



1. Communication

with the public

SUMMARY

Better communication with the public is needed on costs of making the transition to a low-carbon economy

Whatever the path the electricity sector takes and the role it plays in decarbonising the economy to 2030, there will be significant costs in terms of new investment. All participants believe there needs to be a much more honest communication with the public about these costs going forward. Despite the attention focused on new infrastructure in other sectors, like transport, energy remains by far the largest element of the requirements in the National Infrastructure Plan. Some believe the conclusions of the CMA report provide an opportunity to do this.

Many respondents argued that the impact of policies on bills needed to be more clearly explained to customers. Whether the impact is due to supply-side measures (e.g. incentives for low-carbon generation or capacity payments) or demand-side measures (e.g. energy efficiency schemes or balancing services), more needed to be done to engage with consumers and explain how these policies translate to energy bills.

There was some support for the introduction of an independent body to assess the costs of different pathways. Many respondents believed there needed to be more transparency regarding the assumptions and calculations behind DECC's forecasts and impact assessments for the LCF, as well as how this budget is allocated between different mechanisms. Whatever mechanism is chosen, the clear message from the industry is that there needs to be an open and honest debate with the public about the costs of moving to a low-carbon economy.

1.1 Interview responses

Overall, more than 50% of respondents mentioned, unprompted, the importance of open and honest communication with the public from Government and suppliers. Interviewees provided comments such as:

“More honesty is required with consumers about what they are paying and where it is going.”

“There needs to be an honest debate with everyone involved.”

“The Government needs to acknowledge meeting our energy challenge will inevitably increase costs.”

“A key factor in affordability is open and honest conversation with consumers, and investors are focused on this issue.”

“Government should assume responsibility and be honest in communicating the breakdown of energy bill.”

Many interviewees emphasised the importance of putting consumers at the heart of policy-making. This includes engaging closely with consumers regarding the cost of meeting energy sector challenges, the impact of levy-funded spending and how bills are projected to evolve as a result of Government policies. While consumers include both residential and commercial and industrial (C&I) customers, more emphasis is placed on the residential consumer as they can often be less informed but face greater impacts relative to C&I consumers.

Some interviewees believed there should be a shift from levy-funded spending in the energy sector towards general taxation, whilst others thought levies remained appropriate. In general, however, there was agreement that consumers did not have a clear picture of the impact of levies on bills and of the magnitude of this compared with other levy-funded and general taxation spend as a whole.

Some respondents welcomed the CMA's provisional findings following its energy market inquiry, commenting that there was now an opportunity to 'draw a line' under the debate around the market structure of energy companies. Some respondents however noted the significant challenge for regulators and judicial bodies in assessing company returns and market health and noted some inconsistencies between CMA findings and over market data.

There was some support for the establishment of an independent body to assess the cost of different market structures and policy solutions in view of the consumer, although some respondents thought this would not be productive as there was already confusion regarding the roles and responsibilities of bodies such as Ofgem, DECC and National Grid, and some argued this function ought to be fulfilled by DECC. Overall, however, almost all respondents believed greater transparency regarding Government policies and projections was required across the market.

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1.2 Analysis

1.2.1 Profitability and customer bills

Several interviewees commented there was a ‘disconnect’ between consumers and the drivers of consumer bills. They noted the media has paid significant attention to forecasts of company profits but it has not been communicated to customers that increases in bills may be driven by factors outside the control of suppliers, such as commodity prices, network costs and Government support for low-carbon generation and housing stock efficiency.

Following its investigation into the GB energy market, in its Summary of Provisional Findings Report the CMA notes that:

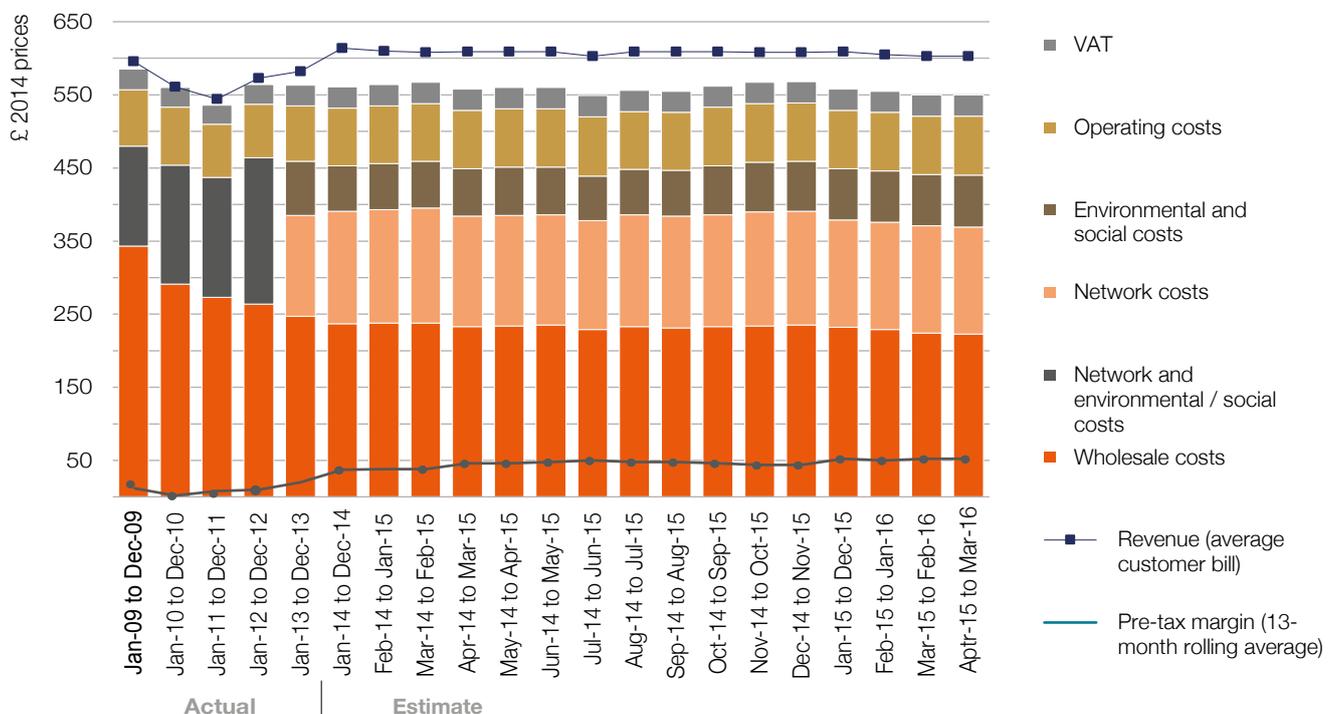
The rapid increase in domestic energy prices in recent years and the perception that profits and overall prices are too high have been a major source of public concern and were key drivers for the market investigation reference.⁶

Despite the significant public attention to company profits, the CMA found that the main drivers of electricity bill increases over 2009 to 2013 were “the costs of social and environmental obligations and network costs”. The CMA notes that profit margins⁷ fluctuated over the period and that margins on sales of electricity averaged just 2.1%. In generation in particular, the CMA found that...

...the profitability analysis does not provide evidence that overall, the Six Large Energy Firms earned excessive profits from their generation business over the period or that wholesale market prices were above competitive levels.⁸

Some respondents noted the significant challenge of regulators and judicial body’s assessing company returns, given the complexity of the task, and pointed out that findings by the CMA and Ofgem (see Figure 1) regarding margins and bills were not necessarily consistent with sources such as the energy company Consolidated Segmental Statements (CSS).

Figure 1: Breakdown of electricity bill over time (Ofgem)



Source: Ofgem (2015), <https://www.ofgem.gov.uk/publications-and-updates/charts-outlook-costs-make-energy-bills>

⁶ Competition & Markets Authority (2015), Energy market investigation: Summary of provisional findings report, July 2015, https://assets.digital.cabinet-office.gov.uk/media/559ad883e5274a155c00001b/EMI_PFs_Summary.pdf

⁷ Earnings before interest and tax (EBIT) margins

⁸ Ibid

1.2.2 Levies and general taxation

There was general agreement among interviewees that consumers did not have a clear enough picture of the impact of levies on bills. Some interviewees argued for a shift from levy-funded spending in energy towards general taxation, whilst others thought levy-funded spending remained the most practical means of delivering energy-related policy goals. Overall, however, it was agreed that more needed to be done by Government and industry to communicate with the public how it is meeting the challenge of security of supply, decarbonisation and affordability.

In its 2015 progress report, the Committee on Climate Change (CCC) estimated that levy-funded policy spending in 2014/15 reached £4.9bn, of which 90% was in the power sector (see Table 1). Taxation-funded spending, on the other hand, was £1.5bn in the same year, of which power sector spending reached only £3m. The majority of taxation-funded spending went to the 'waste and other non-CO2' sector.

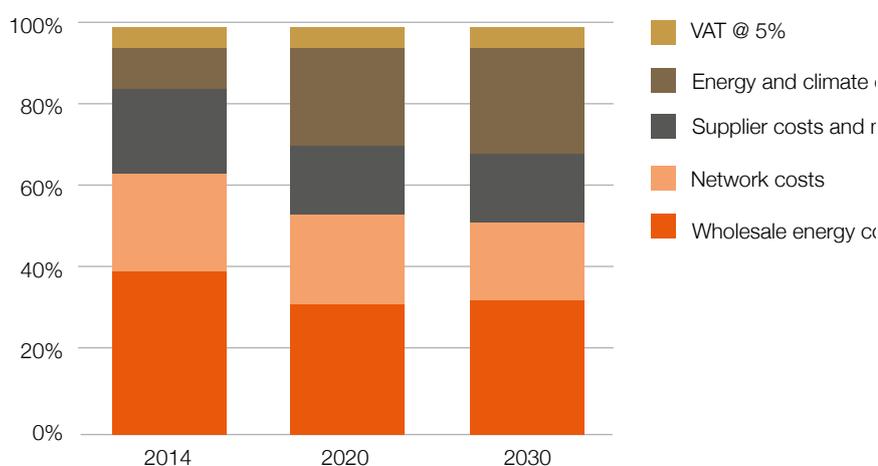
Moreover, the impact of the Capacity Market auctions would not be seen on bills until 2018/19 (for which last year's auction is estimated to result in £0.96bn being levied on consumers in 2018/19). Under current arrangements, these bill impacts will be additional to Levy Control Framework (LCF) spending (projected by DECC to reach £9.1bn in 2020/21 in real terms).

Some interviewees argued that this level of breakdown was not openly communicated to energy customers and the public, and was contributing to misunderstandings over bill increases and use of tax-payer money.

Several interviewees argued that, given the magnitude of levy-funded spending in the power sector, it is important to have open conversations with the public regarding the proportional impact of Government policies on bills. DECC estimates that energy and climate change policies as a proportion of total electricity bills will increase from 10% in 2014 to 24% in 2020 and 26% in 2030 (see Figure 2). Policy impacts are therefore forecast to overtake both 'supplier costs and margins' and 'network' costs in terms of percentage impact on bills.

A small number of interviewees mentioned the potential benefit of establishing an independent body to assess affordability and the impact of policy spending on bills and help communicate these impacts with the public. Others believed it should be Government's responsibility to create a dialogue with consumers.

Figure 2: DECC estimated policy impact on electricity bills



Source: DECC (2014), Estimated impacts of energy and climate change policies on energy prices and bills: 2014, <https://www.gov.uk/government/publications/estimated-impacts-of-energy-and-climate-change-policies-on-energy-prices-and-bills-2014>

* System costs are costs incurred to allow energy to be delivered from a generator to an end user. They include the costs of maintaining backup capacity, of system balancing, of connection to and transmission via the grid, and grid reinforcement and extension.

Table 1: Government support for carbon budgets by sector

Sector	2013/14	2014/15
Levy-finded spending policies		
Power	£3,700m	£4,400m
Buildings	£930m	£500m
Sub-total	£4,600	£4,900m
General taxation funded policies		
Power	-	£3m
Buildings	£100m	£420m
Transport	£230m	£280m
Waste and other non-CO2	£770m	£800m
Cross-cutting	£50m	£50m
Sub-total	£1,200m	£1,500m
Green Investment Bank	[£660m]	[£790m]
Total	£5,800m	£6,400m

Source: Committee on Climate Change (2015), Meeting Carbon Budgets: Progress in reducing the UK's emissions, 2015 Report to Parliament, June 2015, https://www.theccc.org.uk/wp-content/uploads/2015/06/6.737_CCC-BOOK_WEB_030715_RFS.pdf

1.2.3 Whole systems buy-in

An honest and interactive consumer engagement would involve helping customers understand the market in addition to providing transparent information. Enabling consumers to buy-in to the approach being undertaken by discussing the objectives and challenges in the energy market and the interaction of the different sectors, would provide a clear context to consumers. This will encourage policy goals to be met with the best value for money and with greater consumer support.

Furthermore, having more informed consumers, in conjunction with the appropriate 'smart' technologies would enable energy efficiency and demand-side response schemes to achieve greater take-up. This builds up the consumer as an active force in the energy market and hence could be a major contributor in solving the energy trilemma in the UK.

The whole systems approach, energy efficiency and DSR schemes will be discussed in more detail in the following chapters.