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

SSE is one of the largest energy suppliers operating in the competitive energy markets in Great Britain and Ireland. At 31 March 2018, it supplied electricity and gas to 7.58 million household and business accounts. It also provides other related products and services, including telephone, broadband and boiler care, to 0.45 million household customers. It is proud to employ nearly 20,000 employees, be a Living Wage Employer and the first FTSE 100 company to have been awarded the Fair Tax Mark.

SSE Energy Services understands that the Scottish Government committed to establishing a publicly owned, not-for-profit energy company (POEC) with the objective and intention that “energy would be bought wholesale or generated here in Scotland – renewable, of course – and sold to customers as close to cost price as possible. It would give people – particularly those on low incomes – more choice and the option of a supplier whose only job is to secure the lowest price for consumers.” In general, SSE Energy Services remains of the view that these objectives are not best met through the creation of a Scottish POEC and, as part of its inquiry, would encourage the Scottish Parliament’s Economy, Jobs and Fair Work Committee to have regard for the following five characteristics of the GB energy market:

1. **The GB energy market is highly dynamic and competitive, meaning consumers have more choice than ever before.**

As of March 2018, there were 72 energy suppliers actively competing for domestic customers in GB, this is the result of significant entry and expansion of new suppliers, ranging from start-ups to major multi-nationals such as Shell, Vattenfall and ENGIE. New suppliers continue to successfully grow as demonstrated by the reduced market share of the six largest energy suppliers, from 95% in 2013 to just under 80% in 2017, meaning consumers have more choice than ever before.

There is strong evidence to suggest that consumers are taking advantage and benefiting from increased competition in the market as customer engagement continues to increase with 481,677 customer switching in June 2018 and 46% of customers electing to switch to either a small or medium supplier. Against this backdrop, it remains unclear what additional choice the proposed new Scottish POEC would offer consumers, beyond what is already available in the market, and we would encourage the Committee to consider that a Scottish POEC would experience similarly challenging competitive pressures.

2. **Energy supply businesses in the GB energy market typically make low margins, suggesting the scope for a publicly owned energy company to pass on savings to customers is limited.**

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¹Electricity Switching Data, June 2018, Energy UK, [https://www.energy-uk.org.uk/publication.html?task=file.download&id=6702](https://www.energy-uk.org.uk/publication.html?task=file.download&id=6702)
There are seven key cost components which make up a domestic energy bill and latest Ofgem data suggests the following average breakdown across the market: wholesale costs (36.17%), network costs (25.44%), policy costs (9.67%), operating costs (18.33%), direct costs (1.23%), VAT (4.76%) and supplier pre-tax margin (4.40%). The majority of these costs are variable and, crucially, outside a supplier’s control. In particular, over the last year, SSE Energy Services has seen wholesale costs increase considerably and is also seeing an increase in the cost of delivering the smart meter programme. These cost increases were recently acknowledged by Ofgem when it increased the level of the price cap for prepayment meter customers, citing higher wholesale and policy costs. SSE Energy Services’ experience leads it to agree with the conclusions of Ernst & Young’s ‘Strategic Case’ which notes that “the pre-tax profit margins made in this market, on average, are limited.”

At SSE Energy Services, we have a responsibility to run a sustainable business for our customers, employees, broader stakeholders and shareholders and need to make a fair return to do so. In recent years, SSE Energy Services has regularly made an average dual fuel margin of around 5% and continues to work hard to reduce its cost-to-serve by delivering efficiency savings.

SSE Energy Services also notes that a Publicly Owned Energy Company, in the early years of operation, could fall below the current customer threshold required for participation in the WHD scheme of 250,000 domestic customer accounts. This would mean that it would not be liable to offer eligible customers the £140 WHD annual payment. Vulnerable customers may therefore be better served by suppliers that are required to participate in the WHD.

Given this challenging operating environment, it remains unclear how a POEC would have the capabilities to offer customers meaningful reductions in the price they pay for their energy, beyond those already available in the market. Instead, SSE Energy Services would encourage the Scottish Government to support calls for policy costs to be paid for via general taxation, rather than via a levy on consumers’ bills. This would ensure that customers’ contributions were means-tested and would tackle the unfair penalisation of customers who predominantly rely on electricity.

3. Significant numbers of customers are already, or will soon be, subject to price protection measures.

The GB energy supply market continues to be subject to considerable change with the recent introduction of price protection measures for 70% of the market. Following a two-year long investigation by the CMA, Ofgem was required to introduce a price cap on prepayment meter tariffs (PPM Price Cap). This cap was introduced in April 2017 and is due to expire by the end of 2020, in line with the targeted conclusion of the smart meter rollout. On 2 February 2018, Ofgem extended the PPM price cap to a further one million vulnerable customers receiving the Warm Home Discount (WHD).

In addition, on 19 July, the UK Parliament passed the Domestic Gas and Electricity Act, which gives Ofgem a duty and the powers to cap the price of Standard Variable Tariffs (SVTs). On 6 September 2018, Ofgem confirmed its intention to introduce a price cap at the end of 2018 and has published a statutory consultation on its proposal to adopt a “bottom-up” cost methodology to set the level of the cap at £1136. This cap on SVTs would be in place until 2020, after which Ofgem would annually review the state of the market with the possibility of extending the cap out to 2023.
With 70% of consumers now having the price they pay for their energy capped by Ofgem at a level the regulator deems to be reflective of costs in the market, arguably, a number of the original findings and potential benefits of a Scottish POEC, as set out within Ernst and Young’s ‘Strategic Case’, appear outdated.

4. There is limited evidence to suggest that a POEC will help tackle the underlying causes of fuel poverty.

The drivers of fuel poverty are complex and multi-faceted and, in SSE Energy Services’ experience, can be triggered by the following four variables:

   i. *Income*: including low wage and difficulties in accessing benefits;

   ii. *Energy efficiency*: including sub-optimal housing conditions, ‘hard to treat’ homes and inefficient appliances;

   iii. *Price of energy*: and policy costs which, although have long-term benefits, are collected via bills rather than general taxation (FiTs, low carbon CfDs, capacity contracts, transmission and distribution costs, and other taxes and levies; and

   iv. *Personal circumstances*: these can be multi-factorial, temporary or permanent and can include illness, disability and financial pressures, which can affect energy use and the ability to engage with the energy supplier or the market.

Correspondingly, any solution to fuel poverty should aim to focus on all four of these drivers. SSE’s customer service teams deal with thousands of customers every week and, in our view, in a large number of cases, low income is one of the primary reasons why some customers require additional assistance. There are also a significant number of people, particularly amongst those living off the gas grid or in ‘hard to treat homes’ who have inefficient housing and appliances. These people may not necessarily qualify for benefits given it is often their energy bills which can temporarily pull them into fuel poverty due to its fluid nature. Similarly, efficient energy use in the home must be considered in order for fuel poverty to be tackled holistically.

SSE Energy Services does not believe the addition to the market of a POEC will help tackle fuel poverty; rather a carefully targeted system is needed. The solution should be better linked to benefits data, better focused on finding the “right solution” for each customer and better linked with existing energy efficiency schemes and helping people to make the right personal choices. SSE Energy Services continues to support the establishment of a dedicated ‘Fuel Poverty Agency’, which could be a part of Government or the voluntary sector, and specifically focused on assisting the people who need it most. We see the role of the Fuel Poverty Agency to be as follows:

- the first port of call for anyone struggling to pay their bills once their supplier has got them on the best tariff for their needs;

- ensuring that the individual is on any benefits that they are entitled to;
ensuring that those individuals who are struggling with their bills are on a “priority list” for receiving energy efficiency measures through the Energy Company Obligation (which SSE believes should be purely targeted at those in fuel poverty);

• dedicated follow-up to ensure that energy use in the home is managed effectively; and

• ensuring that the individual receives a core element of financial advice. This could be linked to other Financial Inclusion institutions.

SSE Energy Services believes strongly that such an Agency would be best able to find customers and make better assessments of need than energy companies and will have a range of options for improving peoples’ circumstances, far exceeding those offered by energy companies or a Scottish POEC.

Alongside this, SSE Energy Services would encourage focus on maximising the benefits of some of the existing programmes in Scotland, rather than diverting resources towards a POEC. The Route Map for the ‘Energy Efficient Scotland’ Programme sets out the journey Scotland’s homes, businesses and public buildings will need to take to become more energy efficient over the next 20 years. This is a long-term programme with ambitious aims and will require a collaborative approach from existing housing providers, suppliers and voluntary organisations to ensure that the message and the benefit is optimised.

5. The experience of several local authorities of establishing and running energy supply functions exemplifies how challenging it can be in today’s competitive market.

Although on a smaller scale, a number of local authorities have already introduced their own POECs, or else invested in suppliers, with limited success.

Bristol Energy began trading in 2015 as a licensed gas and electricity supply company owned by Bristol City Council but operated independently. Staff are employed by Bristol Energy and the Board has a Bristol City Council representative as well as other Non-Executive Directors. The process of taking the company from initial proposal to fully licensed supplier took around five years. Although Bristol Energy aims to offer city residents the cheapest tariffs in the market, this has arguably caused financial detriment to the company since it made a loss of £8.4m for the year 2016/17. Similarly, Robin Hood Energy owes its parent, Nottingham City Council, £12m and has reported cumulative losses of £9.9m.

In light of these challenging market conditions and the number of suppliers now operating in the market, in August 2018 Portsmouth City Council confirmed its decision to abandon plans to launch its own energy company. This followed an independent report by PWC that said the supplier would need 144,000 customers to sign-up and an investment of £19m over four years to be viable. The Council confirmed the decision, saying: “The decision we have made is to limit the risk of losing millions of pounds of public money. It’s a very difficult decision but we have decided it’s not the right thing for a council like us to be doing. It’s too risky.”

In light of these five characteristics of the GB energy market, SSE Energy Services remains of the view that it would not be appropriate for a Scottish POEC to be involved in the supply of energy to customers. Not only would it risk distorting the competitive market and deterring private investment, given that margins in energy supply are low and suppliers have limited control over the various cost components that make up a household energy bill, SSE Energy
Services does not believe establishing a Scottish POEC is the best way for the Scottish Government to meet its stated objectives.