

Scottish Parliament Committee: Scottish Publicly Owned Energy Company

Consultation response from the
Centre for Competition Policy

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This consultation response has been drafted by the named academic member of the Centre, who retains responsibility for its content.

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ECONOMY, JOBS AND FAIR WORK COMMITTEE BUSINESS SUPPORT INQUIRY

SUBMISSION FROM Catherine Waddams, Centre for Competition Policy, University of East Anglia

Scottish Publicly Owned Energy Company (POEC)

- **What are your general views on the idea of a Scottish publicly owned energy company (POEC)?**

A Scottish POEC could achieve a number of interesting objectives, but there may be better instruments for achieving each of these different objectives in the energy sector. In particular, as other questions indicate, there is a danger that conflicting and/or poorly defined objectives result in poor achievement of any of them. A Scottish POEC clearly could pursue a number of different objectives, but this makes it doubly important, as the Institute of Public Policy Institute (IPPI) Scoping Note emphasises, that the objectives are clearly defined, both in terms of principles and expected outcomes.

- **What role should it fulfil and how?**

The role to be fulfilled by a Scottish POEC should be determined by elected representatives. The Scoping Note makes clear the possibilities. There is no reason why a POEC would have significantly lower costs than a privately owned company, and the low profit margins, particularly in electricity, indicate that there is little scope for much lower prices without breaching state aid rules.

One obvious role for a POEC might be a policy of charging similar prices to 'new' and 'loyal' consumers, i.e. removing the price discrimination which is currently observed in the sector, though initially all its consumers would be new. However if other companies are offering lower prices to attract new customers, this will affect the ability of the POEC to attract consumers without similarly low prices. Given the small, or even negative, margins on these consumers, it may be necessary to raise prices to those who show some loyalty to achieve break even in the longer term. The ability to do so will be somewhat constrained by Ofgem's price cap on default tariffs.

More exploration of alternative business models within the sector, for example with the companies mentioned in the scoping project, but also with longer established companies which have attempted such undifferentiated pricing policies, like Ebico, could help to explore the possibilities.

The tension for any new start up in this market is that while research shows that price savings are the strongest driver in consumers' intentions¹ to switch and in

¹ Empirical Evidence of Consumer Response in Regulated Markets (C. Waddams Price and M. Zhu), Journal of Competition Law and Economics, 12, 1, pp 113-149, 2016.

their actions², there is still a high degree of inertia: savings are necessary but not sufficient to persuade most consumers to switch. While some consumers may have a preference for a Publicly Owned company, there would probably be insufficient active switchers to generate a large consumer base for the POEC.

Moreover experience and evidence suggests that private commercial firms are more effective at communicating with their consumers than their public counterparts (for example in knowledge of privately run price comparison websites rather than official public equivalents). While the private sector may be trusted less, it has a better track record of communicating with consumers.

- **What are the key challenges that the POEC should address?**

The key high level challenge will be for the POEC to have clear objectives and success measures. Attracting consumers will also be a challenge if the POEC is to meet multiple objectives while still breaking even, see comment above.

- **How might a Scottish energy supply company work best to support the growth of local and community projects, and fuel poverty reduction?**

My main comment is on reducing fuel poverty. Our own research confirms historically higher levels of fuel poverty in Scotland than the average in the rest of the UK. Since there is likely to be little profit to redistribute, one way in which the POEC could reduce fuel poverty is to give special assistance to consumers at risk of fuel poverty to switch to cheaper deals, but this will be limited in the market by restrictions imposed by State Aid rules.

The POEC, like other companies, can help consumers with reducing the quantity of energy they use through energy conservation measures, and, like Robin Hood Energy, could voluntarily participate in the Warm Home discount and other schemes. But this will have financial costs for the company.

There is some evidence that those at risk of fuel poverty are more likely to be on more expensive tariffs, so a significant reduction in fuel poverty might be available if such consumers moved to tariffs with lower prices. But there will be limits on how far the POEC itself can stimulate such change, and there might be other more effective instruments which the Scottish government could use to achieve lower prices for groups at risk. One of these is collective auctions, where a group of consumers are offered a better deal. Experience of these is mixed³, and under current legislation consumers are required to opt in, which poses many of the same challenges of inertia for certain consumers as direct switching. The Scottish government might want to explore the potential of opt

² (D.Deller, M. Giuliotti, G. Loomes, C. Waddams Price, A. Moniche and J.Y.Jeon), CCP working paper 17-5, <http://competitionpolicy.ac.uk/documents/8158338/17199160/CCP+WP+17-5+complete.pdf/fdaaed88-56e5-44f9-98db-6cf161bfb0d4>; Consumer behaviours in the British retail electricity market (M.Flores and C. Waddams Price), The Energy Journal, 39, 4, 153-179, 2018

³ Helping customers switch: collective switching and beyond, published by DECC 2013 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/253862/Helping_Customers_Switch_Collective_Switching_and_Beyond_final_2_.pdf

out collective switching as an instrument to offer lower prices to consumers who are not currently active in the market⁴.

One problem for designing and monitoring such initiatives is that those inactive consumers who may be most at need are often hard to reach because of their circumstances. This often makes it difficult to identify their needs and appropriate remedies, and raises the cost of policy development and research which has the potential to benefit this group.

- **How can the POEC be best designed to align with wider Scottish energy policy objectives, and to avoid potential policy conflicts?**

As suggested above, it may be clearer if different objectives are delivered by different bodies and instruments, rather than expecting the POEC to meet several objectives which may be in conflict.

- **How might the POEC be designed to promote objectives and functions beyond the retail of gas and electricity (e.g. supporting investment and innovation in new technologies and infrastructure)? What benefits are there to having wider objectives?**

There are dangers as well as benefits in expecting the POEC to meet wider objectives. One is that it may carry so many potentially conflicting expectations that it will inevitably disappoint at least some of its supporters, who then lobby for changes which are incompatible with its other objectives. Given the importance of the issues, particularly to low income households and those in vulnerable situations, it is important not to 'set it up for failure'.

- **What governance arrangements should a Scottish POEC have? Who should it be accountable to e.g. Parliament?**

The POEC should be accountable to Parliament (rather than government) if it is meeting Parliamentary objectives.

- **Should legislation be required to underpin the creation of a POEC?**

A statutory basis might be the best way of making its objectives and priorities clear, though this is not always easy for politicians to clarify.

⁴ for information on experience of an opt-in auction see and possibilities of opt-out auctions see [Switching Energy Suppliers: It's Not All About the Money](#); and [Collective Switching and Possible Uses of a Disengaged Consumer Database](#) (D. Deller, P. Bernal, M. Hviid and C. Waddams Price), Report for Ofgem, 2017

