



# Simplifying energy tariffs

Standard Note: SNSC-6440

Last updated: 1 February 2014

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Section: Science and Environment

After two years' work the energy regulator Ofgem has now finalised and has begun implementing its proposals on tariffs, under its 'retail market review'. Following a commitment at Prime Minister's Questions in October 2012 the Government is also legislating to provide powers on tariffs in the current *Energy Bill*. These powers are not strictly needed, given Ofgem's ability to set licence conditions, but the Government says they are 'backstop powers'.

Competition in the GB energy supply industry works best if customers find it easy to switch supplier, to better deals. The challenge is to strike a balance between getting simpler and cheaper tariffs for customers, while not actually setting final supply prices and stifling competition in the energy supply industry. Supply price controls were removed in the GB market following privatisation and the introduction of competition.

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## 1 Why does tariff complexity matter?

The Library standard note on [Help with Energy Bills](#)<sup>1</sup> outlines Government support for people with their energy bills and energy efficiency, but the main GB policy driver for keeping bills down is the promotion of competition in the energy supply industry.

For competition to work, people need to be willing to switch supplier, rather than, for instance, sticking with the former monopoly operator in their area, the successor to their regional electricity company.

The Energy Regulator Ofgem's primary duty under statute is to protect the interests of current and future consumers. It seeks to do this primarily through promoting competition in the energy market, along with regulation. Ofgem controls the costs of some contributing factors to domestic bills (such as transmission and distribution charges, basically the charges for transporting energy using the gas and electricity networks<sup>2</sup>) but it does not put a cap on final bills or 'supply' prices, preferring to encourage competition.

This is why Ofgem has supported switching campaigns such as the Citizens Advice [Energy Best Deal](#). Much government support to help people achieve lower energy bills also comes through encouraging switching campaigns. For example, in October 2011 the Government hosted an [energy 'summit' at Number 10](#)<sup>3</sup> with the Big 6 suppliers and Ofgem. One outcome of the meeting was Government support for a Check, Switch and Save to Insulate campaign. DECC and BIS are also promoting [collective purchasing and switching schemes](#).<sup>4</sup>

However, to switch, people need to be able to compare deals to those they are currently on. There has therefore been a long standing push by Ofgem towards clearer bills and tariffs, culminating at present through its retail market review (RMR).

Ofgem's [RMR draft impact assessment](#) estimated, after contacting suppliers, that:

".. the number of tariffs open for consumer to sign up to, as at 28 August 2012, around 900.

Due to the high number of tariffs, consumers are likely to encounter a large range of choices when looking for a new tariff. This is particularly an issue for those consumers unable or unwilling to use online comparison sites which can filter options.

Dead tariffs also contribute to tariff complexity. According to information provided by suppliers, there are over 650 dead tariffs".<sup>5</sup>

DECC says that of the "estimated 650 'dead tariffs', around a third could be poor value".<sup>6</sup> Consumer Focus and Which?, two other advocates of switching, and of simpler bills, have also done work on this. Which? told the Energy Bill committee that it had found people on over 1,440 tariffs.<sup>7</sup>

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<sup>1</sup> House of Commons Library, 13 December 2011 <http://www.parliament.uk/briefing-papers/SN06163>

<sup>2</sup> See for example [Ofgem's Household energy bills explained Factsheet](#) January 2013

<sup>3</sup> Number 10 press release 17 October 2011 Summit was with the six biggest power firms, consumer groups and regulator Ofgem <http://www.number10.gov.uk/news/pm-energy-summit/>

<sup>4</sup> BIS, [Guide for community buying groups](#) 8 February 2013 and DECC, [Community Energy](#) guidance and [Collective switching and purchasing](#) web pages

<sup>5</sup> Ofgem, 26 October 2012

<sup>6</sup> DECC "Turning non-switchers into savvy switchers" – Davey [press notice 17 May 2013](#)

<sup>7</sup> See Library research paper 13/10, [Energy Bill Committee Stage Report](#), 12 March 2013 p. 39

Consumer Focus (now Consumer Futures) has summarised the problem well:<sup>8</sup>

Suppliers offer different prices and different benefits for a homogenous product in order to attract new customers and retain their existing ones. There are hundreds of different tariffs available and the associated benefits are presented in a variety of different ways making direct comparisons difficult, time consuming or impossible. New product features such as termination fees, complex discounts and introductory or short term offers have led to many consumers feeling that they had been mis-sold as they didn't fully understand the implications of what they signed up to. Misselling of tariffs and unsolicited doorstep marketing over the years since liberalisation have also served to cement this distrust. Bills and annual statements are long, full of complex information and hard for many to understand, not least because many households don't have a clear understanding of how to translate their day to day use of gas and electricity into 'units' or kilowatt hours. It is, therefore, not surprising that many consumers are reluctant to engage with the energy market.

Even former Energy Minister Charles Hendry said that he found it too complicated to switch.<sup>9</sup>

## **2 Previous moves to tackle tariff complexity**

### **2.1 Ofgem's 'Probe' remedies; Annual Energy Statements**

An Ofgem [Energy Supply Probe](#)<sup>10</sup> published in October 2008 found a lack of transparency regarding tariffs and introductory offers and some unfair pricing arrangements. As a result, the unjustifiable differentials between different payment methods (e.g. for people on pre-payment meters versus those paying by direct debit) were reduced. Companies are only now allowed to charge 'justified' extra costs associated with different payment collection methods.

Ofgem can make such changes by changing the licence conditions under which companies operate, and has the ability to fine companies heavily (up to 10% of turnover) if they do not comply with their licence conditions. In other words, it can make quite detailed changes without the need for primary legislation.

Another Ofgem requirement was that Annual Energy Statements be sent to all customers. These are intended to show people what tariff they are on and how much energy they use annually, along with a reminder that they can switch. Knowing average consumption improves the accuracy of comparison sites. However, these statements have taken a variety of forms, and are often included on the back of bills, where they can go unnoticed.

### **2.2 Political commitments**

In September 2011 the then Secretary of State for Energy Chris Huhne [announced](#) greater powers for the regulator Ofgem, and that:

The Government and energy suppliers have agreed in principle to ensure consumers know if their supplier has cheaper tariffs. Suppliers have agreed in principle to signpost

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<sup>8</sup> Consumer Focus response to Ofgem retail market review, February 2012  
<http://www.consumerfocus.org.uk/files/2009/06/Consumer-Focus-response-to-Ofgem-Retail-Market-Review-February-resubmitted-version.pdf>

<sup>9</sup> [HC Deb 19 October 2011 c941](#) and [HC Deb 20 October 2011 c1047](#)

<sup>10</sup> The link in the text is to the Probe's home page for all documents, correct as of 18 October 2012;  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensupro/Pages/Energysupplyprobe.aspx>

consumers to cheaper deals information this winter, and we intend that by next year more bespoke information will be displayed on the bill itself.<sup>11</sup>

Early in 2012 Labour announced a policy of requiring energy companies to give their cheapest tariffs to over-75s.<sup>12</sup> During an Opposition Day debate in May 2012 on the cost of living, the Shadow Energy spokesperson Caroline Flint outlined Labour's plans. Replying, the Secretary of State for Energy Ed Davey said:<sup>13</sup>

Last month, my right hon. Friend the Deputy Prime Minister announced the deal that we secured working with the six big energy companies to give customers a guaranteed offer of the best tariff. From the autumn, suppliers will contact consumers annually to tell them which is the best tariff for their household, and if consumers call energy companies, they will have to offer them the best tariff.

### 2.3 The undertaking to legislate

During Prime Minister's Questions on 17 October 2012, the Prime Minister said:<sup>14</sup>

**Chris Williamson (Derby North) (Lab):** At the Prime Minister's energy summit last year, he promised faithfully that he would take action to help people reduce their energy bills. Will he tell the House and the country: how is it going?

**The Prime Minister:** We have encouraged people to switch, which is one of the best ways to get energy bills down. I can announce, which I am sure the hon. Gentleman will welcome, that we will be legislating so that energy companies have to give the lowest tariff to their customers—something that Labour did not do in 13 years, even though the Leader of the Labour party could have done it because he had the job.

As outlined above, the Government had already announced that energy companies had agreed in principle to let their customers know if 'cheaper deals' on tariffs were available.<sup>15</sup> The commitment to legislate was new.

In response to an Urgent Question on 18 October 2012, the Minister of State for Energy John Hayes confirmed that this new commitment "to help energy consumers to get the best deal" would be fulfilled through the then forthcoming *Energy Bill 2012*.<sup>16</sup>

As well as Ofgem's own powers as regulator, the Secretary of State is already able to modify the conditions of supply licences to ensure that a company gives domestic customers *information* about one or more of the company's lowest tariffs, under the *Energy Act 2011*. This may include savings to be made, where to find further information and how to switch.<sup>17</sup>

The PM's and Government's moves prompted speculation in the media that 'clumsy regulation' might adversely affect competition, and cause a 'levelling up' of prices.<sup>18</sup>

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<sup>11</sup> DECC press release 11/076 *More teeth for Ofgem, more rights for energy consumers* [http://www.decc.gov.uk/en/content/cms/news/pn11\\_076/pn11\\_076.aspx](http://www.decc.gov.uk/en/content/cms/news/pn11_076/pn11_076.aspx)

<sup>12</sup> Financial Times 10 January 2012, *Labour calls for over-75s to get best energy tariffs*

<sup>13</sup> [HC Deb 16 May 2012 c563](#)

<sup>14</sup> [HC Deb 17 October 2012 c316](#)

<sup>15</sup> See former Secretary of State for Energy Chris Huhne's [announcement](#) 20 September 2011, DECC press release 11/076, and [HC Deb 16 May 2012 c563](#), and below for more detail

<sup>16</sup> [HC Deb 18 October 2012 c487](#)

<sup>17</sup> See the House of Commons Library [Research Paper](#) on the Energy Bill 2011, pp44-45

<sup>18</sup> See for instance the *Guardian* 18 October 2012 "[Energy tariff plans under pressure](#)" *Telegraph* 18 October 2012 "[Energy policy 'shambles' as David Cameron and Ed Davey outline opposing plans](#)" *Financial Times* 21 November 2012 Energy Bill puts low rates in doubt p4

The Minister for Energy declined to confirm whether the intention was to legislate specifically to put all customers on the lowest tariff, and said this was a “complicated area”.<sup>19</sup>

### 3 Ofgem’s retail market review (RMR)

Behind the scenes, Ofgem was working to follow up its Probe findings through a consultation process which is still on-going. It published its final proposals on 21 June 2013, after what it termed “two years extensive research”.

Its 2011 *Retail Market Review (RMR) domestic proposals document* had initially proposed, among other measures such as ‘four core tariffs’, that Ofgem would set a standard standing charge so suppliers would compete on a single unit rate for each standard tariff.<sup>20</sup>

In this way suppliers would be able to change only the unit price, making comparisons easier.<sup>21</sup> In response, several of the ‘Big 6’ energy companies undertook voluntarily to reduce their numbers of tariffs.<sup>22</sup> But in October 2012, two days after the Prime Minister’s announcement on legislating, Ofgem issued a [press release](#) saying that the Big 6 initiatives did not go far enough, and announcing a further consultation. Consumer Focus thought that trying to present all suppliers’ tariffs in one comparison table was unrealistic.<sup>23</sup>

In its *Retail Market Review Updated domestic proposals document* of October 2012, Ofgem said the responses felt that a uniform national standing charge might “harm particular groups of customers”. It would prevent suppliers from reflecting their fixed costs in the standing charge and result in low or zero standing charge offers (which benefit low volume users) being removed. With the removal of the proposed fixed standing charge Ofgem felt it could no longer “deliver an at a glance comparison of tariffs across the market”, either.<sup>24</sup>

Ofgem proposed in October 2012 to:

- limit each supplier to ‘four core tariffs’ (in each of several categories, see section 5)
- have all tariffs expressed as a standing charge and single unit price, and
- have an “Easy-to-use Tariff Comparison Rate” (TCR).<sup>25</sup>

The ‘four core tariffs’ and the TCR remain essentially the final proposals, even though concern has been expressed about the usefulness of a TCR. The final [document](#) which went to statutory consultation in June 2013 acknowledged the difficulties:

Some concern was voiced in responses as to how effective the TCR would be as a comparison tool and whether it could be misleading for low use consumers. Some

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<sup>19</sup> [HC Deb 18 October 2012 c487](#) and c496

<sup>20</sup> Ofgem, 1 December 2011 *The retail market review: Domestic proposals* <http://www.ofgem.gov.uk/Markets/RetMkts/RMR/Documents1/RMR%20Domestic%20Consultation%20December%202011.pdf>

<sup>21</sup> Ofgem press notice 14 October 2011 *Radical reform for a simpler, more competitive energy market* <http://www.ofgem.gov.uk/Media/PressRel/Documents1/RMR%20Oct.pdf>

<sup>22</sup> See for instance <http://www.consumerfocus.org.uk/feature/simpler-tariffs>

<sup>23</sup> Consumer Focus response to Ofgem retail market review, February 2012 <http://www.consumerfocus.org.uk/files/2009/06/Consumer-Focus-response-to-Ofgem-Retail-Market-Review-February-resubmitted-version.pdf>

<sup>24</sup> <http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/The%20Retail%20Market%20Review%20-%20Updated%20domestic%20proposals.pdf>

<sup>25</sup> Ofgem press release 19 October 2012 *Ofgem publishes plans to deliver a simpler, clearer, and fairer energy market for consumers*

respondents advocated a “single unit price” with a zero or regulated standing charge, which we had consulted on previously. We remain of the view that the TCR is the best way of presenting the different elements of the tariff and associated discounts in a single figure to prompt consumers to engage and seek further information.<sup>26</sup>

### Box: Ofgem’s final proposals in full

- eradicating complex and confusing multi-tier tariffs
- creating easy to compare uniformity by making sure that all tariffs have a standing charge (which can be zero) and a unit rate
- aiding comparison between suppliers through the creation of a standard tariff information label
- limiting the number of different tariffs offered by a gas or electricity supplier to just four core tariffs **[but in various categories - see section 4.1 below]**
- making sure dual fuel discounts remain and are applied uniformly across all tariffs
- allowing suppliers to keep customers on tariffs that no longer exist (dead tariffs) only if they offer value for money; if not the customers should be transferred onto the cheapest variable deal.
- making sure suppliers tell customers key information about their energy tariff and use in an easy to understand way
- ensuring suppliers tell customers if there is a cheaper deal available
- making sure suppliers use a new Tariff Comparison Rate in all of their communications to help customers compare tariffs
- exploring a possible scheme whereby suppliers are obliged to offer their vulnerable customers and others who have not switched for some time, a personalised estimate on the cheapest tariff from across the energy market.
- making energy companies sign up to Standards of Conduct as a condition of their operating licence
- insisting on fairness in all of the different ways that energy companies engage with their customers, including making it easy for consumers to contact them and acting promptly to put right any mistakes
- banning price increases or other changes to fixed term tariffs (not including trackers or structured price increases that are set out in advance and are fully in line with consumer protection law)
- banning practices that automatically move customers onto fixed term contracts without their consent
- making sure that information provided to customers is not misleading and that it relates to products or services that are appropriate for the customer to whom it is directed.<sup>27</sup>

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<sup>26</sup> Ofgem, [The Retail Market Review – Statutory consultation on the RMR domestic proposals](#) 20 June 2013  
<sup>27</sup> <https://www.ofgem.gov.uk/retail-market-review> Ofgem RMR webpage as of 14 August 2013

Ofgem also set out when the provisions will be brought in:

### **1. August 2013 - Fairer treatment**

From 26 August 2013 suppliers are obliged to abide by our new standards of conduct to ensure suppliers treat you fairly and honestly.

This includes requirements such as:

- Suppliers and their reps must be honest, transparent and professional in all of their dealings with you.
- They must embed fair treatment of consumers at all levels of their organisation.
- They will have to be easily contactable, and act promptly and courteously to put things right.

### **2. October 2013 - Consumer protection rules**

From 23 October 2013 new rules have been in place, which, amongst other things:

- Provide better protections for consumers on fixed term contracts
- Ensure consumers are not on poor value 'dead tariffs'

### **3. December 2013 - Simpler choices**

From 31 December 2013 the number and complexity of tariffs will be reduced. This will make comparing tariffs easier and less time consuming. Once you have decided on meter type and how you want to pay, you will face no more than four different core tariff offers for electricity, and four for gas. Complex tiered tariffs will be banned, so all tariffs will be simpler. In addition, the discounts suppliers apply to energy tariffs will be simplified.

### **4. March 2014 - Clearer information**

From 31 March 2014 our new rules will ensure consumers are regularly provided with information about the cheapest tariff for them with their current supplier. They will also receive clear and helpful information about their current tariff and energy usage.

### **5. June 2014 – Migration of “dead tariff” consumers**

By 30 June 2014 any consumers who are on old, expensive, evergreen tariffs that are no longer open to new customers (so-called 'dead tariffs') will be switched to their supplier's cheapest variable rate. If the dead tariff is still cheaper than the standard tariff, you will not automatically be moved off it.

Suppliers will have to annually check after this to ensure any customers who remain on a dead tariff are not paying more than the supplier's cheapest variable rate. The first of these checks will have to happen by 30th June 2015.<sup>28</sup>

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<sup>28</sup> <https://www.ofgem.gov.uk/simpler-clearer-fairer/what-and-when> Ofgem RMR webpage as of 6 February 2014

## 4 The ‘backstop’ provisions in the Energy Act

DECC launched an [Ensuring a better deal for energy consumers](#) consultation after the announcement at PMQs.<sup>29</sup> The Government response in May 2013 said it would use the Energy Bill “to make sure [Ofgem’s] reforms are not delayed or frustrated”. Also, since Ofgem were committed to reviewing the RMR measures in 2017, the Government would keep its powers until 2018, and set a sunset clause accordingly.<sup>30</sup>

Since these provisions were not in the Bill as introduced to the Commons, they had to be added as Government amendments during Committee Stage. This is described in the Library Research Paper on the [Energy Bill Committee Stage report](#).<sup>31</sup> Bill received Royal Assent on 18 December.

As noted by several Members during the Bill’s passage, it is not clear how far these legal powers will be needed or used, because Ofgem, the regulator, already has the power to require energy companies to comply with licence conditions or face large fines.

There was also some discussion of the Government’s stated aim of requiring companies to offer people ‘the cheapest tariff’, which was clarified by Ministers during the Bill’s passage to mean ‘the cheapest tariff that meets their preferences’. The Bill as it stands allows for secondary legislation which would let the Secretary of State; require companies to offer particular types of tariff, to limit the number of tariffs, to offer certain information to consumers, and to move consumers off of poor value ‘dead tariffs’.

An Opposition amendment seeking to force all companies to tell customers once a year whether they were on the cheapest tariff available, and to move all customers aged 75 and over onto that tariff, was defeated in Committee.<sup>32</sup>

DECC says it is its ambition that “by summer 2014, all customers will have been placed on the cheapest price available from their supplier for the tariff type of their choice”.<sup>33</sup>

## 5 Specialist tariffs

### 5.1 Time of Use and dynamic teleswitching tariffs

‘Time of use’ (ToU) tariffs include those such as Economy 7 with fixed off-peak hours, and dynamic teleswitching (DTS), a type of ToU tariff where the price varies according to network conditions. Special meters are required.

An October 2012 Consumer Focus report [From Devotees to the Disengaged](#)<sup>34</sup> has shown that in theory ToU tariffs can save money if a home is well insulated and uses modern storage radiators for space heating by electricity. But in practice, not many ToU customers are aware of their off-peak hours, or use appliances at night, or have storage radiators.

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<sup>29</sup> DECC [Ensuring a better deal for energy consumers](#) Discussion document, 2012

<sup>30</sup> DECC [Ensuring a better deal for energy consumers](#) Government response to consultation on discussion document 20 May 2013

<sup>31</sup> House of Commons Library Research Paper13/19 [Energy Bill: Committee Stage Report](#) 12 March 2013 pp.38-42

<sup>32</sup> Ibid, p.42

<sup>33</sup> DECC [Ensuring a better deal for energy consumers](#) Government response to consultation on discussion document 20 May 2013 p.13

<sup>34</sup> Consumer Focus 10 October 2012 <http://www.consumerfocus.org.uk/files/2012/09/From-devotees-to-the-disengaged.pdf>

Another issue with ToU tariffs is that they are generally less easy – or at least perceived to be less easy - to switch away from.

However, Ofgem does not want to restrict the introduction of new ToU tariffs which are likely to become more common with the rollout of smart meters, and could have an important role to play in reducing or moving electricity demand.<sup>35</sup>

ToU tariffs are also likely to be used by fairly ‘engaged’ customers. Ofgem has proposed that there will be only four core ToU tariffs allowed, and will set up a working group to calculate a TCR for these complex and varying tariffs.

In all, then, there are now five categories under which the ‘four core tariff’ rule will apply, meaning that in effect companies will be offering many more than four tariffs:

- Category A – Tariffs with a single unit rate, single period of time.
- Category B – Other time of use (ToU) tariffs (not captured in the other categories).
- Category C – Tariffs with two unit rates, two periods of time.
- Category D – Tariffs with two or three unit rates, up to three periods of time.
- Category E – Dynamic teleswitching tariffs.<sup>36</sup>

## 5.2 Social tariffs

Social tariffs have been abolished and replaced by a scheme called the Warm Home Discount (WHD). This policy was started by the Labour Government and implemented by the current Government so it has cross-party support.

The old social tariffs were at energy companies’ discretion under a voluntary agreement, and were poorly targeted. The idea is that WHD is better targeted, and it is non-discretionary on energy companies’ part. WHD uses DWP benefits data to identify people on certain elements of pension credit within its ‘core group’ to receive WHD. Energy companies are still able to offer support under the WHD scheme to a less well-defined group of people forming part of a ‘broader group’.

Some people who were previously receiving a social tariff will no longer be receiving support, if they do not meet the eligibility criteria. Further information is available in the Library note on the [Warm Home Discount](#) including more background including criticism of both the old voluntary agreements of social tariffs, and of WHD itself.<sup>37</sup>

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<sup>35</sup> Ofgem *The Retail Market Review: Domestic Proposals* 1 December 2011 p.2

<sup>36</sup> Ofgem, *The Retail Market Review – Statutory consultation on the RMR domestic proposals* 20 June 2013

<sup>37</sup> House of Commons Library <http://www.parliament.uk/briefing-papers/SN05956>