising the Directive later this year will give further weight to this objective. The experience of price deregulation in Ireland, where market conditions are much more comparable than Great Britain, is positive and should be given consideration in considering progress on this issue.

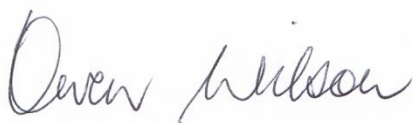
Question 7:

EAI would strongly support a proposal for a period during which the energy retail markets are allowed to operate with no price controls. Retail market monitoring measures currently in the process of being implemented would be sufficient to actively monitor the market response.

Conclusion

The evolution of the electricity market is an important strategic issue for Northern Ireland. EAI believes that effective competition will deliver optimal results for customers. While welcoming the review of the market the UR is undertaking; policy decisions and implementing actions should reflect evolving practice across Europe and European law.

Yours sincerely,



Owen Wilson
Chief Executive,
Electricity Association of Ireland.

Appendix V
Electric Ireland Consultation
Response

Electric Ireland Responses -

Consultation on phase II of the review of effectiveness of competition in NI energy markets

Q1. Whether each option strikes a fair balance between the rights of customers and the rights of any supplier which would be subject to that option?

Answer 1. Yes. It is fair to say that the rights of customers and the rights of potentially impacted suppliers have been rigorously evaluated in both the UR and Cornwall papers.

Q2. *Whether each option strikes an appropriate balance between the protection of customers and the promotion of competition?*

Answer 2. Proposed options / changes to enlarge the scope of regulatory application to all suppliers in all but one of the proposals seem inappropriate to Electric Ireland given the current status of the NI market. The central challenge currently facing the electricity market is to create a level playing field for all suppliers through establishing market conditions for greater competition and choice for domestic / small business customer by reducing the dominance of the incumbent ; and to do so over a defined period to deliver the greatest potential benefits to customers.

It is important to note here the unique nature of the domestic market in NI whereby in excess of 70 % of credit meter customers remain with the incumbent while competition is most active in the keypad segment where the incumbent currently retains a much lower 55% of market share. This highlights the requirement to target changes in the market around the credit meter segment in particular. In this respect Electric Ireland would favour an approach which seeks to significantly reduce the incumbent market share of the credit meter segment. In the context of the options presented, this could be best achieved through the implementation of the Inactive Customers price Control. Electric Ireland does believe that any of the other options presented provide a more optimal basis for enhanced customer benefit.

Q3. *Whether each option is likely to protect vulnerable customers (including, in particular, persons who are chronically sick or disabled, of pensionable age, on low incomes or residing in rural areas)?*

Answer 3. Electric Ireland believes that greater customer benefit through added choice and value is likely, in the first instance, to be delivered through a reduction in the dominant market share of the incumbent, particularly, as we have said, in a reduction of the market share currently held in the credit meter segment. Robust arrangements for the protection of vulnerable customers are already well embedded in the market arrangements and we do not believe that any of the options would dis-improve this situation but it would be reasonable to expect that additional benefit would accrue to vulnerable customers as a result of better pricing outcomes in a more competitive credit meter market.

Q4. What are the burdens that are likely to be placed on suppliers made subject to each option ?

Answer 4. Insofar as all options except one (Inactive customer option) will impose some new requirements on all suppliers in addition to those already in place, new regulatory conditions would place additional burdens on those suppliers in the form of expanded costs related to process design, operation and monitoring ; system change; training, service delivery; product development etc. which are difficult to determine precisely at this time. An unintended consequence might also include a constraint on innovation in the market for all suppliers due to the increase level of regulatory intervention.

Q5. Are those burdens disproportionate to the benefit secured and, if so, is there a less intrusive or onerous measure could be implemented by the UR?

Answer 5. Electric Ireland believes that Option 2, Inactive Customers proposal is the most appropriate next step in the development of the market in Northern Ireland at tis time. Specifically we are proposing that such an option focussed on the domestic credit meter customer segment would deliver the least disruption to current market arrangements with clear customer benefits in the form of improved and fairer pricing outcomes for a greater range of customers.

Q6. Do consultees have any other comments on the options put forward?

Answer 6. Electric Ireland welcomes the publication of this review and options as part of the process started with the publication of the Phase 1 review. In particular we welcome the participative approach which has been adopted by the Regulator , allowing all interested parties to contribute to what is a critical debate about the effectiveness of competition in the Northern Ireland Energy Retail Market. We fully acknowledge that careful, expert and detailed deliberation is required in coming to conclusions in this process and the Regulator has provided an excellent market challenge and focus in these deliberations through the involvement of Cornwallenergy and the associated options and analyses that they have presented.

Notwithstanding this the Regulator has also provided for other market participants to provide alternative options and we believe and have argued that at least one such alternative option should be considered.

Q7. Are there are any other options not included in Cornwall's list?

Answer 7. Electric Ireland's continued preference is to see a deregulated market framework introduced which would set specific criteria (including, particularly, interim and final market share thresholds) for achievement of full deregulation of incumbents within a short , defined timeline of not more than 2 /3 years. We believe this approach will deliver the basis for an optimum enduring outcome for customers in the NI energy market.

Q8. Feed back is sought as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring. This consultation seeks views on whether there should be a period of deregulation or an immediate move to any of the options presented.

Answer 8. Electric Ireland would support the introduction of a period during which the retail markets are allowed to operate with no price controls subject to enhanced monitoring but, critically, also subject to a defined trial period during which target market share expectations (including for credit and keypad meters and overall) for dominant incumbents were set as outcomes of the trial.

Appendix VI

Energia Consultation Response



**Response by Energia to Utility Regulator,
Consultation**

***Review of the Effectiveness of Competition in the
Northern Ireland Energy Retail Market – Phase II
Regulatory Implications***

18th March 2016

1. Introduction

Energia welcomes the opportunity to respond to the Utility Regulator's consultation on the Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market- Phase II. Energia is very supportive of customer protection and competition and through our operations North and South, we have consistently engendered switching by providing competitive offers to customers and maintaining the highest standards in customer service.

This consultation and the questions contained within are framed by the Cornwall report and the CMA findings. What is notable about both these publications is how one pertains to a substantially different market (GB) and the other from the outset acknowledges how different NI is from other markets. In this context the applicability of the CMA findings is questionable. In relation to the timing of the consultation, the consultation is perhaps premature in proposing remedies to an issue that hasn't taken shape yet.

This response makes some general comments before finally concluding.

2. Regulatory Intervention

Regulatory efforts to address perceived shortcomings in a market can have unintended consequences. For example, excessive regulatory intervention may cause concern among investors and prospective market entrants about how stable the policy environment is. This can in turn result in increased costs for consumers¹ by increasing the cost of capital or by stifling innovation and limiting competition in the sector. Any regulatory intervention into a market needs to be cognisant of the negative impacts that interventions can have. This is particularly true in this instance where remedies are being proposed for a problem that hasn't taken shape yet.

Since 2009 there have been 9 regulatory or political interventions in the energy sector in GB². These interventions have continued over this period and culminated in a substantial investigation by the CMA into the sector. While difficult to fully assess the impact of these interventions, it could be inferred that each new intervention or review is an acknowledgment that some or all of the previous efforts were ineffective or perhaps detrimental. In some cases subsequent reports have acknowledged the shortcomings of previous interventions (e.g. removal of ofgem's four tariff rule). Furthermore, solutions as suggested here may be at odds with the European Commission, which has consistently emphasised the need for price deregulation at the earliest opportunity.

3. Cornwall Report

The UR's consultation mentions that the CMA findings will be examined in conjunction with this consultation. However, given the unique nature of the NI market and the fact that the CMA investigation has only focused on the GB market, applying the CMA findings may not be appropriate or beneficial. Furthermore, the CMA

¹ <http://www.publications.parliament.uk/pa/cm201516/cmselect/cmenergy/542/542.pdf>

² <http://researchbriefings.files.parliament.uk/documents/CBP-7243/CBP-7243.pdf>

investigation examined existing perceived market failures. In contrast this consultation and the accompanying report by Cornwall would seem to be premature as it is proposing remedies to problems that do not or may not ever exist. Designing remedies before any problems have been identified or have even begun to surface would seem counterintuitive and may lead to remedies that do not suit the problem.

Some of the tariff controls put forward by the Cornwall report are likely to be punitive to engaged customers by limiting the products that suppliers are able to offer. If suppliers are unable to offer competitive products it may result in previously engaged customers stepping back from the market. Disengaged customers coupled with heavily regulated tariffs will not encourage new entrants or customer switching rates and may result in a market devoid of innovation and competition.

While there is a balance to be struck between reactionary interventions and trying to ensure the market is functioning, designing remedies before any problems have been identified or even begun to surface is counterproductive. As is acknowledge in the Cornwall report, competition has largely worked in the NI context. Based on this observation, efforts here should perhaps be focused on expanding on this success by encouraging further competition and customer engagement rather than introducing complex tariff rules that have been largely discounted elsewhere. There is a responsibility here to be proportionate in protecting consumers and promoting competition in the market.

Conclusion

As the proposals are designed to address a scenario that has not yet arisen, it is difficult to fully assess their impact. However, it is likely that some of the interventions as described by Cornwall would be punitive to engaged customers and lead to a decrease in competition and switching, further limiting the attractiveness of the market to existing and new entrants in the process.

As is outlined in the Cornwall report, competition has largely worked in the NI context. Efforts here should be therefore focused on further encouraging competition and customer engagement in the sector and not on applying restrictive tariffs or implementing findings from an investigation into a substantially different market. If after full deregulation, issues of significant market power do arise then it may be necessary to revisit the topic in an NI context.

Appendix VII
firmus Consultation Response

Nicola Sweeney
Utility Regulator
Queen Street
Belfast
BT1 6ED

firmus energy Ltd
A4-A5 Fergusons Way
14 Kilbegs Road
Antrim
BT41 4LZ

16th March 2016

Dear Nicola,

RE: Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase II. Regulatory Implications and Options for Consultation

Thank you for providing firmus energy with the opportunity to respond to the second phase of the Northern Ireland retail market, competition effectiveness review.

Firmus energy has taken this opportunity to respond to Cornwall Energy's seven identified potential regulatory options that could be introduced, in isolation or combination, to the Northern Ireland (NI) gas and electricity retail markets if and when the current retail price controls are no longer required.

We have provided high level comments on the options presented, but it is evident that the likely advantages and disadvantages of these options will depend on the prevailing circumstances, and the particular ways in which they might be implemented. Furthermore the relevance of each option would have to be considered within the context of it pertaining to gas or electricity and the Licensed Area in question, i.e. Greater Belfast, the Ten Towns or Northern Ireland as a whole.

Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market PHASE 1

The Utility Regulator published a report in November 2015, which, for the first time, provided an independent assessment of the effectiveness of competition in retail energy markets in Northern Ireland.

Overall, Cornwall Energy concluded that:

- Competition in the NI energy retail markets is becoming established and delivers benefits to consumers that have switched.
- Price regulation for smaller business and households has ensured reasonable and stable prices for the benefit of those consumers that have chosen not to switch.
- Vigilance is required to avoid the risk that a small number of suppliers may use their market dominance to set prices that adversely affect consumers; and Cornwall expect to see continuing price regulation for some time to come.
- The NI experience strongly suggests that regulation and competition can usefully co-exist. This "hybrid" approach to the energy markets provide the dual benefits of competitive offering

and regulated prices to ensure excessive profits are avoided, and there is transparency with regards pricing for regulators, government and customers.

- There are a number of measures that could or should be considered to improve the functioning of the energy markets in NI – including improving aspects of the competitive process, improving customer access to information or improving predictability of costs.

The Cornwall report did not focus on the Ten Towns Licensed Area as domestic market opening was not coming into effect until April 2015. Since the report's publication the market has now opened and, nearly one year on, firmus energy has not seen any other supplier enter the domestic sector. This raises questions in terms of why the current market conditions are frustrating competition in this sector, and indeed, whether regulation and competition can co-exist in a hybrid state.

It is our opinion that, at present, a number of factors are frustrating competition in the Ten Towns domestic sector, including:

- Current UR regulated retail margin of 1.5%
- Small size of gas market in the Ten Towns Licensed Area.
- Envisaged market share for new entrants.
- High fixed costs for suppliers entering domestic market.
- Unfavourable acquisition costs relative to market share possibilities.
- Impact of fixed/variable costs on gross margin.

OPTIONS

Option 1 – identification of Significant Market Power (SMP) and consequent licence conditions;

In considering all options, firmus energy Supply Ltd would, from a high level view, have preference for less interventionist approaches to be used where possible. These options will exhibit the benefits that increased flexibility and commercial responsiveness can provide for. Nevertheless, as discussed previously, the advantages and disadvantages of such an approach will depend on the competitive context and on the specific way in which the option it is implemented.

Option 2 – an “inactive customer” tariff for former incumbent supplier’s disengaged customers;

Option 3 – introducing a “default tariff” for those consumers unwilling or unable to engage with the market;

Option 4 – a cap on price differentials between the cheapest and most expensive tariffs to limit the rates disengaged customer face compared to proficient and active consumers;

Options 2, 3 and 4 all provide different potential options for addressing the concern that some portion of customers are insufficiently protected by the competitive process, and thus that some form of (more or less) targeted protection should be provided for those customers.

Firmus energy Supply Ltd considers the key contextual point to note for these options - in terms of the Ten Towns Licensed Area - is the lack of the development of any competing offers for domestic supply as yet. As discussed previously, a process has not emerged where a competitor has found it sufficiently advantageous to offer better terms to those that firmus energy Supply Ltd has to offer as a result of

the current regulatory regime. Firmus energy Supply Ltd would highlight that there should be further analysis into the reasons for this, especially in relation to the current retail margins allowed by UR.

In addition, the consideration that a subset of consumers are in some way inactive and insufficiently protected by competition is premature. The lack of any competing offers strongly suggests that the existing regulation of margins have been such as to frustrate the emergence of competition even in relation to those customers most likely to be interested in switching.

Option 5 – mechanisms for determining where a supplier or suppliers are deemed sufficiently dominant to be able to exert market power and possible regulatory solutions;

Similarly to option 1, option 5 involves the use of a threshold question that is concerned with when relevant regulatory powers should be switched on.

Option 5 contemplates a number of metrics that might be used to determine whether regulatory powers should be triggered. Firmus energy Supply Ltd's principal concern with such an approach is that it can result in the mechanistic application of a test that does not adequately capture the relevant market context. In view of this, firmus energy Supply Ltd would favour a more principle based approach that requires assessment of the particular market context, over the 'hard wiring' of such metrics.

Option 6 – a gross margin cap where suppliers would only be permitted to put rates into the market with a maximum level of gross margin;

Firmus energy Supply Ltd again considers the key contextual point to note for this option - in terms of the Ten Towns Licensed Area - is the lack of the development of any competing offers for domestic supply. As discussed previously, a process has not emerged where a competitor has found it sufficiently advantageous to offer better terms to those that firmus energy has to offer as a result of the current regulatory regime. This suggests, as previously discussed, that gross margin available for competitive suppliers may be limited as a result of the net retail margin of 1.5% imposed of firmus energy.

Given the gross margin takes into account operational expenditure, then it may be the case that the fixed market entry and start-up costs may also be frustrating competition. This again raises the question of whether retail margin should be increased to encourage market entry.

Option 7 – Price-to-beat tariff

The Cornwall report stated that the determination of a tariff rate that all suppliers would have to match or better, would lead to consumer confusion and extensive levels of monitoring and analysis. Similarly to Option 5, firmus energy also considers that this approach may not adequately capture the relevant market context, and questions its relevance within the Ten Towns Licensed Area given the current lack of competition.

Conclusion

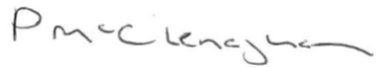
Firmus energy Supply Ltd continues to provide consumers in the Ten Towns and Greater Belfast Licensed Areas with gas at the most competitive prices. Northern Ireland gas prices continue to be among the lowest in Europe and this accolade continues to be a long term objective for the industry as a whole.

UR has an opportunity to work with suppliers and invoke a regulatory regime that continues to bring the best energy costs to Northern Irish consumers. This can only be achieved through constructive engagement and comprehensive consideration of the operational needs of each individual supplier in the Northern Ireland gas and electricity markets.

Firmus energy is proud of its role in developing the Northern Ireland natural gas market over the last ten years and it is imperative that any new supplier entering the gas market exhibits and maintains the same high levels of customer service and corporate responsibility (e.g promoting energy efficiency). Anything less would undoubtedly be to the detriment of the entire natural gas industry and subsequently Northern Ireland consumers.

We hope that these comments prove useful and look forward to future discussions on this topic.

Yours sincerely,

A handwritten signature in black ink that reads "P McClenaghan". The signature is written in a cursive, slightly slanted style.

Peter McClenaghan
Regulatory Affairs Manager
Firmus energy

Appendix VIII

Flogas Consultation Response

Flogas Natural Gas Response To Utility Regulator Consultation entitled

Review of Effectiveness of Competition in the Northern Ireland Energy Retail Market-Phase 11 Regulatory Implications dated December 2015

QUESTION 1 to 6 (Combined Response)

General

While we have not taken legal advice on the issue our understanding is that the Directive 2009/72/EU on the Internal Market is designed to facilitate consumer protection primarily through the operation of a competitive market. The Directive makes no reference to regulated pricing, other than in respect of specific public service obligations and the protection of vulnerable customers. The suggestions relating to price regulation put forward by the Utility Regulator appear to be contrary to the intentions of the Commission in relation to achieving liberal competitive retail markets. Progress has been made in Northern Ireland in moving towards competitive retail energy markets and this has brought benefits to both Domestic and Business customers. We believe that the Utility Regulator should look to facilitate this progression further. The results of increased competition in Northern Ireland have to date been universally positive. Heavy handed price regulation runs the risk of damaging the market, setting back the competitive market and damaging the longer term interests of energy consumers.

Significant Market Power

Domestic Market

In the circumstances where a particular supplier is dominant in the market or meets the criteria for being deemed to have Significant Market Power it seems reasonable that additional licence obligations would become effective. We do not believe that re-introducing some form of price regulation (along the lines which are currently in place) would be an appropriate response as this would distort competition and potentially discourage switching.

Assists vulnerable customers

Business Market

Similarly in the circumstances where a particular supplier is dominant in the market or meets the criteria for being deemed to have Significant Market Power it seems reasonable that additional licence obligations would become effective. We do not believe that re-introducing some form of price regulation (along the lines which are currently in place) would be an appropriate response as this would distort competition and potentially discourage switching.

Inactive Customer Tariff (for previous incumbents)

Domestic Market

The fact the different Domestic Customers of a particular Supplier may be paying different rates should not be seen in itself as a problem or evidence that the market is not working. Actually to a large extent its evidence that the market is working. Customers who shop around or switch can get better prices. Some customers are not interested in switching for a variety of reasons including:

- They feel more secure with their current provider
- The current supplier provides additional services eg Boiler maintenance
- They like the customer service they receive from their current supplier
- A 10% saving on a dual fuel bundle could be around £100 pa. Some customers do not see this as worth the effort of switching (though switching is easy)
- Some Suppliers have softer credit policies which suits some customers
- Not all suppliers offer the same product eg Two Year Fixed etc

It is therefore wrong to assume that these customers are not getting a fair deal. In most cases they have considered switching but decided not to. Their interests are being protected because they have the option to switch.

As noted by the UR and with reference to the CMA report in Britain there can be a tendency for the previous incumbent suppliers to have a base of 'sticky' customers who do not consider switching and for these suppliers to try and squeeze out new suppliers by pricing new customers at cost or below cost. In this situation existing disengaged customers are effectively subsidising new customers. It may well be the case that the incumbent supplier is only earning a normal level of return from the Market but, depending on how you view the matter new customers are paying too little and existing disengaged customers are paying too much.

We do not believe that re-introducing some form of price regulation (along the lines which are currently in place) for dis-engaged customers would be an appropriate response as this would distort competition and potentially discourage switching. The issue could be addressed through a combination of a 'Price Banding methodology' combined with a prohibition on below cost selling.

Assists vulnerable customers

Business Market

The fact the different Business Customers of a particular Supplier may be paying different rates should not be seen in itself as a problem or evidence that the market is not working. To a large extent its evidence that the market is working. Customers who shop around or switch can get better prices. Some customers are not interested in switching for a variety of reasons including:

- They feel more secure with their current provider
- The current supplier provides additional services eg Energy Efficiency Services
- They like the customer service they receive from their current supplier
- Their energy cost may be a very small part of their overall business costs
- Some Suppliers have softer credit policies which suits some customers
- Not all suppliers offer the same product eg Fixed or Variable pricing
- Some Suppliers may offer bundles eg Electricity and Natural Gas, Oil and electricity

It is therefore wrong to assume that these customers are not getting a fair deal. In most cases they have considered switching but decided not to. Their interests are being protected because they have the option to switch. We do not see the concept of a 'dis-engaged customer' as holding validity in the B2B market.

Within the IC1 and IC2 Business sectors there are a wide range of different types of customers. There are single premise sole traders, multiple business outlets, and mixed customers. A lot of customers have their own particular preferences re Energy Products, Tariff types and Billing requirements. For Suppliers to meet these customer requirements flexibility and innovation is required.

We believe that re-introducing some form of price regulation (along the lines which are currently in place) would distort competition and potentially discourage switching. There are more suppliers in the B2B market than the B2C market with a significant increase in switching over the last eighteen months. There are now seven supply companies operating in the B2B electricity sector and six suppliers operating in the natural gas B2B sector. The incumbent market shares have reduced considerably. Business customers are generally focused on input costs and have a high awareness of energy costs. All businesses use electricity and hence can be easily targeted by competitors. We have recommended that a full listing of Business Gas Points be made available to suppliers.

Default Tariff (Applying to all suppliers)

The UR appears to be considering two options:

- A Default tariff set by each supplier
- An Industry Default tariff set by the UR

Domestic Market

Our understanding is that Suppliers do currently set their own Default Tariff, frequently called their Standard Variable Rate. Hence this option is effectively already in place. This tariff would reflect all cost inputs and in particular the Suppliers Hedging Position. Suppliers put commodity hedges in place for a variety of reasons including

- Facilitated structured planning
- Provides customers with price certainty
- Avoids need for frequent tariff changes
- Evens out commodity price spikes

The General Hedging Policy becomes more complicated when you factor in the need to provide specific back-to-back hedges against specific contracted customer agreements eg two year fixed price. No two suppliers will have common hedging positions. The concept of an Industry wide Default Tariff is unworkable. Suppliers have different cost structures and different attitudes to risk. Most importantly suppliers have different Hedging Positions.

It is reasonable for the UR to review Default Tariffs under the REMM process. It would not be acceptable for any details to be published as this is sensitive market data, and publication could be detrimental to the interests of the supplier and damage competition.

Assists vulnerable customers

Business Market

We believe that it is more appropriate in the B2B market to allow Suppliers to decide whether they wish to offer a Default tariff or not. We expect that most Suppliers will offer a Default tariff.

Suppliers put commodity hedges in place for a variety of reasons including

- Facilitated structured planning
- Provides customers with price certainty
- Avoids need for frequent tariff changes
- Evens out commodity price spikes

The General Hedging Policy becomes more complicated when you factor in the need to provide specific back-to-back hedges against specific contracted customer agreements eg two year fixed price. No two suppliers will have common hedging positions. The concept of an Industry wide Default Tariff is unworkable. Suppliers have different business strategies, cost structures and different attitudes to risk. Most importantly suppliers have different Hedging Positions.

Suppliers need to be afforded the opportunity to be innovative in developing Products and Tariffs in the B2B sector. Many customers have different preferences and efforts at limiting or inhibiting these would not be positive for the market.

It is reasonable for the UR to review All Business Tariffs under the REMM process. It would not be acceptable for any details to be published as this is sensitive market data, and publication could be detrimental to the interests of the supplier and damage competition.

Tariff Cap Spread

Domestic and Business

We see that this could be of some use as regarding dealing with the dis-engaged customers of Incumbent suppliers or suppliers with significant market power. Otherwise we believe that the imposition of this approach could hinder fair competition and switching.

Dominance Thresholds

Domestic and Business

We believe that it would be appropriate for the UR to set Dominance Thresholds. While it is unlikely that these would be met it does provide a safety net. Full Re-Regulation of the Dominant party's prices should be a last resort. A Tariff Cap Spread would be a preferred alternative.

Gross Margin Cap

Domestic and Business

We are not in favour of the Regulator setting general Industry wide Gross Margin Caps for the following reasons:

- Its highly intrusive
- It potentially restricts competition
- Different suppliers have different business strategies
- Different suppliers have different attitudes to risk
- It potentially restricts innovation

- It fails to allow for different hedging strategies
- It's complicated

Price to Beat Tariff

Domestic and Business

This Option constitutes a maximum price set by the Regulator which applies to all Suppliers.

This would clearly be seen by the public as applying price regulation to all suppliers. It would seem counter intuitive to the whole concept of opening the market up to Competition and the UR would be seen as the 'Price Setter'. The process appears very complicated and time consuming and potentially open to error. It does not seem to recognise that different suppliers have different hedging strategies.

Appendix IX
FSB Consultation Response

Ms Nicola Sweeney

The Utility Regulator
Queens House
14 Queen Street
Belfast
BT1 6ED

17th March 2016

Dear Ms Sweeney,

FSB response to the Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase II

The Federation of Small Businesses (FSB) welcomes the Utility Regulator's review of competition within the energy market.

FSB is Northern Ireland's largest business organisation with approximately 6,500 members, from across all sectors of industry, and over 200,000 members throughout the UK. As experts in business we offer our members a wide range of vital business services, including legal advice, financial expertise, support and a powerful voice in government. The aim of FSB is to help smaller businesses achieve their ambitions.

FSB Northern Ireland would firstly like to thank the regulator for placing small I&C firms at the heart of this review. Much of the political and media spotlight on energy prices tends to fall mainly on the domestic sector and FSB is concerned that the views of businesses may be under-represented.

Northern Ireland is a small business economy, and micro and small businesses form the bedrock. Northern Ireland has the highest concentration of SMEs of all the nations and regions in the UK – here, 98% of all firms employ fewer than 20 people, while 95% employ fewer than 10. Northern Ireland SMEs provide 75% of all private sector jobs. Clearly, small businesses are the core of the local economy and have a vital role in contributing to employment opportunities.

Research conducted by the Ulster University Business School for FSB in 2015 asked small businesses to identify their main barriers and obstacles to doing business in Northern Ireland. One of the highest responses was

the cost of energy, where 34.5% of businesses identified it as a major barrier to economy growth.

Businesses highlight difficulties in comparing contracts, unclear terms and conditions, automatic rollovers, and a lack of confidence in the industry as major factors in identifying the best energy deal.

Protection for Small Businesses

As has been conceded by the regulator, it has become increasingly apparent that smaller businesses share many of the same characteristics as domestic consumers. FSB Northern Ireland's preferred option would be for our members to have the same level of protection as is currently afforded to domestic customers.

The most common issues raised by small businesses in relation to energy include:

- Complex bill formats
- Infrequent meter readings
- Incorrect billing
- Poor customer service
- Lack of information on switching suppliers
- Lack of transparency in contract terms and conditions
- Direct selling methods

These issues must be addressed to build small business' confidence in those who operate Northern Ireland's energy supply.

Competition

Competition is not as strong as it could be. The large majority (93%) of business customers in Northern Ireland have a sub-70kVA connection to the grid. Although there are now seven suppliers active in this section of the market, they have not eroded Power NI's dominance. Power NI still controls 54% of this market, while Energia controls another 10%, giving the Viridian Group nearly two thirds of the entire Northern Ireland small I&C market.

Go Power entered the market in 2012 and has made spectacular inroads into the large customer segment, but it has just 11% of the smaller (<70kVA) business market, compared to 23% of the larger (>70kVA) energy market.

The decisions taken by the regulator should try to find the best way to increase competition in the energy market for the smaller energy users. FSB urges the Utility Regulator, when evaluating the seven options, to consider how to best protect small business consumers.

Small business disadvantages

As it stands, small businesses are disadvantaged compared to large businesses and domestic consumers when taking out a contract with a new energy provider. Most small businesses have a similar level of

expertise as a domestic customer when purchasing products and services, and they are much less likely than large businesses to have staff with a specific procurement role. Additionally most small businesses will often be very focused on running their core business effectively. The perceived cost of spending a lot of time searching for a new energy supplier may, therefore, be high, and small businesses often do not think they will benefit significantly by doing so. Finally, smaller businesses have far less bargaining power, especially compared to large companies, and may struggle to access favourable energy rates.

This results in a lot of small business 'sticky' customers. FSB would support measures that will tighten rules on auto-rollover of tariffs, to reduce the risk of exploitation of the smallest businesses by suppliers. Additionally FSB would support measures that would grant greater protection to those business customers who are on 'default' tariffs, with a view to preventing exploitation, as well as providing greater information and prompts about better offers available throughout the energy market.

FSB believes the 2003 Communications Act which regulates the telecoms industry is a model of best practice that could be replicated across all regulated industries. Under this law, the regulator treats the smallest businesses like domestic consumers other than where there are clear reasons not to. This would give a much fairer level of consumer protection to these firms.

FSB also believes that smart meters will present a major opportunity to provide additional information to customers. A successful roll-out will help small businesses to understand and manage their energy, and provide new opportunities for accessing and interpreting information.

Yours faithfully,



Wilfred Mitchell OBE
Northern Ireland Policy Chairman

Appendix X
PNGL Consultation Response



Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market

Phase II Regulatory Implications

December 2015

Phoenix Natural Gas Ltd. ("**PNGL**") is the largest natural gas distribution business in Northern Ireland, being the owner and operator of the Licence for the distribution of natural gas in the Greater Belfast Area and Larne.

PNGL welcomes the opportunity to respond to the options presented by the Utility Regulator ("**UR**") for consultation following its review of the effectiveness of competition in the Northern Ireland energy retail market ("**the Consultation**").

PNGL notes the seven options for the Northern Ireland market which could be employed in the event that the current regime of price controlling the domestic and small I&C retail markets of the former supply incumbents is changed.

As a Network Operator, PNGL is not best placed to comment on whether each option strikes an appropriate balance between the protection of consumers and the promotion of competition or on the rights of a supplier and the rights of consumers. However PNGL welcomes the clarity that developing a clear way forward for the regulatory regime will bring.

PNGL would also comment that UR's preferred option must continue to support the growth of the gas distribution networks, encourage the maximum number of connections to the system and be cognisant of the operating policies of Network Operators e.g. the need for a commissioning supplier. Any such issues should be addressed when the preferred option is identified to ensure that industry is well prepared should the change in regulatory framework need to be made.

Appendix XI
NEA Consultation Response



Action for Warm Homes

**National Energy Action's Northern Ireland
response to the Northern Ireland Authority
for Utility Regulation Review of
Effectiveness of Competition Phase II**

March 2016

National Energy Action Northern Ireland (NEA NI), the leading national fuel poverty charity, works to ensure energy is affordable for disadvantaged energy consumers. As such we welcome the opportunity to respond to this consultation from the Northern Ireland Authority for Utility Regulation (NIAUR).

The latest House Condition Survey showed that in 2011, 42 per cent of all households in Northern Ireland were in fuel poverty. This is one of the highest rates in Northern Europe and is significantly higher than England, Scotland and Wales. While the recent fall in the price of oil is very welcome we still find families struggling to fill the tank and although predications indicate that oil will continue to fall in 2016 it is still imperative that we do all we can to mitigate other upward pressures on bills.

On average, the proportion of household income which is required to be spent on domestic fuel in NI is higher than anywhere else in the UK. Consequently, progress to eradicate fuel poverty has been very badly affected, despite relative parity in relation to access to the UK social security system. This situation has been highlighted in the UK Fuel Poverty Monitor (UKFPM) for many years. In particular, rising fuel prices and stagnating or decreased incomes have been exacerbated by Northern Ireland's energy inefficient housing stock which continues to impair the physical and psychological health of thousands of people, leaving an estimated 42% of all households in Northern Ireland in fuel poverty

Northern Ireland also has the largest percentage of domestic homes using home heating oil in Western Europe, 68% of all households are reliant on oil. With such high dependency on heating oil, the price of home heating oil remains a serious issue for many fuel poor households despite recent falls in wholesale costs. During December 2010 heating oil prices were on average 30 per cent higher than in December 2009. While the recent dramatic decrease in the price of oil is now having a positive impact for many

households in Northern Ireland, this is not set to be the long term trajectory and much of the saving is subsequently wasted through poor quality housing. In addition, whilst some customers have the financial ability and large enough home heating oil tanks to store the full amount needed for winter and to beat higher winter prices; the majority of homeowners do not have this option and often have to refill their tanks several times during the winter period and are therefore more affected by winter price spikes or fail to benefit from the economies of scale brought about by larger fills of oil.

This has been mitigated somewhat in recent years by the emergence of oil stamps and oil buying clubs which while first established by local communities have now been rolled out with support from some local councils, the Public Health Agency and the Northern Ireland Housing Executive with Bryson Energy. However, coverage of these types of voluntary initiatives is still not universal and many households still struggle with the upfront price of oil. **We therefore call on the NIAUR to use their authority to highlight the need for regulation with oil ensuring that the 68% of households dependent on oil can avail of the same protections afforded to those with natural gas.**

While this particular consultation relates to competition in the retail market to drive down costs for households, we also feel it pertinent to highlight the fact that improving energy efficiency, for example through insulation and heating standards, is the most rational and sustainable means of ensuring affordable warmth. Poor housing standards are responsible for the impaired physical and psychological health of millions of UK households. The links between low indoor temperature and poor health have been well understood for many years. Cold homes increase the likelihood, repetition and the severity of respiratory and cardiovascular illnesses. The links between dampness and mould growth on asthma and allergies are also well known and understood. There is also some evidence that a cold home impacts on poor mental health, low self-esteem, educational performance and social

isolation. **We therefore call on the NIAUR to play its role in protecting vulnerable consumers by supporting the targeting of energy efficiency schemes to the vulnerable.** With responsibility for the Northern Ireland Sustainable Energy Programme (NISEP) since 1998 the NIAUR has played a significant role in this area and ensured that the 80% ring fence of the NISEP was targeted at fuel poor households as per the instruction from the Northern Ireland Assembly in 2002. We also believe that any new and emerging energy efficiency scheme such as Energywise should ensure that the profile of those receiving measures under the NISEP should receive at least the same measures in any new scheme which purports to use customer monies. It is a fact that the 'poor pay more' in market conditions, therefore the role of regulation in relation to correction of market failures, intervening in supply structures (price controls) and helping customers in vulnerable positions is fundamental to having fair, inclusive and transparent markets.

We believe that competition is good bringing about choice in service, quality and price. It can on the other hand be complex and exclude certain consumers. People on low incomes are not always best positioned to take advantage of such markets and at worst may be vulnerable to exploitation. For many households in Northern Ireland, there is no awareness that they can switch and with over 60% of electricity customers still with the incumbent supplier it seems that much more could be done to improve this situation.

That said, we believe the price control applied to the regulated companies can give us some trust in the market, and that the current mixture of regulation, in the form of the recent licenses and codes of practice etc. and competition goes some way in protecting consumers.

When markets fail to protect the vulnerable, especially in relation to vital commodities, it is incumbent on Government to intervene.

It is therefore our assertion that, should deregulation become an issue in the future something akin to the current mix of competition and regulation, is adopted. We depend on the knowledge and expertise of the NIAUR to ensure that the best is adopted for those who need it most and look forward to working with the NIAUR to that end.

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Appendix XII

Power NI Consultation Response

Review of the Effectiveness of Competition in the Northern Ireland Energy Retail Market – Phase II.

Regulatory Implications.

Utility Regulator Consultation

Power NI Response

18 March 2016

1. Introduction

Power NI welcomes the opportunity to respond to the Utility Regulator's (UR) consultation on Phase II of the review of the effectiveness of competition in the Northern Ireland energy market and specifically the regulatory implications.

As the only retail electricity supplier in Northern Ireland subject to price control regulation, Power NI is particularly concerned regarding the continued retention of price regulation and the lack of a clear regulatory position in relation to the market framework post its removal. To date the UR has arbitrarily sub-divided the market in an attempt to retain price regulation. In relation to the non-domestic market this position is currently untenable and is becoming increasingly unsustainable in relation to the domestic market. Power NI therefore welcomes the UR consulting on the post price regulation framework and hopes that it will result in overdue regulatory certainty.

2. The Non-Domestic Sector

For some time Power NI has argued that the non-domestic electricity market is competitive and it remains our firm belief that the UR should consult on the removal of price regulation in the non-domestic sector without delay.

To date, in relation to the non-domestic market, the UR has not yet dealt with the European context or the absence of harm. Power NI believes that within the non-domestic sector it is not dominant and despite the UR's assertion that the non-domestic sector is somehow benefiting from the current price regulated / non price regulated mix; Power NI considers the retention of price regulation to be ineffective, distortive and disproportionate.

European Context and the absence of harm

The European Commission has repeatedly stated its requirements in relation to price regulation. Publications such as the EC Communication "Making the internal energy market work" (November 2012, published January 2013) states that regulating of prices should cease.

In particular, section 3.2.1 states that:

"Member States should seek to cease regulating electricity and gas prices for all consumers, including households and SMEs, taking into account universal service obligation and effective protection of vulnerable customers. Suppliers should clearly spell out the different cost elements in the final cost for their customers, to encourage well-informed decision-making. The Commission will continue to insist on phase-out timetables for regulated prices being part of Member States' structural reforms. The Commission will continue to promote market-based price formation in retail markets, including through infringement cases against those Member States maintaining price regulation that is not meeting the conditions laid down by EU law."

ACER has also commented on the position of regulated prices: *"Regulated end-user prices are not compatible with the objective of establishing liberal competitive retail markets. Therefore, CEER will develop guidance, based on experiences at national*

level, on the approaches to be used to facilitate the phasing out of regulated end-user prices, as soon as practicable, whilst ensuring that customers are properly protected where competition is not yet effective”¹

The European commentary highlights the negative impact that price regulation has on competition and that any active market intervention to address a clear identified harm must be time limited. Further, the UR’s focus on the domestic context emphasises that there should be specific policy reasons for the retention of price regulation, which is not the case for the non-domestic sector in Northern Ireland.

In Northern Ireland the non-domestic market has active competition, unrestricted switching, Codes of Practice (including a Marketing Code) and full Market Monitoring. Given the level of competition in the non-domestic market in Northern Ireland, Power NI fails to see what specific and identified harm is mitigated by the continuation of price regulation.

Absence of dominance

The UR analysed the non-domestic market by reference to three market sectors (0-50MWh, 50-100MWh, and 100-150MWh per annum) during the previous price control process. Disappointingly, the UR does not publish market share information that allows for a like-for-like comparison with the data included in the price control decision. Nevertheless, Power NI has reviewed the information made available in the Quarterly Transparency Reports to assess the Power NI non-domestic market share. Using <70kVa as a proxy, the Power NI/Energia market share of the rolling 12 months consumption in Northern Ireland has been less than or equal to 50% for in excess of a year. As a result, the dominance trigger set by the UR has been met and a consultation exercise should be undertaken.

The Phase I Cornwall Energy Report does not clearly distinguish between domestic and non-domestic consumers. Nevertheless, we note that the Cornwall Energy Report highlights that the current segmentation of the market for the purposes of the assessment of dominance is unhelpful and should be considered further.

Separately, from a European perspective, the relevant market for the assessment of dominance may be the Island of Ireland, rather than Northern Ireland alone. This is due to the operation of the single electricity market, with price coordination and an aligned regulatory framework. This further strengthens the evidence that Power NI is not dominant in the non-domestic sector and therefore price regulation should be removed.

Ineffective

The UR’s 2013 Decision Paper included an assessment as to whether competition was sufficiently effective so as to “protect the interests of consumers in relation to

¹ ACER - Energy Regulation: A Bridge to 2025 Conclusions Paper (19 September 2014), and in particular, para 51

price". The Decision Paper concluded that the UR considered the 0-50MWh non-domestic sector remained in need of regulatory intervention.

Power NI considers this decision was fundamentally flawed. Price regulation is not in place for the entirety of this sector but rather a sub-section of a sub-section of the market share figure described above i.e. it is not in place for the entire 50% of the combined Power NI/Energia share but rather a percentage of Power NI's share only.

Based upon latest figures, Power NI supplies only 29,916 MPRNs or 102GWh of Q3 2015 sales on price regulated tariffs. Positioning this within the UR Quarterly Transparency Report this means that only 27% of consumption in the <70kVA reported sector or 8% of all non-domestic consumption is subject to price regulation. In terms of customer numbers this equates to 46% of <70kVA or 43% of all non-domestic consumers are subject to price control.

For the majority of customers price regulation offers no protection.

Distortive

Power NI has argued consistently that the retention of a price control in a market that is demonstrably competitive, compromises the proper operation of that market and is counterproductive. A regulated tariff that acts as a market reference price (and Cornwall acknowledge that the Power NI tariff acts in his way) but is based on an unrepresentative set of cost drivers distorts the market and leads to poor customer outcomes. These outcomes are clearly not in the best interests of customers generally, or those customers who are taking supply from a competing supplier, whose price offer is distorted upwards in line with the unrepresentative reference price. The UR is now faced with a situation whereby 9% of consumption² is driving the offers for the remaining 91%³.

The restrictive clauses with in Power NI's licence also prevent engagement with the various TPI's active in the market. This narrows this form of competition and prevents full competitive pressure being realised.

As set out above, the European Commission is increasingly concerned about the distortive effect that the maintenance of price regulation can have on the development of competition in electricity supply markets.

Disproportionate

The retention of price regulation in the non-domestic sector has a significant impact on the Power NI business. As you will be aware, linked to the price control requirements are additional licence conditions in relation to business separation, independence and the use of assets. These conditions prevent Power NI from realising efficiencies and economies of scale which would benefit consumers. The current standpoint of the UR has not been adequately justified, particularly in light of

² Price regulated demand as a percentage of non-domestic excluding LEUs who will seek bespoke tariffs

³ While the UR has not accepted this reference in the past it is noteworthy that the recent DFP tender asked for pricing in reference to the "regulated" commercial price.

the UR's statutory duty to protect consumers, including by way of promoting competition within the electricity supply sector.

Power NI believes that by actively restricting its managerial and operational model, the UR is treating Power NI in a manner which is not consistent with its competitors, some of which are part of much larger organisations and are actively utilising the economies of scale their respective Groups can offer. The restrictions placed upon Power NI are increasing cost to consumers and restricting the further development of competition in Northern Ireland.

For these reasons Power NI believes that the focus of the Phase II work should be on the post-price control domestic market regulatory arrangements only. The UR has said within the consultation paper that it is "*sufficiently concerned about ineffective competition for the same I&C customer group*" however fails to provide any evidence to justify this statement.

Power NI would welcome the UR clarifying –

- What specifically is the UR concerned about?
- Does the UR have any evidence of harm?
- How has the UR judged "effective competition"?
- What evidence supports this?
- What steps are the UR taking to address this perceived lack of competition?
- Does the UR believe it is best placed to intervene in the market?
- How long will this intervention last?

In not presenting this information the UR is not fulfilling its European requirements in relation to its market intervention and failing to meet its statutory duty not to discriminate between parties involved in the supply of electricity.

3. The Domestic Market

In relation to the domestic electricity market the European context and questions discussed above equally apply. It is inherent upon the UR to identify a clear harm, explain the intervention and include a time limit. The UR has yet to do this.

To some extent Power NI acknowledges that the UR may be able to meet these criteria in the domestic market due to the current market shares of participants. This is however changing with new participants entering the market and existing suppliers changing tactics.

Within the paper the UR explicitly states that they are unwilling to fetter their discretion in relation to future decisions. In not providing clarity, the UR compounds the current uncertainty and places that risk on market participants. It is vital that through this consultation process the UR establishes a clear framework for the post price control market. Without this how can current participants be expected to plan and will new participants enter into such an uncertain regulatory environment?

Uncertainty will undoubtedly increase the cost of capital for all suppliers. This is an industry wide issue as all market revenues flow through suppliers to network companies and generators etc. and ultimately become a cost to consumers.

The consultation outlines 7 potential options which could be applied in a post price control, domestic electricity market –

- Identification of significant market power
- Inactive customer price control
- Default tariff
- Tariff cap spread
- Dominance Thresholds
- Gross margin cap
- Price to beat

At a principle level Power NI favour less UR intervention. Any form of UR price setting represents a significant risk to affected suppliers and should be strongly resisted. Price setting is a core supplier activity, critical to the financeability of the business. Should the UR determine any form of price are they willing to indemnify affected suppliers should it be incorrectly set?

4. Specific Questions

As discussed above, Power NI believes the frameworks outlined by Cornwall should be considered in relation to the domestic electricity market only.

Q1. Whether each option strikes a fair balance between the rights of customers and the rights of any supplier which would be subject to that option?

Power NI is somewhat surprised by the wording of the UR's question. Consumers' rights are governed by consumer protection law. The UR's statutory mandate is to ensure the protection of vulnerable customers and the promotion of competition.

Through the last number of years the UR has taken steps to implement unrestricted switching, significantly increase the amount of information provided to customers, extend the remit of the various Codes of Practice, write the marketing rules and implement market monitoring.

The UR should set the framework for the market, ensure customers are informed, switching is possible and anti-competitive behaviour is avoided. It is important that the UR focus on enhancing competition rather than considering measures which will stifle it.

The options described by Cornwall raise a number of customer related issues. Two main questions come to the fore from a customer perspective –

- In relation to the options in which the UR adopt a price setting role, is the UR best placed to set tariffs?

- In relation to the options in which the UR is forcing choices on a customer, is the UR comfortable assessing an individual's requirements and deciding what is best for them? e.g. the inactive price control in which the UR would decide that the customer is disengaged then would not allow marketing from their current supplier unless they switched away.

Equally, a supplier should be allowed to operate in a market which is clearly defined and transparent. Regulatory uncertainty and risk is unhelpful in that regard. The UR should ensure that the framework provides an incentive for suppliers to be competitive in terms of price and service, with the penalty for failure the loss of market share.

At a principle level, any option which involves the UR setting a price exposes the supplier(s) to high levels of regulatory risk. As such the "inactive customer price control", the ex-ante "default tariff" option, the "tariff cap spread" and the "gross margin cap" proposals all unjustifiably increase regulatory risk for suppliers.

It is noteworthy that Cornwall Energy highlighted that a group of former GB regulators in writing to the CMA, raised concerns in relation to potential external pressure which a regulator would come under in setting prices and a tendency to seek short term benefit at the expense of long term sustainability, choice and new entry. Power NI believes previous regulatory regimes in Northern Ireland also sought short term benefits at the expense of medium term price stability.

Q2. Whether each option strikes an appropriate balance between the protection of customers and the promotion of competition?

As stated above, the UR should recognise that consumer protection in the retail context is governed by consumer protection law, provisions within the Competition Act and the role of Trading Standards. Has the UR identified any electricity market specific gaps which are not adequately covered by existing legislation? Should this not be advised to DETI?

As also described above, the UR should also be cognisant of the distortive effect of regulated prices (in any of the varied proposed forms) on the effective operation of the market. This issue is recognised at a European level and Power NI believes is already present in the non-domestic electricity market and will increasingly be witnessed in the domestic market.

Q3. Whether each option is likely to protect vulnerable customers (including, in particular, persons who are chronically sick or disabled, of pensionable age, on low incomes or residing in rural areas)?

Each of the options represents a risk to consumers regardless of their vulnerability. As described above, those options which involve less regulatory intervention are best placed to result in a competitive outcome. The REMM framework facilitates robust monitoring and could prompt the UR to request information from suppliers to justify their actions. A failure to adequately justify their actions may prompt the UR to refer the matter to the relevant authorities under the legislation noted above.

This approach would both ensure the market can operate and enhance the enforcement of competition law through the availability of information. This outcome is more efficient, transparent and cost reflective than a distortive regulatory price or regulatory decision making on behalf of consumers.

As described throughout this paper, a regulated price or margin is distortive and will lead to poor price outcomes over the short and long term.

Of equal concern is a reliance on an imposed framework replacing customer choice. Switching levels are not the only metric of effective competition. The UR should look to the metrics surrounding awareness and customer satisfaction. Ultimately in a competitive market suppliers will look to gain and retain market share. The UR and Cornwall Energy appear to ignore the retention aspect. Competition drives suppliers to deliver service and price which build customer trust and satisfaction. If the supplier can achieve this they can retain their market share. This is competition being effective. It has driven the behaviour of a supplier (sufficiently concerned about the competition) to ensure that their customer offer is such that the customer will not be tempted by a competitors proposition.

Q4. What are the burdens that are likely to be placed upon suppliers made subject to each option?

As described above, any option which involves a regulatory price or ex-ante review places a disproportionate burden and regulatory risk upon suppliers. As the UR is aware a price control process is lengthy and onerous. A number of the options include such a requirement (inactive customer price control, ex-ante default tariffs, dominance thresholds and gross margin cap). The price control process is not suited to a dynamic market setting. The review itself typically takes 18-24 months to complete and as the UR further sub-divides regulated/non-regulated thresholds it only becomes more complicated and open to error. While price controls are required in a monopolistic setting and have a place during market transition, in a market with open competition they are a transitory measure.

Removing the commercial decision making process from the business in question relies on the UR's ability to get all decisions right. Will the UR indemnify a supplier against uneconomic decisions?

Q5. Are those burdens disproportionate to the benefit secured and, if so, is there a less intrusive or onerous measure could be implemented by the UR?

Power NI believes the burdens associated with regulatory pricing, default tariffs, price controls and margin caps are excessively onerous. The UR should look to the competitive market, active monitoring and step in measures as a means of facilitating an effective outcome in the interests of consumers.

Q6. Do consultees have any other comments on the options put forward?

Power NI has no further comments.

Q7. Are there any other options not included in Cornwall's list?

Power NI is somewhat surprised that Cornwall Energy did not explore both the European requirements and the likely outcomes of a liberalised market with enhanced market monitoring as a base case.

The perceived harm is set at an assumed level with no analysis or likelihood assessment. There is also no indication of a time limitation for intervention which is also a European requirement.

Q8. Feed back is sought as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring. This consultation seeks views on whether there should be a period of deregulation or an immediate move to any of the options presented.

Power NI strongly believes that the electricity market should be allowed to operate without price controls. The UR has taken significant steps to implement retail market monitoring and enhanced Codes of Practice. It is now time for the UR to implement a regulatory framework which is consistent with other markets and thereby align with both European and national objectives.

5. CMA Provisional Remedies

The UR has indicated an intention to take into account the CMA Energy Market Investigation. Power NI notes that a provisional decision on remedies was published on 10 March 2016.

While proposals in relation to customer databases and prepayment measures may grab the headlines it is important to recognise that the CMA also looked at many wholesale and policy issues affecting competition and end user prices.

Power NI would welcome the UR also critically reviewing the wholesale electricity framework and specifically the ISEM design to ensure that the outcome delivers a benefit to customers. In particular Power NI would welcome a UR focus on the design of the forwards market which is critical for the delivery of price stability.

In reviewing the CMA's provisional decision it is important to recognise the fundamental difference in the Northern Ireland prepayment solution in comparison to those in place in GB. As the UR is aware the prepayment solution in Northern Ireland is overwhelmingly a lifestyle choice made by consumers and does not have the debt stigma which appears prevalent in GB. As the UR is also aware, prepayment tariffs in Northern Ireland are lower than "standard" rates due to the working capital benefit realised. The common services model in Northern Ireland also affords unrestricted switching regardless of meter type.

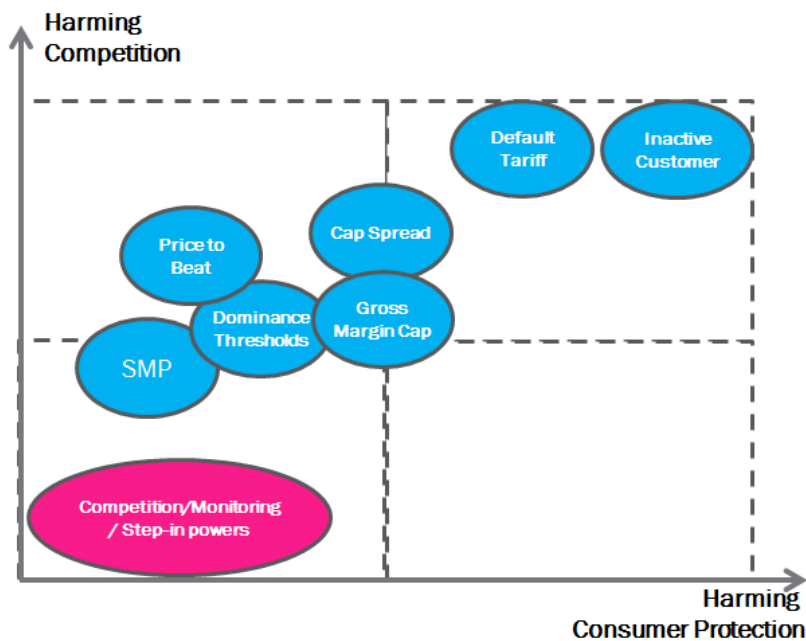
It is noteworthy that the CMA expressly calls for an evidence based decision making approach to be adopted in relation to regulatory interventions in the market place; reinforcing the need for rigorous testing and trialing. The CMA also supports the use of principles rather than detailed rules.

Additionally, the CMA provisionally found that Ofgem’s statutory objectives and duties may constrain its ability to promote effective competition. Power NI believes that the UR’s statutory obligations suffer from the same constraint. The issue which the CMA highlight in relation to Ofgem needing to be more proactive in analysing and communication the effects of government and regulatory policies on energy prices is also equally applicable in Northern Ireland and Power NI would welcome the UR taking steps to increase transparency in this issue

In summary, Power NI notes that aside form the prepayment issue which is not applicable to the Northern Irish context; the CMA has focussed on customer engagement, regulatory transparency and evidence based decision making. This is significantly different from all of the Cornwall Energy options and set in a context which does not have the comprehensive REMM programme or extensive Codes of Practice in place in Northern Ireland.

6. Conclusion

Power NI has attempted to map the options put forward by Cornwall Energy.



The options described all present aspects of harm to consumers and or competition. Any option which places a reliance on an imposed framework replacing customer choice raises protection concerns. Switching levels is not the only metric of effective competition. The UR should look to the metrics surrounding awareness and customer satisfaction. Ultimately in a competitive market suppliers will look to gain

and retain market share. The UR and Cornwall appear to ignore the retention aspect. Competition drives suppliers to deliver service and price which build customer trust and satisfaction. If the supplier can achieve this they can retain their market share. This is competition being effective. It has driven the behaviour of a supplier (sufficiently concerned about the competition) to ensure that their customer offer is such that the customer will not be tempted by a competitors proposition. The UR should recognise that consumer protection in the retail context is governed by consumer protection law, provisions within the Competition Act and the role of Trading Standards.

Equally, any option which involves a regulatory price or ex-ante review places a disproportionate burden and regulatory risk upon suppliers. As the UR is aware a price control process is lengthy and onerous. A number of the options include such a requirement (inactive customer price control, ex-ante default tariffs, dominance thresholds and gross margin cap). The price control process is not suited to a dynamic market setting. The review itself typically takes 18-24 months to complete and as the UR further sub-divides regulated/non-regulated thresholds it only becomes more complicated and open to error. While price controls are required in a monopolistic setting and have a place during market transition, in a market with open competition they are a transitory measure.

Power NI strongly believes that the electricity market should be allowed to operate without price controls. The UR has taken significant steps to implement retail market monitoring and enhanced Codes of Practice. It is now time for the UR to implement a regulatory framework which is consistent with other markets and thereby align with both European and national objectives.

Appendix XIII
SSE Airtricity Consultation
Response



SSE AIRTRICITY RESPONSE TO
THE UTILITY REGULATOR ON REVIEW OF THE EFFECTIVENESS
OF COMPETITION PHASE 2

2016

INTRODUCTION

SSE Airtricity welcomes the opportunity to comment the Utility Regulators consultation paper on the Review of Effectiveness of Competition Phase 2 which considers the regulatory options for the Northern Ireland (NI) energy supply markets which could replace the status quo should the current form of price regulation cease.

GENERAL COMMENTS

SSE Airtricity considers that the energy supply markets in Northern Ireland have progressed significantly over the past number of years. Competition has developed in some areas; however, there are a number of markets where competition is not fully established. This is partly due to the limiting size of the market which makes the scope for commercially viable suppliers low, and also structural or regulatory issues.

SSE Airtricity fully supports the development of competition and any associated removal of regulatory barriers to facilitate growth in competition. While the publication of the Regulatory Options paper is welcomed, SSEs view is that more can be done to increase competition in the market. Data shows that a significant number of customers have not switched and SSE is of the view that measures to increase awareness of the benefits of switching should be prioritised over longer term regulatory measures that can only be implemented with a certain level of existing competition and customer engagement in the market. These levels have not been achieved in domestic energy markets in Northern Ireland.

SSE Airtricity has serious concerns about the comparison or link that the paper appears to be making between the findings of the Competition and Markets Authority (CMA) Review undertaken in Great Britain and the Northern Ireland (NI) supply market. SSE believes that both markets are at completely different stages of development and it is unjustifiable to suggest that the CMA findings have implications and/or learnings for the current NI market. While in principle the goals of some of the consultation options have merit, the Options seem to have been developed in an attempt to address issues in the Great Britain market rather than in NI. SSE would also note that the CMA investigation is ongoing and many of the responses to the preliminary findings found flaws and inaccuracies in the CMA analysis¹. If comparisons are to be made with the state of the GB market, SSE would

¹ See: https://assets.digital.cabinet-office.gov.uk/media/55a908c3e5274a6fea000013/Stephen_Littlechild_-_Submission_to_PFs_and_notice_of_possible_remedies.pdf

note that an outcome of the CMA review was that the regulator introduced some rules that restricted suppliers' ability to innovate and offer tariffs tailored to customers personal circumstances². SSE would caution against the continued introduction of prescriptive regulations and rules in the current market given the possible knock on impact on innovation and competition that this can have as evidenced by the GB experience. This in conjunction with continued price regulation would reduce competition.

SSE is unclear as to how the Utility Regulator can make a decision on the application of any of the options without knowing what these options are going to be addressing. This makes it particularly difficult for SSE to evaluate the options without reference to the current market. It is unclear as to the Utility Regulators (UR) view on the market conditions that would lead to a cessation of the current form of price regulation. The criteria set out for the removal of price regulation in the non-domestic electricity market did not indicate the point at which the UR would deem that price regulation was no longer required but these represented the basis on which further consultation would take place (SSE would also argue that these criteria are insufficient and should be reviewed³). Without understanding the situations or instances where the options would be considered, SSE cannot fully evaluate each option. SSE considers that the first step of this exercise should be for the UR to set out its objective for the market and identify the options that can achieve the objective. If price deregulation is an objective, UR must identify the market conditions that would support the removal of the current form of price regulation before identifying the options that it will use in remedying any anomaly after price deregulation.

Many of the options are akin to price regulation. The introduction of such interventions in response to a perceived issue in a market would be onerous on the affected suppliers. The reintroduction of price controls could only be justified if designed in a manner to fix a real issue impacting on competition. These options would represent a significant intervention in the market and would have profound implications for competition. There is a significant risk of adverse consequences of such interventions in a market where conditions allowed for the lifting of price controls. Consequences would include a: decrease in customer engagement as customers are dis-incentivised from engaging; decrease in competition; deterrence of new suppliers from entering the market; increase in regulatory uncertainty with a knock-on impact on customer prices. The imposition of regulated prices, margin caps or price caps for one or all suppliers would have significant practical issues in implementing and would be subject to errors. Such errors could put suppliers in a loss making position and this uncertainty and the possibility that this could happen would deter market entry and expansion, or induce market exit.

² This view was also supported in the response by industry experts. Ibid.

³ See response to Price Control Approach Consultation in December 2015.

Related to this, while SSE identifies a number of issues with the individual options identified in the consultation paper, at a broader level SSE would question the Utility Regulators legal powers to implement some of the options identified.

There is a lack of recognition of the benefits that a fully competitive and price deregulated market can bring. The protection of consumers is the Utility Regulators main role and delivering effective competitive markets is part of this. SSE Airtricity is concerned that the majority of the options presented retain a form of price control. Experience in other markets, such as the Republic of Ireland, show that markets can be competitive and deliver for customers without the need for price control. The face of retail regulation has changed in such markets and customers have benefitted in terms of more competitive prices, innovation, more options and the development of competition in terms of customer service and protection. NI now remains one of a declining number of European jurisdictions that retains price regulation **and** has no roadmap for price regulation removal⁴. It could be argued that this has competitiveness implications not just for the NI energy industry but for the wider Northern Irish economy and consumers as a whole. While there is a clear recognition of the benefits of competition and price deregulation at a European Union and international level, SSE would question the Utility Regulator's commitment in this regard.

SSE Airtricity is of the view that the Utility Regulator needs to consider how it can remove current structural barriers to greater competition that exist in the market. These barriers include:

- Small market size. In particular gas where there will soon be three distribution areas;
- Only recently opened markets;
- Low profit margin regulated markets, in particular gas supply;
- Relatively high level of meter interference (theft) in the market;
- Continuing clear links between distribution and supply businesses, particularly in 10 towns area;
- The presence and continuous review/introduction of prescriptive regulatory requirements which create a burden on suppliers, restrict innovation and present a barrier to entry;
- Fragmented market segments (three gas distribution areas);
- In electricity, regulated prices and their volatility have a significant impact on the ability to do business in particular with respect to smaller commercial contracts. Regulated prices do not move with the markets, lags in changes are hard to explain and have in recent years been significant.

⁴ Derived from CEER Market Monitoring Report 2015. The Utility Regulator has identified criteria for the non-domestic electricity market but has stated that this point is not an automatic trigger for deregulation but the UR will undertake further consultation.

SSE would note, however, that given the size of the market, there may always be a small number of suppliers operating in the market. While this is the case, it should not undermine efforts to reduce barriers to entry where practical (e.g. addressing the low margin gas domestic market). Our view is that it is possible to develop a higher level of competition in the NI markets, provided the correct market signals are provided and the structure of the market is appropriate

The consultation paper states that '*customers who wish to switch have arguably done so.*'. This statement has no foundation and should be backed up by evidence. SSE considers that many customers may not fully understand the benefits of switching or even may not be aware they can switch. Efforts to increase awareness and switching rates should take priority in the immediate term to determine the potential of the market.

The paper states that the options were informed by research into regulatory frameworks in other jurisdictions worldwide. Unfortunately no information was provided in the paper on the experience elsewhere. It would be useful for suppliers to have information on the application of these options elsewhere to determine their practicality and impact. Looking at other jurisdictions, SSE would also highlight that there is recognition internationally that price controls can restrict competition and so the trend is to remove price controls not reintroduce them (e.g. in New South Wales).

Finally, SSE would caution against the reliance on REMM information to make significant decisions. SSE is of the view that the data can be used to inform the UR and provide information on trends and the development of competition but should only be used as a trigger for further investigation rather than the reason for a significant decision to be made.

RESPONSES TO CONSULTATION QUESTIONS

The following section outlines SSE Airtricity's response to the specific consultation questions. These responses distinguish between domestic and IC where relevant.

Q1. Whether each option strikes a fair balance between the rights of customers and the rights of any supplier which would be subject to that option?

In a situation where the current price controls have been removed, it can be assumed that incumbent suppliers no longer hold dominant positions in the market and / or there is a sufficient level of competition in the market. Some of the options identified for regulatory intervention in this situation target the 'incumbent' suppliers (specifically option 2). This is contrary to what the situation is in the

market if the UR has deemed that price controls should be removed. There are no longer any incumbent suppliers so there should be no reason to target them specifically.

SSE has provided a response to this question under each option below.

- Option 1 – Significant market power

This option would see Regulatory intervention where a supplier is deemed to be in a position of significant market power (SMP). The option does not describe how SMP would be measured but that such would be enshrined in all supply licences. While the paper states that SMP would be similar to, but fall short of, dominance, it is not immediately clear to SSE what the difference would be. SSE would be of the view that in a scenario where the current price controls are no longer deemed appropriate, there should be no issue in relation to dominance or SMP. However, this option would help ensure that SMP or dominance does not become an issue in the market.

While there are some limitations, in comparison to some of the other options, this may provide a less intrusive method of intervention in the market. This option could potentially strike a fair balance between the rights of suppliers and customers given that customers would be protected from unfair practices without the need for restrictions on customer choice. In relation to competition, suppliers would be protected from any potential dominance in the market.

- Option 2 – Inactive consumer price controls for incumbents

This option is targeted at the former incumbents. While the incumbents may have been deemed no longer dominant, there may be a subset of customers that have never switched. SSE considers that there are a number of limitations associated with this option and it does not strike a balance between the rights of customers and suppliers.

This option does not support switching and could have detrimental impact on competition in the market. SSE would argue that some customers may have made the choice not to switch and therefore imposing price regulation on this specific set goes against their rights as consumers. This option makes the assumption that disengaged/inactive customers pay significantly more for their energy than engaged customers. In a price deregulated market, it is assumed competition thrives. Competition is underpinned by customer switching, and regulatory measures introduced that do not support switching will therefore negatively impact competition. SSE would highlight that customers who stay with a supplier may have switched package with the supplier and so may already be on a publicly available tariff. This option does not consider that this scenario happens in reality and furthermore, the option restricts the 'regulated' suppliers from marketing to customers on the inactive tariff, even if that supplier has the most competitive offer in the market. Customers must switch to a

competing supplier in order to be on an unregulated tariff. This is inappropriate and compounds the issue.

SSE would also have concerns that imposing price regulation on a part of a suppliers business will impact on the service and offers it provides to other customers.

SSE also suggests that this option would create high levels of confusion and uncertainty in the market.

- Option 3 – Default tariff

This option in effect introduces price regulation across all suppliers. The UR would assess if a suppliers default tariffs are fairly priced including their profit margins. The default tariff would be reflective of the costs and a 'reasonable profit'. This in effect is price regulating all suppliers in the market and SSE would question the legality of this option.

SSE considers that this option would have serious negative consequences on suppliers. In particular, suppliers who entered any market and were not price regulated would only be required to make a profit margin at a maximum of 1.5% (if we take the example of the current regulated gas margin). This 1.5% would be applied to the default tariff but in this option no customer of a supplier can be on a tariff higher than the default and therefore the supplier will never be profitable. The UR seems to forget that suppliers are commercial entities and by their nature must make a profit. The rights of suppliers would be seriously affected by this option. The rights of customers may also be affected as there would be no incentive on suppliers to offer a tariff less than the default (or they would risk making a loss).

Additionally, this option would present serious enforcement difficulties. The Cornwall Energy paper outlines the possible audit process that would be undertaken for a default tariff and states that if the UR deems a default tariff not to be reasonable and where a supplier cannot justify the rate, the UR will investigate or take enforcement action. We consider that if this option was to be seriously considered then the UR will have to be explicit in terms of what it considers 'reasonable' and what will and will not be accepted by the UR as 'justification' for the tariff. The UR would have to be clear about the instances where an investigation is warranted and where and what enforcement action will be undertaken. Without clear guidance for suppliers, we would be at risk of creating an even greater barrier to entry and creating a disproportionate burden on existing suppliers. Suppliers are commercial entities and need certainty and clear guidance in order to undertake their business so any unclear processes, methodologies or terms will increase uncertainty in the market and therefore costs.

- Option 4 – Tariff cap spread

In a competitive market, suppliers are operating in a scenario where they must strike a balance between the option of pricing below cost and above

competitor prices. In effect there is already a 'tariff cap spread' situation in a competitive market without the need for regulatory intervention. The 'tariff cap spread' option, however, seems to suggest that the UR would estimate the spread for each supplier using certain criteria and by analysing that suppliers customer base. The proposals states that there would be provisions for green tariffs, which SSE would be supportive of.

In practice, price spread changes over time as market conditions change. In this scenario, the UR would have to be responsive to market changes and have the knowledge to know when the spread should be changed. In this respect, the option does not support the rights of suppliers to change prices when required because the defined spread might not be sufficient to allow this.

This option also has the potential to confuse customers and may result in a reduction in the number of offers available to customers thus affecting customer choice.

- Option 5 – Dominance thresholds

This Option has merit and SSE considers that this would have to be an option if any market was fully price deregulated. This option in effect is 'price reregulation'. It may not apply to the incumbent but should bear the same criteria as those used to deregulate the market. While customers may not necessarily be negatively impacted by the dominance, it has implications on competition, suppliers and other factors.

The paper suggests that dominance would be determined based on a number of factors (market share, active suppliers, switching). SSE considers that each market must be evaluated in isolation to determine the relevant dominance thresholds that would be applied and these factors would not be the same across markets.

With regard to the HHI and other metrics to determine concentration or market share, SSE would caution the use of some metrics in small markets. While in large markets there can be a large number of suppliers, in smaller markets, such as Northern Ireland, these ratios may not provide insightful data unless they are adjusted to take account of market size.

Certainty will be important to suppliers in this situation and the UR should be clear about what type of intervention will be introduced if a supplier is deemed to be dominant and of course in relation to the dominance factors being evaluated. This is an onerous option in the scenario where the current price regulations have been removed. The reintroduction of price controls in such a scenario could only be justified if it is designed to fix a very real and serious adverse effect on competition.

- Option 6 – Gross margin cap

This option would see the introduction of gross margin regulation (or price regulation) for all suppliers in a market. The cap would be a market wide cap.

SSE is unclear as to the purpose of this option as an interim /post price regulation solution in a competitive market given that it is reminiscent of price regulation. SSE would highlight that UR has stated that these options will only be considered when/if the current form of price regulation is removed. SSE cannot see how this option supports competition or protects consumers in a competitive market.

The option states that the focus would be on more established suppliers. Given SSEs general concerns about the existing market, we consider that this would represent a barrier to entry. Currently in the domestic gas market there is a 1.5% margin cap in place for the existing suppliers. SSE has stated its view on a number of occasions that the current low-margin domestic gas market is not an attractive market for new entrants and therefore not encouraging of competition. Clear guidance would need to be provided to new entrants as to when price regulation will be applied to them.

SSE would point out that this option assumes a situation where there is a unit charge and a standing charge. This is not the situation at present and there is no evidence to suggest that this will change.

- Option 7 – Price to beat tariff

It is not clear if this tariff is for the market or individual suppliers. If it is a market rate, it would be very difficult for the UR to develop a 'reasonable price' which takes account of all supply costs and reasonable margin. Depending on existing supplier costs, which vary across suppliers, there would be some suppliers that would benefit considerably and other that would not benefit.

Notwithstanding the ambiguity, this option is very similar to the gross margin cap option and would almost represent the price reregulation of the market.

SSE agrees that this option would be resource intensive for UR but would argue that many of the other options will also require ongoing updating and communication with industry. The current price controls are extremely resource intensive for both the affected suppliers and the UR. Many of the options presented would require similar levels of resources, or more, and are not practical or rational in a market that has been deemed competitive. The paper states that this option would respond to changes in market conditions. But there is no acknowledgment of changes in supplier conditions. The fact is that suppliers are structured in different ways, some have parent companies and others operate in different markets. Many changes within supplier companies are dictated elsewhere and regard should be taken account of this. This option simply ignores the reality of the situations that suppliers operate under.

Q2. Whether each option strikes an appropriate balance between the protection of customers and the promotion of competition?

The options do not facilitate competitive forces to operate at their maximum and therefore may not result in the level of consumer protection that a fully competitive market can provide. SSE is of the view that the options describe situations where the Utility Regulator can maintain a significant level of control in the market and are primarily price related. The paper ignores the fact that suppliers in Northern Ireland already have stringent obligations set out in their codes of practice which ensure customers are protected. These obligations would likely continue in a hypothetical market where the current form of price regulation ceases.

The options do not facilitate competition. The options regarding non-switchers only inhibit competition and could potentially reduce the level of competition and choice for customers. The best approach to address sticky customers is firstly to understand fully the reasons why they do not switch, to promote the benefits of switching (in a competitive market) and to address any issues. The message from the Regulator should be one that supports competition and switching, not one that assumes a monopolistic situation in the market.

While this is the case, we see merit in considering actions that may increase the level of switching and SSE considers that more can be done by the UR and other key stakeholders to inform customers of the benefits and to support the competitive market. SSE notes that the recent UR Work Programme contained a work item on customer education and switching but that this was not listed as a priority project. This is concerning for SSE given the immediate benefits to customers and the market that could be realised from such an exercise.

The paper states that *'Promoting effective competition and protecting consumers are both obligations of a national regulator under EU law'*. While this is stated in the consultation paper, in practice, and as evidenced by the consultation, the UR places all its efforts in the area of customer protection and seriously neglects on its duties to promote and support competition. The UR does not seem to recognise the benefits that competition can bring, for example:

- Downward pressure on prices;
- More options for customers;
- Innovation;
- Higher levels of customer protection as suppliers will compete on customer service, etc.

Competition and customer protection go hand in hand and SSE has evaluated each of the options below.

- Option 1 – Significant market power

SSE would be of the view that in a scenario where the current price controls are no longer deemed appropriate, there should be no issue in relation to dominance or SMP. Nevertheless, SSE is of the view that this option could help protect customers and could assist in the development of competition. However, this option would only be required where a market player (s) has a SMP position in the market.

- Option 2 – Inactive consumer price controls for incumbents
This option assumes that disengaged customers are being exploited when this is not the case in reality. Customers may not engage with the market for a variety of reasons and should be encouraged to engage with the market through customer education. This option does not promote competition.
- Option 3 – Default tariff
This option does not support customer protection or the promotion of competition.
- Option 4 – Tariff cap spread
This option does not support customer protection or the promotion of competition. This option limits the amount of options available to customers and in the market.
- Option 5 – Dominance thresholds
This option achieves customer protection and can protect competition, but only if it is clear to all what the dominance threshold is. SSE would highlight however that this option would not be necessary in practice given that the cessation of price regulation will inevitably develop competition further and benefit customers.
- Option 6 – Gross margin cap
This option does not support customer protection or the promotion of competition.
- Option 7 – Price to beat tariff
This option does not achieve customer protection or the promotion of competition.

Q3. Whether each option is likely to protect vulnerable customers (including, in particular, persons who are chronically sick or disabled, of pensionable age, on low incomes or residing in rural areas)?

SSE suggests that it is impertinent to assume that vulnerable customers are not in a position to shop around or switch or are in a financially unviable situation. SSE Airtricity considers that the current obligations set out for suppliers in the codes of practice offer vulnerable customers a high level of protection. Even in a situation where one of the Options exists, the requirements around the protection of the most vulnerable customers will remain.

SSE does not consider that vulnerable customers will be affected differently to other customers by any of the options proposed.

Q4. What are the burdens that are likely to be placed on suppliers made subject to each option?

SSE would raise some serious concerns in relation to the burdens that are likely to be placed on suppliers. Most of these burdens are common across options. Under most options suppliers would no longer be in control of their own business and therefore would not be free to meet commercial needs. This lack of control would result in a restriction in the activity of affected suppliers and impact on their ability to innovate and compete. The options would negatively impact on competition, would represent a significant barrier to entry and potentially lead to market exit.

Each option is summarised below.

- **Option 1 – Significant market power**
This option would see new licence conditions in place for all suppliers. Without a definition of SMP, it is difficult to determine the impact on suppliers. This option would require the UR to set out a clear definition of what SMP is and the scenarios where a supplier (s) would be regarded to be in a SMP position. UR would also need to set out a clear process for industry in relation to the intervention that would likely take place. Without a clear process, suppliers will not have certainty and this will impact on their operations.
- **Option 2 – Inactive consumer price controls for former incumbents**
This will only affect the former incumbents and will present a significant burden on SSE. The incumbents will need to invest in the same level of resources as required under existing price regulation arrangements. This would present a burden in the scenario where price regulation has been removed. SSE would have to divide its existing customer base into two subsets and would have to set up monitoring units to determine which customers are active/ inactive on an ongoing basis.
- **Option 3 – Default tariff**
SSE will need to invest in the same level of resources as required under existing price regulations. This option effectively imposes a regulated tariff on all market participants. Where a price control is introduced, the Regulator needs to ensure consistency in the evaluation of the price on an annual basis.
- **Option 4 – Tariff cap spread**
Depending on how the UR will develop the tariff cap spread, this may not present a significant burden in terms of resources. However, the implications of a stationary spread level (i.e. one that is not updated

regularly) could result in a significant financial burden on suppliers. This option requires that suppliers would inform the UR of any new tariffs, and we assume SSE would have to inform the UR of the cessation of certain tariffs. This is burdensome in a fast-moving competitive market. It is also unclear if this includes introductory offers.

- Option 5 – Dominance thresholds
This is effectively the same as the current situation in regulated markets. However, it will be important that suppliers are well aware of the scenarios where this option could occur and when exactly the UR will impose it on a supplier. This creates certainty and therefore means that resources can be effectively utilised.
- Option 6 – Gross margin cap
This is price regulation and will present a significant burden on SSE, and all suppliers in a market, both in terms of financial and other resources.
- Option 7 – Price to beat tariff
Significant burden because SSE sets prices in a certain way and prices will be set in response to various factors. There is potential that this 'price to beat' will change over time and will impose an additional factor for SSE to consider when reviewing tariff.

Q5. Are those burdens disproportionate to the benefit secured and, if so, is there a less intrusive or onerous measure could be implemented by the UR?

The burden varies depending on the Option. In general most options present significant burdens and do not provide much in terms of benefit in a market where competition has developed.

SSE would consider that option 5 is the most realistic and is likely to be required in an event where the UR removes price regulation.

Q6. Do consultees have any other comments on the options put forward?

As discussed earlier, many of the options are akin to price regulation. The introduction of such 'remedies' in response to a perceived issue in a market would be onerous on the affected suppliers. The reintroduction of price controls could only be justified if designed in a manner to fix a real issue impacting on competition. While this is the case, these options would represent a significant intervention in the market and would have profound implications for competition. The imposition of regulated prices, margin caps or price caps for one or all suppliers would have significant practical issues in implementing and would be subject to errors. Such errors could put suppliers in a loss making position and this uncertainty and the

possibility that this could happen would deter market entry and expansion, or induce market exit.

Related to this, if current price controls have been removed for a period, the reintroduction of such significant interventions could risk dis-incentivising customer engagement and undermining customer trust in competitions to deliver the best outcomes.

Some of the options are based on assumptions that are contrary to the current situation in the market. For example, some options assume that prices are comprised of a unit and a standing charge. This is not the case and SSE does not know of any timeline for this to change.

The consultation paper made a point of stating that option 7 would be resource intensive for UR. SSE would argue that many of the other options will also require ongoing updating by UR and communication with industry. The current price controls are extremely resource intensive for both the affected suppliers and UR. Many of the options presented would require similar resources (or more) and are not practical or rational in a market that has been deemed competitive.

We consider that upon the consideration or implementation of any option, the UR must provide industry with clear guidance on the specifics of each option. This would also be the case for any possible enforcement action that the UR will consider in each scenario. A lack of clear and consistent guidance will increase uncertainty in the market and add to commercial entities operating costs.

Q7. Are there are any other options not included in Cornwall's list?

SSE Airtricity is of the view that the Utility Regulator needs to consider how it can remove barriers to greater competition that exist in the market currently. The paper focuses on a future unknown scenario when the focus should be on the future direction of the market and how this can be achieved.

The following are some current issues in the market which impact on the level of competition, and potential solutions include:

- Promoting switching. Promotional campaigns can be useful and assist customers in educating themselves and choosing to switch. However, these must be targeted and switching processes need to be easy and clear for customers. SSE would highlight however that there are a cohort of customer who may not want to switch and this should be taken into account when evaluating the options identified.
- Addressing the small market size. SSE Airtricity believes extending the gas network may improve competition as the more customers available the more attractive the market may be to suppliers. However, at this time NI is

operated as two separate markets with different distribution operators and different practices and charges in some cases. Adding a third set of requirements for a minimal number of customers when the network is extended to the west could prove problematic. Consideration should be given to harmonising practices and charging. Extending the gas network may have a positive impact on financially vulnerable customers as it will allow wider access to more competitively priced fuel which has a positive impact.

- Revenue protection (RP). Theft is a key issue for suppliers in the NI gas market. SSE is of the view that more can be done to significantly reduce the level of theft in the market to ensure it does not present as a barrier to market entry. Solutions for the UR to consider include: promotional campaigns informing customers about the illegality of interference with a meter and the associated safety issues; work with suppliers to understand the issues they face and the pass through of RP costs to all customers; and work with networks and suppliers to ensure that the network meter replacement plans and revenue protection processes are fit for purpose.
- Information availability. Brokers and comparison websites can help develop competition by providing customers with a one stop shop for information, however it is important that sites are monitored and controlled to ensure the information presented is correct and does not cause bias. The publication of advice for consumers may contribute to a higher level of knowledge and empowerment for customers. However, there is a large amount of information already available and we need to be careful not to overload customers 'for their benefit'.
- It is unclear whether more sophisticated meters can assist with the development of competition, this will come down to what information is available and whether suppliers can access data and offer products that allows them to differentiate without confusing customers.
- The geographical split in markets and networks within the NI gas market add an unnecessary layer of complexity for market entry and may contribute to higher levels of network costs being passed through to customers through duplication of systems and operations. SSE urges the UR to consider establishing a single gas retail market for NI to reduce the barriers to entry for new suppliers and encourage a higher level of competition by building a larger customer base for new entrants to access. In addition, SSE believes the UR needs to consider the return on investment needed for successful and sustained entry to the natural gas market in NI. The historical low margin allowed in the NI gas market has led to low levels of investment in customer services, system development and innovation in tariff offers for example dual fuel.

Q8. Feedback is sought as to whether or not there should be a period during which the energy retail markets are allowed to operate with no price controls, subject to enhanced monitoring. This consultation seeks views on whether there should be a period of deregulation or an immediate move to any of the options presented.

SSE Airtricity and other suppliers in the market require certainty. Without certainty suppliers cannot plan efficiently and this ultimately negatively affects customers. If the UR is serious about the possibility of removing price controls in markets, it should set out the criteria that must be met for price deregulation to take place in each market. These criteria should be set and when met, price regulation should be removed. The UR has clearly stated in the paper that the criteria set out for the non-domestic electricity market did not indicate the point at which the UR deemed that price regulation was no longer required but these represented the basis on which *further consultation* would take place. This does not provide certainty to market participants or customers. Without clear direction from the UR, the future of the market is unclear. When considering the criteria, SSE suggests that consideration is given to comments it has previously provided to the Utility Regulator in response to the Price Control Approach Consultation in December 2015.

CONCLUSION

In summary, welcomes the opportunity to comment the Utility Regulators consultation paper on the Review of Effectiveness of Competition Phase 2. We have raised a number of concerns in this response in relation to the issues in the Consultation paper. While the Options identified are analysed, SSE has highlighted a number of broader concerns with the URs consultation paper.

- SSE Airtricity fully supports the development of competition and any associated removal of regulatory barriers to facilitate growth in competition. SSE considers that more can be done to increase competition in the current market.
- SSE Airtricity has concerns about the comparison the paper makes with the findings of the CMA Review undertaken in Great Britain.
- SSE is unclear as to how the Utility Regulator can make a decision on the application of any of the options without knowing what these options are going to be addressing.
- Many of the options are akin to price regulation. The trend internationally is to remove price controls because of the recognition of the benefits of fully competitive markets.
- There appears to be a lack of recognition of the benefits that a fully competitive and price deregulated market can bring. SSE considers that the

first step of this exercise should be to identify the desired future direction for the retail markets and then identify methods to achieve this.

- SSE Airtricity is of the view that the Utility Regulator needs to consider how it can remove current structural barriers to greater competition that exist in the market. Such barriers include: small market size, energy theft, low profit margin regulated markets (impeding market entry), and fragmented market segments (three gas distribution areas).