The European Union of the Natural Gas Industry

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ERGEG DRAFT GUIDELINES OF GOOD PRACTICE ON INDICATORS FOR RETAIL MARKET MONITORING

Response on behalf of
Eurogas's Supply & Market Development Committee

Introduction

Further to the ERGEG consultation dated 16th April on retail market indicators, Eurogas is pleased to contribute this response on behalf of the Supply & Markets Development Committee of Eurogas.

Eurogas accepts the importance following full market opening in July 2007 of national regulators monitoring the development of their retail energy markets. We also agree that there is value in sharing experience of the use of market indicators by national regulators and others, although we are less convinced of the need for or value of EU best practice guidelines in this area.

In general, Eurogas believes the approach to market indicators should be pragmatic, focused and proportionate and they should not lead to bureaucratically heavy or expensive reporting obligations for companies - their cost is very likely to feed through into the prices paid by customers.

Before turning to the specific questions in the GGP on retail market monitoring, we believe it is essential to be clear about:

- The objectives of market indicators
- How these objectives can be best achieved
- The validity of comparisons between Member States
- The publication of market indicators (noting that unambiguous data collection methodologies and audits would be necessary)

This note begins by offering our views on each of these aspects (section A). We then consider the specific questions asked in the consultation (section B).

Finally we give more detailed comments on the individual indicators proposed (section C).

Section A - The role of retail market monitoring

1. The objectives of market indicators

Eurogas sees the purpose of the current work by ERGEG to develop market indicators as being twofold:

- to assist in building up a picture of the development of retail markets across Member States
- to provide an indication of where there are concerns about the functioning of the competitive market, either structural or operational.

Retail market indicators should not be seen as a substitute for retail market reviews, which many national regulators periodically undertake to highlight barriers to competition or aspects of the consumer experience which should be addressed.

2. How these two objectives can be best achieved

In our view, the first objective can be met by reports by regulators reviewing among other things the number of suppliers, market concentration and the effectiveness of the switching process in their Member State. This simple 'checklist' should be complemented by the work done by the Consumer Market Scoreboard. The scoreboard is also at a high-level, with a view to allowing the energy consumers' experience to be compared with that in other sectors.

The majority of the indicators being considered by ERGEG really focus on the second objective – to provide an indication of where there are problems with the functioning of the competitive market, either structural or operational. We believe that such information should be seen as helping to direct NRA attention if one or more national indicators suggest there may be grounds for concern. From time to time the indicators may point to a more general problem, which can be followed by in-depth analysis by the regulator concerned.

Eurogas agrees with ERGEG when it says (on page 18 of the consultation) that complaints data, for example, must not be considered in isolation. Any assessment of retail market functioning has to be based on a wide number of factors which contribute to the overall picture.

3. The validity of comparisons between Member States

It is not necessary or useful for this second purpose that indicators are compared at an EU-level. National markets and the priorities for market development and improvement vary. There are also evident differences between Member States affecting the comparability of data across Member States – for example varying market sizes, structures and demand aspects (all of which can affect market entry economics), and national characteristics (e.g. regulated versus market prices, different levels of public service obligations).

Simply comparing quantitative results will not lead to a fair assessment of the functioning of the market in a given Member State or the state of competition there. For example, the failure of an interconnector or other supply problems may have an impact on end-users, but a rise in complaints prompted by such a failure says nothing about the functioning of the retail market. While trends in complaint levels are an indicator of how well a national market is functioning, they should not be seen in isolation or without proper context.

Similarly, while indicators such as the effectiveness of switching can be gathered by a Member State, indicators in this area have to be related to wider considerations affecting each market.

We would therefore caution strongly against seeing indicators as the basis for comparisons between Member States. This is likely to lead to wrong conclusions being drawn and inappropriate actions being taken, as well as resulting in higher costs for customers.

In the view of Eurogas, the value of market indicators lies not in comparisons with other Member States but in enabling the NRA to identify trends within a Member State. We are extremely concerned by the value attached to comparisons between Member States and the importance of collecting information in a consistent format (see page 9 of the ERGEG consultation). In our view, there is a great risk of the goal becoming the establishment of a standard data collection process in the EU (which would be heavy, costly and not necessarily more accurate), rather than focusing on means by which individual national markets may be improved.

4. Publication of market indicators

Eurogas recognises that NRAs or third parties within a Member State may wish to publish information on supplier performance. However we would be concerned if regulators or third parties published information which identified individual companies, until the reliability and comparability of such data have first been verified. Unambiguous data collection methodologies and audits would be necessary.

We would point out that publication of company-specific information is not necessary to show whether the market as a whole is working for consumers. In addition, while publication of data on individual companies may result in efforts to improve performance, there is also the possibility it could encourage companies to manipulate their statistics; this could actually make it more difficult to have confidence in the usefulness of the data or mean that more onerous auditing is required.

Section B – ERGEG questions

1. Any indicators which should be left out of the final recommendations

The number of indicators is of concern if, encouraged by these guidelines, NRAs were to set up extensive and detailed statistical monitoring systems, with which suppliers would then have to comply. In some Member States this would mean suppliers having to develop new IT systems and processes; in general existing systems are likely to have to be upgraded.

Eurogas would highlight the indicator 2 on complaints as especially problematic – we remain concerned about the definition of a complaint (how to distinguish it from a simple enquiry, how to classify unambiguously in one of 14 categories), the cost of data collection and the value of this particular indicator.

More generally, the cost and administrative burden of any obligation of this kind has to be considered against the likely benefits for customers. Eurogas therefore believes that every effort should be made to derive indicators from existing data sources and information systems, rather than requiring new monitoring systems. Since in our view there is little or no benefit from statistics being harmonised at EU level, it should be readily possible for a Member State to use existing sources and to omit those indicators proposed by ERGEG where it proves impossible to obtain sensible, reliable or conclusive figures.

We would draw ERGEG's attention to Section C of this response, which sets out a number of concerns related to the introduction of particular indicators, at least in some Member States.

2. Any indicators which are insightful which are not present

Eurogas sees no point in extending this already long list. If an NRA sees a need for additional information, there is no reason why this cannot be introduced at MS level. ERGEG members will be interested to share experience of the usefulness of such additional data and the data can be subsequently requested by one or more other NRAs who find it to be valuable.

3. Any indicators which should be measured differently

We believe that for the most part, indicators should be measured in a way which best suits national circumstances and industry structures. Thus we do not feel the exact way in which indicators are developed has to be prescribed at an EU level. Attempts to standardise across Europe are misguided and if pursued will result ultimately in customers bearing unnecessary costs.

In section C, we comment in detail on the derivation and value of individual indicators – we would highlight here our comments on end-user prices and retail margin (indicators 4 & 5).

4. In the light of national circumstances, whether the suggested frequencies for collection are appropriate and feasible

Particularly where markets are already functioning reasonably well, Eurogas believes that there is unlikely to be value in collecting indicator data more often than annually.

5. Any indicators for which the results should be published in an un-aggregated form, thus naming the individual energy company

As noted above, Eurogas does not believe that publication of company-specific information is necessary to show whether the market as a whole is working for consumers. We recognise that NRAs or third parties within a Member State may wish to publish information on individual performance, which might include naming suppliers. However while publication of data on individual companies may result in efforts by suppliers to improve performance, naming suppliers could encourage companies to manipulate their statistics. This could actually make it more difficult to have confidence in the usefulness of the data or mean that more onerous auditing is required.

We would be concerned if regulators or third parties published information which identified individual companies, until the reliability and comparability of such data have first been verified. Unambiguous data collection methodologies and audits would be necessary.

Section C – Textual comments

Customer satisfaction

Indicators 1 – 3 Customer complaints, enquiries & requests for information

This is a major area. Our main concern relates to the difficulty of classification. For example, customer contacts related to the complexity of the bill the customer has received – is this a complaint or an enquiry? What if there is an enquiry related to the price comparison website operated by the regulator?

Where customer complaint figures are already being provided to the NRA or other authorities, the classification, logging and monitoring criteria must be aligned to national practice and to move with changes to that practice. A prescriptive approach here will cause unnecessary changes to present arrangements at MS level and could constrain what is done at national level.

In general, as regards both customer enquiries and complaints, we are not sure how accurate these statistics will be, given the numerous channels and reasons for customer contact. The risk of double counting is high and categorisation of telephone contacts (e.g. request for information or complaint) will be especially subjective. In this connection, we would also note the high cost of recording telephone calls and the practical difficulty of relying on this as a source of monitoring data.

Ad hoc national surveys around specifically identified difficulties can be carried out at lower cost and greater efficiency than developing a large and permanent statistical system, which is liable to obsolescence in an evolving environment and may in practice produce less accurate results.

Retail market outcomes

Indicator 4 End user prices

We are concerned that this indicator may not be clearly understandable and suggest further consideration is given to it.

Even within a Member State there can be significant differences in the way in which gas is used e.g. the proportion of gas used for heating purposes. For indicators to be effective the rules would have to be clear (e.g. the rules for what is a typical household). The rules would have to specify if deemed or default contracts should be included, and to take account of markets where there are regulated and free-market tariff systems. Also there are various options that can influence price, in particular dual fuel and prepayment.

These considerations are even more significant if EU-wide comparisons are to be contemplated. Eurostat (on behalf of the European Institutions) already publishes information in this area and in some Member States, price information is already collected in connection with price comparison websites, so it is important that data collection is not duplicated or conflicting information produced.

EU-level comparisons are also complicated by the existence of taxes and levies in many Member States, which significantly affect results.

We therefore see problems in establishing another 'ex post' indicator, particularly because of the many different types of contract and contract variables that would have to be taken into account and the risk of conflict with existing published data.

Indicators 5 & 6 Retail margin & price spread

We agree with ERGEG's warning that such calculations may be 'highly theoretical'. Assuming that the indicator does not require suppliers to provide commercially sensitive data, it would have to be derived from consideration of wholesale prices, which requires decisions to be made on which wholesale price information is an appropriate basis. It also assumes a simplistic relationship between wholesale and retail prices, without considering hedging strategies.

A further complication in determining margins arises when retail prices are linked to an index.

Even assuming these concerns can be addressed, assessment of retail margin information is not straightforward - the existence of high margins will tend to encourage market entry and in regulated markets, negative margins may be recorded. Low margins can be the consequence of both high and limited competition, and vice versa.

Price spreads typically narrow after market opening, at least in the more competitive sectors of a market. However in a fully competitive market, inappropriate use of indicators based on price spreads could produce a market response where products are designed narrowly, reducing customer choice.

Given all these considerations, we find the margin indicator particularly problematic in view of its analytical difficulties, the omission of relevant exogenous factors and its uncertain link with the level of competition. It is evident that any results would have to be interpreted with great care, and that at the very least the indicator would need to be presented with detailed methodological notes to guide interpretation.

ERGEG should review its proposals in regard to this area, ensuring that its approach is proportionate and pragmatic. It should in any case not oblige suppliers to unveil commercially sensitive information.

Indicator 7 Diversity of contracts (offers)

This is not only related to the number of suppliers and size of Member State. In general, competitive markets tend to produce simple offers that can be clearly communicated. In that sense, it is unclear whether high or low diversity is preferable. We therefore agree with ERGEG that the regulator will have to consider results intelligently.

Information in this area should be readily available without further requests to suppliers.

Indicator 8 Regulated end-user prices

In considering this indictor, regulators should also take account of indirect price regulation, such as wholesale price regulation or cases where the regulator influences product design (such as social tariffs) or when the Regulator has to approve a new product before it can enter the market).

Market structure

Indicator 9 Number of suppliers

Although trend data in this area is useful, we agree with ERGEG that simply monitoring the number of suppliers nationally is not by itself a meaningful indicator of the strength of competition. Such information has to be assessed alongside other information.

As an example, market structures in Member States are very different and not all suppliers are active nationally. What is important therefore is not the number of suppliers nationally, but the choice which customers locally have when considering a change of supplier. A Member State could also give consideration to the number of customers per active supplier.

Indicator 10 Market concentration

It must firstly be recognised that HHI and CR are theoretical indices reflecting an 'ideal market', the scope of which would have to be determined in accordance with competition analysis.

If consumption is to be used in calculating indices, the consumption bandings need to be clear. There are Europe-wide consumption bands already defined and used in Eurostat price statistics. However most MS do not use these definitions internally (for example in Great Britain, 0 to 73,200kWh, 73,200kWh to 200,000kWhs, 200,000kWh to 732,000kWhs and >732,000kWhs are used). It should therefore be expected that different bandings will be used, negating the possibility of EU-wide comparisons.

Market condition

Indicator 11 Branding

The quantitative indicators proposed refer to 'separate branding' which seems to us as possibly a more onerous requirement than the 3rd Package reference to 'separate identity'. If the quantified indicators continue to refer to separate branding, this could give a very superficial and misleading picture. We believe that any indicators in this area should follow the wording of the 3rd Package.

We note that the indicators seem to be less about routine monitoring and more about analysis of the retail market, within which branding practices may be a factor in causing customer confusion and/or low switching. We agree with ERGEG's caution to NRAs that results should be considered alongside other indicators of competition and consumer welfare – the overarching aim is to determine whether a market is working.

Identity and confusion are not easily quantified. We therefore support the need for further investigations perhaps through questionnaires or focus groups into this area. It would be interesting to explore for example if there is any correlation between branding practices and higher/lower switching rates (see below).

Indicator 12 Switching rates

We acknowledge the value of this indicator. However in interpreting the results from this indicator, it should be recalled that a high rate may result from newly opened markets where there are no switching process problems and high price spreads. High switching rates may also be more likely in countries where the share of gas cost in the typical household budget is high; in warmer countries, the value of any saving will be less and switching rates likely to be lower.

We would also note the difficulty of distinguishing switching and house-moves when these occur at the same time.

Indicator 13 Renegotiations (household)

The circumstances around renegotiations need to be taken into account. Particularly in mature markets, 'renegotiations' can actually be seen as another reflection of 'product choice' – i.e. switching between products as well as between companies. The important point is then that the customer has actually engaged with the market – they have chosen the product they are on and are engaged just as much as a customer who prefers a fixed price product but switches between companies on this type of product every year.

In practice this indicator will be particularly hard to track and may be of limited value.

Indicators 14 and 15 lack clarity in terms of what a 'delayed switch' means. What if the customer requests a re-arranged supply start date? We assume that 'cooling off' periods designed to protect consumers for certain types of contract are not included in the three weeks mentioned, since they do not indicate market failure.

DSO services

Indicator 16 & 18 Connections & disconnections

DSO service levels in this area are relevant to the customer experience but do not reflect the activities of retailers or the effectiveness of competition. If they are to be retained, it should be recognised that they are very different from the other indicators mentioned.

We accept that the response time is an indicator of DSO effectiveness. However it must be borne in mind that the actual time for physical connection may be linked to local factors such as the condition of the terrain, so monitoring the overall time till completion may not be appropriate.

While we accept that the number of disconnections should be monitored, it should be recognised that this may not be related to the operation of the competitive energy market, as it arises from the customer's payment behaviour and economic circumstances, and may also depend on some regulations or safety requirements.

Indicators 17 and 19 refer to maintenance and repair but do not say of what. Does this refer to problems associated with the network or could it include metering systems (operation of prepayment services introduces problems not encountered by Member States where such meters are not used)? Could it even include appliances?