

# ENERGY ACT 2010

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## EXPLANATORY NOTES

### PART 3: REGULATION OF GAS AND ELECTRICITY MARKETS

#### *Adjustment of energy charges*

##### *Summary and Background*

127. In 2008, a market probe by Ofgem<sup>1</sup> into the energy supply markets for domestic and small business customers found that, in general, the ‘big six’ suppliers<sup>2</sup> were acting competitively. The probe did identify, amongst other concerns, that energy suppliers have consistently earned significantly higher margins for electricity supply than for gas supply in the period 2005-07 and that this difference in margins was not justified by cost differentials. Ofgem noted that in effect this represents a large difference in prices offered to ‘dual fuel’ customers (those who buy electricity and gas from the same supplier) compared to those who source their electricity and gas from separate suppliers, or do not have access to the gas grid.
128. Ofgem has introduced (with effect from 1 September 2009) a modification to the standard conditions of the gas and electricity supply licences held by suppliers with over 50,000 household customers to deal with these concerns by prohibiting undue discrimination in terms and conditions offered to customers<sup>3,4,5</sup>. This licence condition will expire on 31 July 2012 – a reflection of Ofgem’s expectation that the full package of measures proposed<sup>6</sup> to deal with concerns raised by the probe will have improved competition in the energy market to the extent that the licence condition is no longer necessary. Ofgem will, however, keep the situation under review.
129. Sections 41A and 41B of the Gas Act 1986 and sections 43A and 43B of the Electricity Act 1989 contain powers (not used to date) to allow the Secretary of State to adjust charges for gas or charges for electricity to help customers who are treated less favourably than others by their supplier. These powers do not currently allow the Secretary of State to intervene in cases where suppliers appear to be cross-subsidising their gas businesses from their electricity businesses and where, consequently, electricity-only customers are being treated less favourably, facing excessive prices not justified by cost differentials. This means that if Ofgem had not taken the action described above, the Secretary of State would have been unable to step in and the situation would not have been addressed.
130. These sections replace the powers in sections 41A and 41B of the Gas Act 1986 and sections 43A and 43B of the Electricity Act 1989. These new powers are derived from the pre-existing powers, but are amended to enable the Secretary of State to deal with

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<sup>1</sup> “Energy Supply Probe – Initial Findings Report”, Ofgem 140/08, 6 October 2008

<sup>2</sup> Centrica, EDF, EON, RWE Npower, Scottish Power and Scottish & Southern Energy

<sup>3</sup> “Addressing undue discrimination – decision document”, Ofgem 72/09, 26 June 2009

<sup>4</sup> “Notice of modification of the Standard Conditions of the Electricity Supply Licence requiring cost reflectivity between payment methods and prohibiting undue discrimination in domestic supply”, Ofgem 100/09, 7 August 2009

<sup>5</sup> “Notice of modification of the Standard Conditions of the Gas Supply Licence requiring cost reflectivity between payment methods and prohibiting undue discrimination in domestic supply”, Ofgem 101/09, 7 August 2009

<sup>6</sup> “Energy Supply Probe - Proposed Retail Market Remedies”, Ofgem 99/09, 7 August 2009

situations where energy suppliers treat customers less favourably according to the type of energy supplied.

### ***Commentary on Sections***

#### ***Section 26: Adjustment of charges to help disadvantaged groups of customers***

131. Subsection (1) gives the Secretary of State the power to make a scheme that will adjust charges for gas and/or electricity if the Secretary of State considers one set of customers of a particular energy supplier are treated less favourably than another set of customers. Subsections (3) to (5) provide that these sets of customers can consist of any combination of the following: the electricity customers of that supplier, the gas customers of that supplier, customers that are supplied with both gas and electricity, or any sub-division of these groups. For example, electricity customers could be subdivided into those who have access to the gas network and those who do not.
132. Subsection (6) specifies which energy charges (gas and/or electricity) the Secretary of State may consider. Subsection (7) allows the Secretary of State to make any appropriate calculations or assumptions to establish whether a particular set of customers is being treated less favourably when comparing different charges for the same type of energy, or charges for different types of energy.

#### ***Section 27: Schemes: supplementary***

133. This section makes provision about energy charge adjustment schemes made under the powers in section 26. Subsection (1)(b) allows for the scheme to adjust the charges of the customers that the Secretary of State considers have been treated more favourably as well as those that have been treated less favourably. Subsections (2) and (3) require the scheme to describe the less favourably treated customers, specify the energy companies whose charges will be adjusted by the scheme and the geographical area to which the scheme applies (unless it covers Great Britain). Subsection (2) also requires the scheme to set out the basis for the adjustment of charges.
134. Subsection (4) enables the scheme to require energy companies to provide information to each other and provides for any necessary modification of licence conditions. This section closely follows subsections (2) to (5) of section 41A of the Gas Act 1986 and section 43A of the Electricity Act 1989.

#### ***Section 28: Regulations adjusting energy charges: supplementary***

135. Subsection (2) requires the Secretary of State to give notice that it is proposed to make regulations to establish a scheme. Any such notice must be given before the regulations are made, and must set out the effect of the scheme and the reasons for making the scheme. The Secretary of State must give not less than 28 days for representations to be made in relation to the scheme. Subsection (3) provides that a copy of this notice must be given to the company whose energy charges will be covered by the proposed order and provides that the notice must be publicised sufficiently widely so that it will be seen by all those likely to be affected by it.
136. Subsection (4) provides that regulations will remain in force for the period specified in the regulations, and that the maximum period is three years, although further regulations may be made at the end of that period. Subsection (5) allows the Secretary of State to make regulations to require energy companies to provide information to each other for the purpose of enabling the making of regulations to establish a scheme.
137. Subsection (6) provides for Ofgem to monitor the effect of all regulations made under section 26 and report its findings to the Secretary of State. It also enables Ofgem to require energy suppliers to provide any information necessary for this purpose. Subsections (2) to (6) of this section closely follow subsections (1) to (5) of section 41B of the Gas Act 1986 and section 43B of the Electricity Act 1989.

*These notes refer to the Energy Act 2010 (c.27) which received Royal Assent on 8 April 2010*

***Section 29: Adjustment of energy charges: interpretation***

138. Subsection (2) allows regulations made by the Secretary of State to exclude certain sets of customers from being considered in relation to an energy charge adjustment scheme. Subsection (5) provides that the definition of 'energy supplier' includes electricity suppliers, gas suppliers, and suppliers of both gas and electricity.