

**Addressing undue discrimination: final proposals:
Response to Ofgem's consultation from Catherine Waddams¹
Centre for Competition Policy, University of East Anglia**

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Ofgem's proposal to introduce an undue discrimination clause, particularly relating to prices charged in different geographical areas, is likely to stifle competition in the retail energy market for reasons which I have outlined in previous responses to Ofgem on such proposals (December 2008 and February 2009). The detailed proposals for license changes do not address adequately the concerns which I described there, and raise some new worries. This brief response focuses first on the main proposal, and secondly on the exceptions which are designed to ameliorate undesired effects.

The impact assessment recognises potential dangers to competition, but continues to underestimate them. Even in the short term, it is unlikely that any consumers will benefit from these measures. All former electricity incumbents will soften the offers which they make in areas where they are 'entrants', and, as incumbents, they will know that their main competitors are doing the same. While the differentials in prices will disappear (apart from those which reflect regional cost differences), the removal of competitive pressure is likely to maintain prices at a higher level than they would otherwise have reached, with detrimental effects on all consumers, including those defined as vulnerable, in both the short and long term. It could be argued that the outcome will be 'fair' in the sense that those who have and have not switched supplier will be supplied at similar prices. But others might argue that it is unfair that those who have gone to the trouble of switching in the past, motivated by an expectation of paying lower prices, will have this benefit arbitrarily removed. Moreover these 'equalised' prices will be higher than they would otherwise have been for all consumers, and there will be long term detrimental impacts on the market, which will make it much less competitive when these temporary measures expire.

To address such concerns, Ofgem propose allowing companies to compete to gain consumers by offering temporary discounts, so long as it is made clear to consumers that these are temporary, and will be removed after a limited time. This will have one of two effects. Either it will prove very effective, and reintroduce the very differences which Ofgem is seeking to remove (but only for consumers who switch after the new license conditions). Or, more worryingly, it may make things worse, by realising the anticompetitive effects outlined above, while hindering consumers in making good decisions. There is increasing evidence that consumers often fail to act in their own best interests when comparing present and future prices, so that they allow a temporary current discount to 'over influence' their decisions². This is likely to be particularly problematic for just those vulnerable consumers whom Ofgem is seeking to protect, and so exacerbate the problems in consumer choice which Ofgem has identified so well. There is a real danger that the regulator will succeed in achieving the worst of both worlds, with the undue discrimination ruling softening competition, while the exception for temporary discounts leads consumers, particularly those for whom the regulator has a statutory responsibility, to make poor decisions.

¹ CCP, UEA, Norwich NR4 7TJ; 01603 593715; c.waddams@uea.ac.uk

² See, for example, Assessing the Effectiveness of Potential Remedies in Consumer Markets, a report for the Office of Fair Trading http://www.offt.gov.uk/shared_offt/economic_research/oft994.pdf