



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

Management of Customer Payments & Arrears

Report on the Consultation and Decision Paper

CER/05/060

April, 2005

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1. Background

1.1 The Commissions Decision

The Commission has decided that the Change of Supplier process and other market procedures shall not include or accommodate objections for the purpose of restricting customers in arrears or in debt from changing supplier.

Other arrears-prevention options open to suppliers, as outlined in consultation paper 04/044, *Management of Customer Payments & Arrears*, are a matter for suppliers in their dealings with consumers – provided that contractual conditions specified in S.I. 60 of 2005 are met including the relevant Suppliers' Customer Charters.

1.2 Consultation Background

In January 2004, the Commission issued a consultation paper – *Management of Customer Arrears* (CER 04/044) – on the issue of potential customer debt¹ in the electricity retail market and the methods that may be employed by Suppliers in mitigating this debt.

The purpose of this consultation paper was to:

- Restate the Commission's opposition to the inclusion of a formal 'debt-blocking' objections process in the Electricity Retail Market Review Group (ERMIG) design and the reasons for the Commission's position;
- Outline a number of measures which suppliers could themselves employ to reduce potential customer debt, such as use of security deposits and credit checks;
- Summarise 'debt-blocking' practices employed in other jurisdictions.

Responses to this consultation paper were published on the Commission's website in April 2004. Responses were received from each of:

- Airtricity;
- Bord Gáis Eireann ('BGE');
- ESB Customer Supply ('PES');
- ESB Independent Energy ('ESBIE')

At this time the Commission also signalled its intent to revisit this issue in early 2005 in light of the up-and-coming implementation of legislation on consumer

¹ The definition of debt – in particular the time or monetary level at which normal arrears becomes debt – depends on the contract that exists between the supplier and the customer. Accordingly what constitutes debt varies on a case-by-case basis and therefore is not defined in this paper.

protection in the electricity industry. This legislation, S.I. 60 of 2005², was passed into law in February 2005.

The issue of customer debt has also arisen in the gas retail market, in particular at Gas Market Opening Working Group (GMOWG) business process meetings where gas suppliers have requested a decision on this matter from the Commission.

The Commission considers that the issue of consumer debt, and the means by which consumer debt may be mitigated, applies equally to both the electricity and gas markets. There is no reason why a decision on this matter should apply to the electricity market should not also apply to gas. In this light, the decision contained in this document will apply to both the electricity and gas retail markets.

1.3 Legislative Issues

In 2003, Directive 2003/54/EC³ outlined Member States duties with regard to protection of consumers, namely duties relating to suppliers' dealings with customers. Article 3 of this Directive, in addition to the Annex, outlines minimum statutory contractual rights of consumers.

Statutory Instrument 60 of 2005 transposes these conditions into Irish legislation. Regulation 23 refers to minimum contractual requirements that shall exist between suppliers and domestic customers for the purpose of consumer protection. The Commission may also extend this Regulation to small and medium sized businesses. Supplier-customer contractual conditions for large customers are not covered by this Regulation and as such are outside of the Commission's remit in this area.

Therefore this document is prepared in the context of the fact that customer debt is not explicitly addressed in Statutory Instrument 60 of 2005 and the fact that regulation of customer-supplier contract provisions in the S.I. extend to domestic customers and small & medium sized businesses only. However, the Commission has a duty, in exercising its powers, to do so in a manner that protects the interest of final customers.

Article 3 of EU Directive 2003/55/EC concerning common rules for the internal market in natural gas also provides that Member States ensure that eligible customers are effectively able to switch to a new supplier.

² The European Communities (Internal Market in Electricity) Regulations 2005 (SI 60 of 2005) was signed by the Minister for Communications, Marine and Natural Resources on 8 February last.

³ Directive 2003/54/EC of the European Parliament and of the Council Concerning Common Rules for the Internal Market in Electricity and Repealing Directive 96/92/EC

1.4 Rationale

Throughout 2002 and 2003, suppliers representatives at the Electricity Retail Market Review & Implementation Groups (ERMRG & ERMIG) industry meetings expressed concern that full market opening may result in an increased incidence of customers switching suppliers to avoid bill payment.

The rationale for consulting on this issue, therefore, has been to gain the views of suppliers and consumers on the general issue of how to mitigate the effect that potential customer debt in the electricity retail market might have on the market post-full market opening in 2005.

Specifically, the majority of suppliers were of the view that retail market opening processes and systems should incorporate a formal objection for the purpose of restricting customers in debt from moving supplier. This objection process, as viewed by the Commission in light of comments received from the industry groups and in response to the consultation paper, would at least allow for suppliers and/or the MRSO – as meter point registrar – to be notified of the payment record/status of the in-debt customer, and at most would restrict a customer moving supplier via a formal debt-blocking process.

On the point of a change of supplier objections process, the consultation paper stated the Commission's view that the change of supplier process is not to be used to stop customers in arrears from changing supplier.

In the context of the above, the purpose of this Decision paper is twofold:

- To reiterate and outline the Commission's position on the interaction of the issues of customer debt and the Change of Supplier procedures, in particular that these procedures will not accommodate objections for the purpose of restricting customers in debt from changing supplier;
- To outline the Commission's views on options open to suppliers in preventing customer debt.

The structure of this decision paper is as follows:

- Section 2 contains comments submitted by suppliers on the issue of a Change of Supplier processes related to this issue. The Commission's response to these comments are made at the end of this section;
- Section 3 sets out comments submitted in respect to a number of other debt prevention options open to suppliers in dealing with customer debt, as presented by the Commission in CER 04/044. The Commission's response to these comments is made at the end of this section.

2. Customer Debt & Market Processes

Although the issue of customer arrears, and the mitigation of the effect of customer debt on suppliers, may be remedied by way of a number of preventative measures, the main focus of suppliers to date, has been on proposing the introduction of a formal debt-blocking measure, that is a mechanism that would allow an old supplier to prevent an ‘in-debt’ customer from changing to a new supplier so as to avoid bill payment. In essence such a process would give suppliers recourse to pursuing breach of contract conditions via the change of supplier process.

Respondents to the previous consultation, CER 04/044, also proposed a number of other ways which market processes could be used to mitigate the exposure of several suppliers to customer debt. These include:

- The transferral of in-debt customers to a ‘supplier of last resort’;
- Restrictions to be placed on customers moving once a de-energisation request or meters works request has been placed on a customers meter point;
- The transferral of debt from the old supplier to the new supplier.

Finally respondents also commented on the Change of Supplier frequency restriction cited in the consultation paper.

2.1 Objections Process

Over the life of Electricity Retail Market Review & Implementation Groups (ERMRG & ERMIG) industry meetings, independent suppliers and ESB PES have put forward proposals for the incorporation of a formal objection mechanism in the change of supplier process for the purpose of restricting customers in debt from moving supplier.

While an ‘objections to Change of Supplier’ industry process already exists, this process does not allow objections for the purpose of debt. Objections currently permitted include circumstances where a customer has been erroneously registered with a new supplier. The scope of what are known as “erroneous transfers” include circumstances where a supplier code of conduct provision has been breached. For example, where an unauthorised person (e.g. a minor) signs for an independent supplier on behalf of a customer, and where a change of supplier request is submitted to the MRSO for processing for that customer, an old supplier may object to the said transfer. In this case the objection is made on behalf of the affected customer. In other words erroneous transfers are ‘customer led’ for the most part.

Suppliers’ proposals for a formal debt objections process, on the other hand, are ‘supplier led’. Such a process, as understood by the Commission in light of comments received in the industry groups and in response to the consultation paper, would at least allow for new suppliers and/or the MRSO to be notified of

the payment record/status of the in-debt customer, and at most would restrict a customer moving supplier via a formal change of supplier blocking process. Variations on this restriction, such as the blocking of customers who have de-energisation requests placed on their connection point, have also been proposed.

A large number of comments were received on the issue of a formal objections process for customers in debt. These comments are summarised below⁴:

- Blocking will not of itself solve the problem of bad debt. Forcing a customer to stay with a supplier is more likely to result in the level of debt increasing, rather than it being paid off;
- A formal notification/objection process, within the change of supplier process, will assist the market to identify 'special action' customers and monitor their resolution. Such a process operating with strict timescales will ensure the integrity of the market from a customer, supplier and regulatory view; The Commission will, through a formal Change of Supplier ("COS") process for objections, be able to monitor and evaluate supplier behaviour;
- It should be noted that the Change of Supplier process as designed does not permit, as is the case in other jurisdictions, a supplier to prevent a customer who is in arrears from changing supplier. The MRSO can penalise the new supplier for cancelling new customer registrations in certain circumstances; this will help ensure that erroneous transfer are minimised and that new suppliers perform effective credit checks. We are not entirely convinced that a similar restriction need apply here assuming that the existing change of supplier design can operate. As this design allows a flag to be raised, the new supplier in these circumstances is alerted to make further enquiries if he thinks fit. This reduces or eliminates the need to for a restriction. We would welcome the opportunity to discuss this still further.
- In the Northern Ireland market, independent suppliers are entitled to object in cases where the customer has outstanding debt. Such a facility is required in the Republic of Ireland market to prevent customers from changing supplier to avoid payment of electricity charges and to promote good customer behaviour in the market. It is in everyone's interest (suppliers and customers alike) that all measures are taken to minimise bad debt and afford protection to suppliers without recourse to legal action, which can be prohibitively expensive. The following objection procedure should be adopted in the Republic of Ireland market.
 - The old supplier has a number of days to raise an objection when notified of a change of supplier for an existing site;

⁴ Full and original responses to this consultation were published by the Commission on April 22nd 2004. These can be obtained at www.cer.ie

- The objection should be in line with objection reasons to be agreed by all market participants and CER. Valid objections would consist of cases where the customer has outstanding debt (monies owed on an invoice that has not been paid in line with the terms of the contract) or because the customer is under contract with the old supplier;
- The reason for the objection is communicated to the new supplier by MRSO;
- The new supplier can then approach the customer to resolve the issue (this may involve the customer discharging their debt with the old supplier in which case the objection can be withdrawn by the old supplier or may involve the customer confirming that they are in fact still under contract with their old supplier in which case the COS is withdrawn).

This process can be handled by the MRSO with appropriate input from the old supplier, new supplier and the customer. It need not be bureaucratic and with objection reasons agreed by all participants should not be open to abuse. This approach is more transparent and more direct than limiting the number of times a customer can change supplier in a period.

2.2 Changes to Other Market Processes

One supplier suggested a number of other ways (other than via a formal objections process) that the market processes could be used to mitigate customer debt. For example, a customer could be restricted from moving when a de-energisation or meter works request has been place on the customer's site.

This supplier stated that:

- The only real sanction against 'delinquent' customers that is available to suppliers is de-energisation. Customers receive a number of written warnings prior to disconnection and therefore have an opportunity to change supplier if they so wish. Experience shows that some customers choose this route, so it is clearly a real option. However, once the affected supplier has incurred the cost of calling out Networks to de-energise, then either the intended change of supplier should be blocked until meter works commissioned by the existing supplier have been completed. Alternatively, the cost of the meter works could be charged to the new supplier.

The first of these measures – blocking customer movement until de-energisation has been completed – was this respondent's preferred option:

- As it prevents a bad debt from being compounded by charges for abortive meter works while still allowing the customer to change supplier prior to the meter works being instructed. If a new supplier is willing to accept the cost of the meter works, then the change of supplier could proceed unhindered. In neither case would the customer's ability to change supplier be affected, nor would the original supplier necessarily be able

to recover the debt. The second suggestion would result in a charge to the intending new supplier, rather than to the customer, so could also be regarded as compliant with the EU Directive.

2.3 *Transferral to Supplier of Last Resort (SoLR)*

In addition to the above described proposal for a formal objections process, one respondent proposed that indebted customers could be transferred to a supplier of last resort. Such a policy would be in line with provisions in place in Northern Ireland.

Regulation 22 of S.I. 60 of 2005 provides that the supplier of last resort mechanism is to be used in the event of a supplier exiting the market. The universal service obligation provision of the above Statutory Instrument, as specified by Regulation 21, refers to the duty of a nominated universal service provider. Clearly the transfer of an in-debt customer would fall under Regulation 21.

Likewise it has also been proposed that large industrial customers whose plant/premises pose a significant safety/environmental risk should be automatically transferred to the universal service provider upon payment default⁵.

Notwithstanding the scope of the SoLR role, what has been proposed is to transfer in-debt customers back to the universal service provider, a service that has been provided to date by ESB PES.

The Commission received one proposal to transfer customers in debt to the SoLR. This proposal outlined how, in cases where customers (and in particular large customers) have outstanding debt with a supplier, an independent supplier should be permitted to de-register the site to the Supplier of Last Resort. This respondent argued that, as the SoLR is a regulated monopoly, any debts incurred by SoLR could be factored into the regulated revenues approved by Commission. This would send the correct signal to customers who default on payments as it would effectively remove their choice of supplier and force them to remain on published tariff for a period.

2.4 *De-energisation*

The issue of de-energisation, or more specifically the current requirement on suppliers to pay system charges for six months on accounts after those accounts have been de-energised, was raised in one response to this consultation. While the consultation paper did not raise this point, the Commission acknowledges that suppliers are affected by this industry rule.

This respondent argued that the current rule whereby suppliers are still liable for the fixed charge elements of DUoS/TUoS post de-energisation for 6 months

⁵ This issue has been considered as part of a separate consultation process.

should be removed – as these charges cannot be passed on to the customer, their effect is to increase the amount of bad debt a supplier faces. All network charges should cease upon de-energisation.

2.5 Debt Transfer

One supplier suggested that another way to mitigate customer debt could be to allow for the transfer of debt from the old supplier to the new supplier upon completion of the change of supplier.

Such a measure, if implemented, would require agreement from customers to allow debt to be transferred.

2.6 Change of Supplier Frequency Restriction

The consultation paper also listed a change of supplier frequency restriction as a measure that has been used in other countries to mitigate customer debt.

While the frequency restriction itself would not *per se* stop customers in debt from changing supplier, it would have the effect of limiting the risk suppliers face. For example if a customer could only move, say, every 12 months, then that customer would have to pay the majority of its bills for the remainder of that period so as to avoid de-energisation.

Two comments were received on this measure. One respondent did not see the need to place limitations on the number of times mass-market customers may switch supplier in a period. Another supplier who was in favour of such a measure, stated that there should be a limit on the number of times a customer can change supplier in a specified time period and suggested that this a maximum of say, 3 moves in 2 years unless the customer had a clear payment record. This respondent added that the implementation of this restriction would require the resolution of practical and possibly legal issues

2.7 Commission's Position

A number of general points should be emphasised when considering whether or not to expand the scope of the current erroneous transfer objections process or, indeed to any other market process to cases where in-debt customers wish to change supplier.

While the Directive does in fact refer to certain contract conditions that should exist between customers and suppliers, it does not refer to potential remedies for customer indebtedness. Without commensurate consumer protection measures the introduction of an objections process could potentially leave consumers exposed. Even if the Commission supervised an objections process, the Commission considers that the resources required for this bureaucratic role would outweigh the benefits and it would be more efficient for suppliers to put in place preventative measures such as deposits, receipt of credit history details etc.

Finally, while there is the possibility that customers may wish to use the Change of Supplier process to circumvent bill payment, this practice could occur in any industry in the absence of safeguards put in place by suppliers to stop such practices. It is the position of the Commission therefore that the risk posed by customers in not paying their bills is a factor in any commercial environment irrespective of whether the service is being paid for during or after the use of the product.

Therefore, given the above points, the Commission is opposed to the extension of the existing erroneous transfer process to circumstances where a customer is in debt for the following reasons:

- Applying such a customer switching objections process may be contrary to the Directive and the consumer protection measures contained therein;
- The monitoring of such a formal objections process would place a large bureaucratic burden on the Commission;
- Suppliers may themselves employ a number of effective debt prevention measures.

In respect of supplier's proposals for changes to other market processes, these can be summarised as follows:

- Transfer to Supplier of Last Resort (SoLR): Customers in debt would be transferred to the supplier of last resort as nominated by the Commission in line with powers granted under S.I. 60.
- Use of Meter Works/De-energisation Requests to restrict customer movement: Customers with the above requests active on their account would be restricted from moving supplier until those requested actions are completed;
- Transfer of Debt to New Supplier: The new supplier, upon registration of the new customer, would inherit the debt;

On this first point, it should be noted that a designated supplier undertakes the SoLR role when customers are transferred to it by a supplier exiting the market. The scope of this role, therefore, does not extend to the transfer of defaulting customers, and therefore should be excluded as an option in this case.

The use of alternative market processes, such as de-energisation requests, would limit defaulting customers' ability to change supplier. However, the employment of these processes for this purpose would restrict customers from moving supplier in the same way that a formal objections process would restrict customers from moving supplier. As such, the Commission is against the use of these business processes as debt prevention measures for the same reasons stated above in respect of the formal objections process⁶.

⁶ The electricity and gas market business rules, as they currently stand, are not explicitly designed to cater for debt prevention. The Commission will revisit these rules if they are used for the purpose of blocking indebted customers from changing supplier.

The same reasoning applies to the proposal to transfer debt. For this proposal to function properly, the customer would have to agree to the transfer of monies owed. To the knowledge of the Commission, in Britain if the customer does not consent to debt transfer the change of supplier request is blocked. In this instance the requirement of a customer to acknowledge debt would act as *de facto* change of supplier restriction. In any case the Commission is not mandated by S.I.60 to request customers to acknowledge debt.

Another measure used in other countries – as described by the Commission in the original consultation paper CER 04/044 – concerns the use of change of supplier frequency restrictions. This method, as considered by the Commission, is very much a second-best option given that customers would be restricted from moving supplier while suppliers would still face the possibility of in-debt customers changing towards the end of the restriction period. As such the Commission is against such a restriction.

Finally the period of time a supplier is registered to a site is a wholesale market rule. The Commission considers that any change to this rule should be considered by the Trading & Settlement Modification Panel.

3. Customer Debt Management

Consultation paper 04/044 put forward a number of preventative measures which suppliers could employ to reduce the instance of bill payment default. These measures included the potential use of:

- Security Deposits;
- Direct Debiting;
- Credit Referencing facilities/agencies.

This paper also referred to the future expansion of structures that would allow all suppliers to avail of prepayment meter accounts.

In addition, as stated in section 2, the Commission's remit under S.I. 60 does not explicitly extend to monitoring supplier-customer contract conditions for the purpose of debt or arrears. As such the above options are presented for information purposes only. Ultimately it is the responsibility of each supplier to determine how it applies contract conditions that are not covered by S.I. 60.

3.1 Security Deposits

Suppliers could possibly charge security deposits⁷ as a means of encouraging customers to avoid the build-up of arrears. ESB PES currently charges certain customers a security deposit typically based on a 2-bill estimate.

This issue raised a large number of points from suppliers. These are summarised as follows:

- Security deposits are more straightforward to enforce in a monopoly market; with competition, customers may view imposition of a security deposit as a blockage to changing Supplier, or may simply choose another Supplier who is not asking for such a payment. In practice therefore, security deposits may be less helpful than they initially appear.
- In a competitive market the application of security deposits is not realistic.
- If security deposits were used, would the existing supplier disclose if they held a returnable security deposit to the new supplier? Or is the refunded security given to the customer before they are able to pay the new supplier? Or is the new supplier transferred the existing security deposit from the existing supplier? How would this be controlled at change of supplier process, if informal there are no controls, and the risk will always lie with the new supplier if they act before knowledge of the situation?

⁷ In this consultation, Security deposits were proposed as a measure that could be devised by the supplier. Such a system would be operated by the supplier itself and would not therefore be operated by the DSO or MRSO.

- New suppliers, to minimise risk, would request customers to pay a security in advance before submitting a change of supply. How many customers would pay in advance? It is our simple view that security deposit requests would be a constraint to customer switching;
- The payment history record on existing customers is obtainable with the permission of the potential customer by independent suppliers from the normal bill;
- ESB PES Deposits are fully refundable to customers after 14 months if payment of the accounts has been kept up to date. A typical 2 bill domestic security deposit is €150 but this is not levied on all customers. The normal procedure is that the customer is offered the option of DD, Security Deposit or guarantor. This makes good commercial sense and is in the interests of customers generally because in many cases the customers in rented accommodation have no previous track record with PES. It is also the case that the above requirements would be waived in the customer had a previous good track record of bill payment at a previous address;
- In many cases, the use of security deposits is not a viable option because the size of the security deposit would typically need to cover one or two months billing charges to afford meaningful protection to the supplier. In the case of a large customer (MV and above) it is not practical to levy one to two months billing charges

3.2 Direct Debit

Another means put forward for addressing the issue of customer payments and arrears is the option of giving all customers the choice of paying by direct debit.

The main comments received on the use of direct debit to mitigate consumer debt were as follows:

- A "bounced" direct debit is an early warning sign of potential payment difficulties, but once a payment is missed this payment method offers no guarantee that debt build-up will cease, the reality of payment by direct debit is that it is more risky than any other form of credit sale arrangement.
- The paper's reference of comparing direct debits to a security deposit is misleading, even customers on direct debit can default;
- While Direct Debit is useful, it does not have the advantages of a deposit e.g. a customer may cancel a direct debit;
- Payment by DD does not afford the supplier any protection against a customer getting into arrears due to short-term cash-flow problems or due to company closure because the customer can cancel a direct debit mandate at any time

3.3 Prepayment Meters

At present, token meters or 'budget controllers' are used by ESB PES as a customer debt management measure as well as a means by which customers

may budget for both future electricity use and arrears. The introduction of an industry-wide prepayment-metering scheme would allow all suppliers to charge customers in advance for electricity used.

In August 2004 an industry prepayment working group was established by the Commission to further this issue.

One or a number of prepayment meter types will be chosen for a pilot project to take place in 2005. The Commission would like to see the pilot project involving at least two suppliers, in order to ensure that the fundamental requirement that the technology can support many suppliers is met.

Most respondents noted that their comments on this issue had been submitted as part of a separate Commission consultation process on prepayment metering. However, one respondent stated its view that:

- Prepayment metering is an effective tool for prevention/recovery of bad debt;
- the rollout of appropriate new prepayment metering technology will facilitate competition in supply and effective debt management, for domestic and smaller commercial enterprises.

3.4 External Customer Register

The use by suppliers of an external customer register or credit referencing agency would entail the use of a credit agency to maintain customer payment records for all customers, accessible by all adhering suppliers.

Suppliers could potentially consult these records to discern if a contract should be offered to a customer, and if so, on what terms.

One respondent, however, noted that

- independent suppliers have limited knowledge on the credit history of customers being supplied by other suppliers. While there is publicly available information through credit checking agencies, frequently this type of information is too generic, usually out of date and not suited for the particular credit difficulties associated with the supply of electricity as noted above;

3.5 Commission's Position

While recognising that debt prevention measures are of little or no use once debt has been accrued, suppliers can still take steps to prevent the build-up of debt in the first place. The Commission maintains the view that the use of security deposits, direct debit payment, and prepayment metering (when introduced), could have a considerable impact on the level of arrears in the electricity industry, especially on arrears borne in respect of small and medium-sized customers.

While the above-mentioned measures will be of limited use for larger customers, suppliers can still request payment history details from external debt registers or from customers prior to signing a customer.