

Regulatory Duties and Fairness in Retail Energy: perspectives from the regulatory community

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Context: markets and regulation

- Cross-subsidies from one set of consumers to another (discounts for fuel poor)
 - Reducing or removing tariff differentials (which may result in less switching, competition and higher prices for consumers)
 - ***Decisions by the regulator which has significant redistributive effects raise important questions of legitimacy, accountability and independence***
- Cross-subsidies:
 - e.g. Warm Home Discounts (BEIS responsibility, but administered by Ofgem)
 - Price-caps
 - e.g. PPM and Warm Homes Discount consumers (c.5m)
 - Interventions which are aimed to reduce tariff differentials, but reduce the benefits of switching/competition:
 - Non-discrimination clause (2009-12)
 - Simpler tariffs (2013-2016)

Overview

- The interviews
- Evolution of the regulator's statutory duties
 - The role of the consumer interest, including vulnerable consumers
- The problem of policies which have significant redistributive effects
 - Raise questions on legitimacy, accountability and independence
- How should a regulator decide on the appropriate limits of its powers

Research Overview

- ✦ Research draws on **document analysis, archival methods** and **elite interviews**.
- ✦ Interviews feature **13 elite participants** from:
 - ✦ **(i) Ofgem** (in addition to former members of Ofgas and Offer).
 - ✦ **(ii) Government departments** (**but no MPs, unfortunately ☹**).
 - ✦ **(iii) Other regulatory agencies**.
- ✦ **Interviews are anonymised** but our participants have been assigned 'descriptive indicators' which we intend to use for contextual purposes.

The interviewees

Our interviewees (descriptive indicators):

-  **Ofgem**, Partner
-  **Ofgem**, Head of team
-  **UK competition authority**, Panel member
-  **Independent**, Regulatory academic and policy participant
-  **UK competition authority**, Executive member
-  **Independent**, Senior advisor in telecoms regulation and consumer representation
-  **Ofgem**, Executive member
-   **Ofgem and Government department**, Senior member
-   **Academic commentator on energy issues**
-  **Ofgem Board**, Executive member
-  **UK energy regulator**, Senior member
-  **Ofgem Board**, Executive member
-  **UK energy regulator**, Senior member

*All indicators begin with 'Former or current' unless otherwise stated.

Statutory duties

The dawn of the general statutory duties

(Gas Act 1986, s.4)

Primary duties



Suppliers meet
demand



Supplier finance

Secondary duties



Protect consumers



Promote efficiency



Public safety



Competition
(Commercial premises)



Disabled



Pensionable age

Evolution of the regulator's general duties

Gas Act 1986

Electricity Act 1989

Competition and Service (Utilities) Act 1992

Gas Act 1995

Competition Act 1998

Utilities Act 2000

The Utilities Act 2000 (Commencement No. 4 and Transitional Provisions) Order 2000

Enterprise Act 2002

Sustainable Energy Act 2003

Communications Act 2003

Energy Act 2004

Consumers, Estate Agents and Redress Act 2007

The Legislative Reform (Health and Safety Executive) Order 2008

Counter-Terrorism Act 2008

Energy Act 2008

Energy Act 2010

Energy Act 2011

The Electricity and Gas (Internal Markets) Regulations 2011

The Electricity and Gas (Smart Meters Licensable Activity) Order 2012

Energy Act 2013

The Public Bodies (Abolition of the National Consumer Council and Transfer of the Office of Fair Trading's Functions in relation to Estate Agents etc) Order 2014

The Enterprise and Regulatory Reform Act 2013 (Competition) (Consequential, Transitional and Saving Provisions) Order 2014

The general statutory duties today

(Following Energy Act 2013 amendments)

Principal



Primary



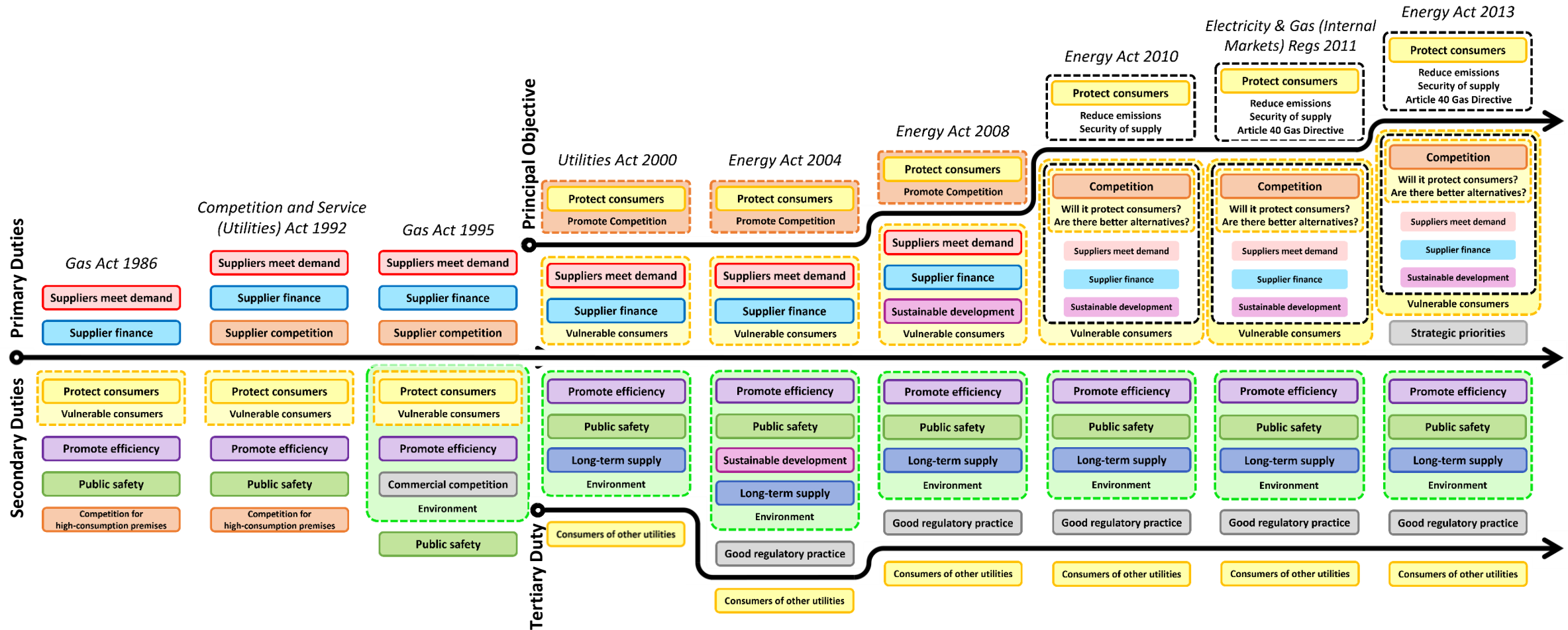
Secondary



Tertiary

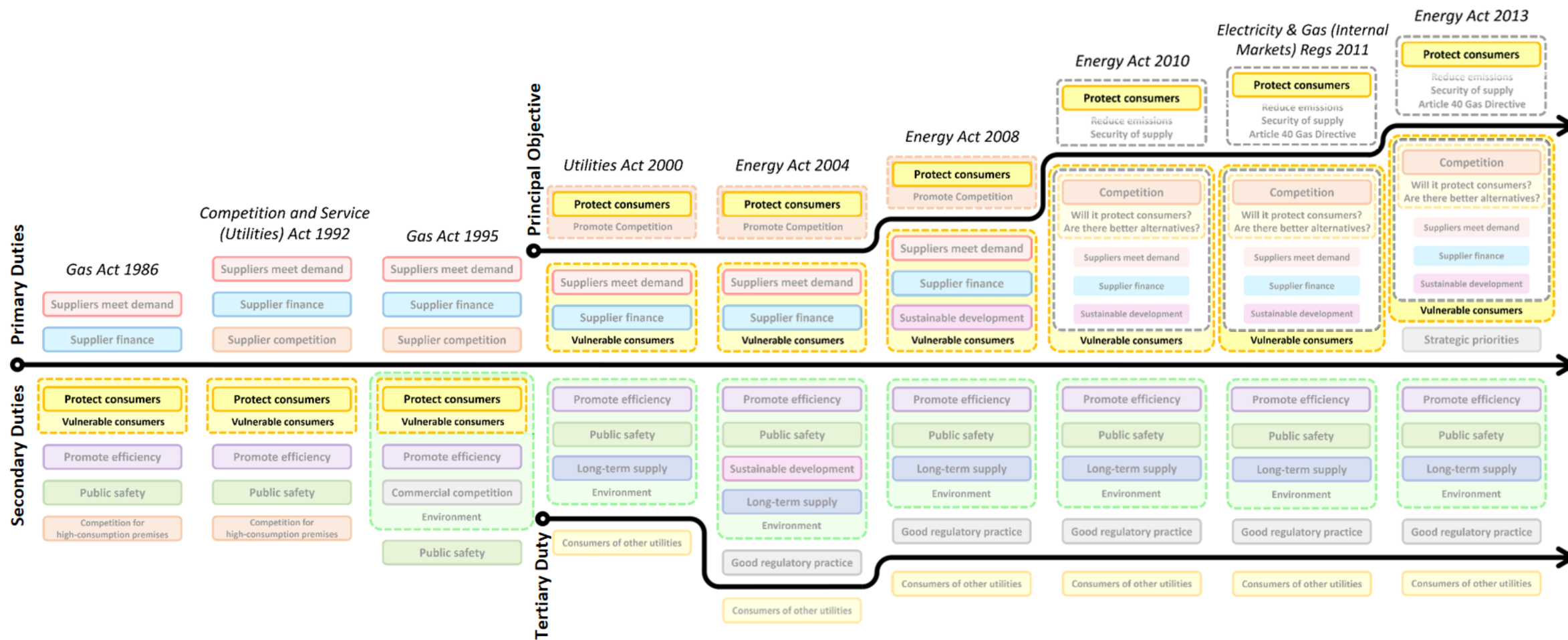


Evolution of the regulator's general duties



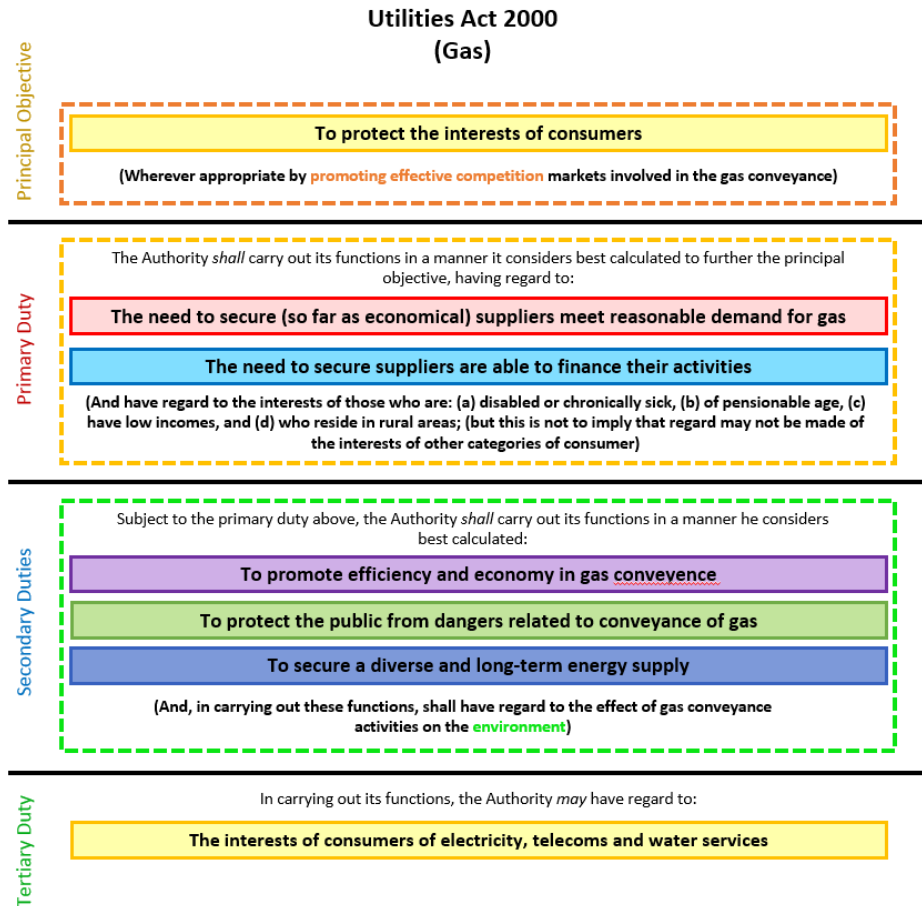
Evolution of the regulator's general duties

(Protecting the interests of consumers)



Evolution of the regulator's general duties

('Vulnerable' consumers)



Categories of consumers for regulator to have 'particular regard' to

Chronically Sick

Disabled

Pensionable Age

Low incomes

Reside in Rural Areas

The views of the regulators:
complexity, fairness and
distributional issues

House of Lords Committee on Regulators (2007)



HOUSE OF LORDS
Select Committee on Regulators
1st Report of Session 2006–07

UK Economic Regulators

Volume I: Report

Ordered to be printed 23 October 2007 and published 13 November 2007

Published by the Authority of the House of Lords
London: The Stationery Office Limited
£18.50 (inc VAT in UK)

HL Paper 189-I

We conclude that:

- ✦ *Independent regulators' statutory remits should be comprised of **limited, clearly set out duties** and that the **statutes should give a clear steer to the regulators** on how those duties should be prioritised*
- ✦ *Government should be **careful not to offload political policy** issues onto unelected regulator*

“The scope of regulators’ duties is more likely to be kept manageable if one recognises that matters of social equity and distributive justice are often best addressed, essentially by Government and Parliament, through other means such as the tax system.” [5.49]

How does the regulator interpret its duties?

General perceptions on the range of duties



Executive member
UK Energy Regulator

[L]ike a frog in a slowly warming pan of water; it doesn't realise it's going to boil.



Executive member
UK competition authority

So you end up with this bloody great Christmas tree of duties and regulations.



Executive member
Ofgem Board

[W]ith this smorgasbord, you could always point to something...



How the regulator interprets its duties?

Prioritising duties and dealing with trade-offs

Prevailing views

- ✦ Those who have worked within Ofgem say ‘the principal objective is at the heart of decision-making’: “[It’s] **absolutely front and centre all the time.**”
- ✦ Non-Ofgem regulators say: we have consumers in mind, but feel that competition is the best way to serve the consumer, so we proceed on that basis.
- ✦ Ofgem’s lawyers play a big role in ensuring decisions are consistent with the general duties.
- ✦ Ofgem’s documents on *Strategic Outcomes* and *Regulatory Stances* are intended to be its outcomes-driven interpretation/articulation of the duties; these help to guide decision-making and priorities.
- ✦ Creature of statute (**current regulators**) vs. Considering wider political context (**former regulators**).

Minority views

- ✦ Aside from the duties, the personal preferences of senior figures can have a huge impact on what approach the regulator prioritises.

BIS: Principles of Economic Regulation (2011)



Commitment 5

The Government will ensure that regulators' objectives are clear and appropriately prioritised (including through broader guidance) to reflect the issues that the regulators should take into account in their decisions.

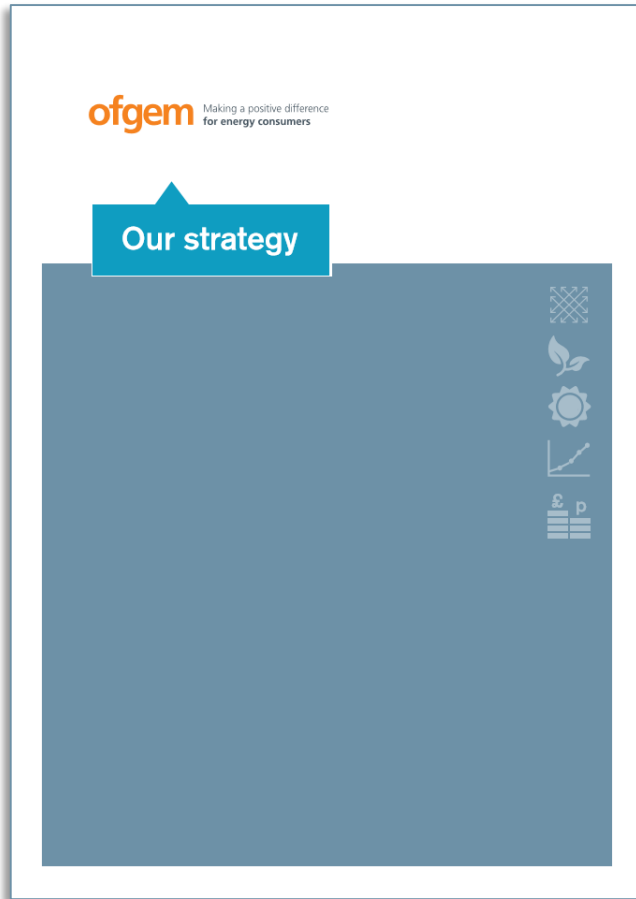
The Government will take opportunities to simplify and clarify regulators' objectives where appropriate as and when the frameworks are reviewed.

The Government will not seek to add objectives, responsibilities or duties to regulators' remits without detailed consideration of the impact of the addition on the overall framework, and consideration of cross-sector impacts and even then only when it is clear that the addition is the optimal way to achieve the outcome sought.

To achieve these objectives it is important to establish a clear division of responsibilities between the Government and economic regulators. Setting the policy direction and making politically sensitive trade-offs between objectives is likely to require democratic legitimacy and accountability and is clearly the role of Government. **Government should not avoid making these difficult policy decisions or pass them to regulators to determine.** [18]

How does the regulator interpret and enact its duties?

Prioritising duties and dealing with trade-offs



Strategic outcomes: interpretation of duties in terms of practical outcomes.

Parliament has enacted legislation requiring the government to set out its strategic priorities for energy policy through a Strategy and Policy Statement (SPS). We will have to ensure that our work has regard to these priorities... .

In doing this, we acknowledge that when we are considering how best to deliver our consumer outcomes in the context of the SPS, **we do not believe it is for us as an independent regulator to initiate or pursue a policy to achieve social or environmental outcomes which has the purpose of levying significant costs, or seeking significant redistribution of costs among consumers.** We believe it is important to provide clarity on where legitimacy and responsibility properly sit for any significant redistribution arising from interventions.

Implications for ‘fairness’ and ‘justice’ in energy markets

What do you perceive as Ofgem’s role in facilitating equity and justice in energy markets?

“I do think that we have limited powers for that wider question and our statutory duties give us limited remit to look into that wider question. We do consider issues of fairness in terms of protecting consumers, for instance, but I think the big issues of distribution are issues for government and, indeed, that is explicitly in our regulatory stances.”

“Well, I’m actually going to slightly disagree with the premise of the question, because it’s not really our job, as such, to facilitate equity and justice in energy markets. I think our job is to protect the interests of existing and future consumers. Now, equity and justice might be a decent-sized part of that but it’s not the whole of it...”

“Looking after vulnerable customers (be it energy or transport or anything else), no government can simply say, “I wash my hands of it. I’m going to leave it to a bunch of unelected regulators.” So you’ve got to kind of think conceptually: it’s perfectly reasonable for the government to be (as far as possible) hands-off in one area, and not exactly hands-on in another area but certainly to be very close to the regulator... talking to the regulator... influencing and being influenced by the regulator.”

Implications for ‘fairness’ and ‘justice’ in energy markets

What do you perceive as Ofgem’s role in facilitating equity and justice in energy markets?

“I will say that, in terms of that, in the last 5 years, I think that looking at issues such as fairness, we specifically use those terms at times – which, 10 years ago, a regulator like Ofgem would not have used. Whether that’s legitimate or not, I don’t know, but we have specifically thought more about the vulnerable consumers duty... and have invoked it more, I would say, in the last few years, than we did, say 15 or 20 years ago.”

“I mean, I think the problem with that is that I have grave misgivings about asking any regulator to do anything around fairness and justice, because I think there is a high degree of subjectivity in there about one person’s ‘fairness and justice’ isn’t another’s. And I have real concerns about an unelected independent regulator being asked to make judgements in that arena...”

“...I think that’s a matter for politicians. It just muddies the waters if you try to give those sorts of duties to the regulators.”

Conclusions

The statutory duties

- These have increased in complexity: there is a general consensus that there is 'undue' complexity.
- Virtue signalling and 'passing the buck' may be partly responsible for the 'creep' of new duties appearing on the list.
- But (via principles-based regulation) Ofgem has interpreted its duties in such a way as to give significant consideration to the interests of vulnerable consumers (beyond mere "regard to").

Fairness and distribution

- There is a general consensus that interventions with significant redistributive consequences should be for government
- Ofgem has attempted to put more emphasis on vulnerable consumers (public apology by CEO)
- The difficulty is knowing where to draw the line
 - what is 'significant'?
 - what level of harm (for vulnerable consumers) requires an intervention which may impose costs / 'harm' other consumers
- The concept of 'independent regulation' cannot be used to prevent government intervention?