Consultation Response:

Ofgem Standing Charges: Call for input

Response by the Money Advice Trust

Date: January 2024

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Introduction

About the Money Advice Trust

The Money Advice Trust is a charity founded in 1991 to help people across the UK tackle their debts and manage their money with confidence.

The Trust's main activities are giving advice, supporting advisers and improving the UK's money and debt environment.

In 2022, our National Debtline and Business Debtline advisers provided help to 140,980 people by phone, webchat and our digital advice tool with 1.87 million visits to our advice websites. In addition to these frontline services, our Wiseradviser service provides training to free-to-client advice organisations across the UK and in 2022 we delivered this free training to 2,780 organisations.

We use the intelligence and insight gained from these activities to improve the UK's money and debt environment by contributing to policy developments and public debate around these issues.

Find out more at www.moneyadvicetrust.org.

Public disclosure

Please note that we consent to public disclosure of this response.

Response to consultation

Thank you for the opportunity to respond to the Ofgem standing charges call for input. We have taken the decision not to respond to all the individual questions but to provide a statement response instead.

We are pleased that Ofgem acknowledges the scale of the problem in its paper.

"Standing charges for domestic electricity customers have increased significantly since 2021. For a customer who pays for their electricity bills by direct debit, they have more than doubled from £86 per annum to £186 per annum on average between 2021 and 2023. The reason for this increase in electricity standard charges is that suppliers are now having to pay more fixed costs and are passing them on to customers in the form of standing charges rather than a unit cost basis."

We hope that Ofgem will use the responses to the call for input to consider changes to the standing charge system, particularly for people on prepayment meters (PPMs), who are most disadvantaged by the current system. Over the years both government and Ofgem have made policy decisions that have loaded a variety of costs on to the standing charge, in particular network charges and the costs of failed suppliers.

This series of decisions has had a disproportionate impact on the most vulnerable energy users, and consumers on prepayment meters in particular. We would urge Ofgem to work with government to consider how future policy costs should be allocated across bills.

Our recent research into energy debt

We are very concerned about the impact on consumers of high energy bills. Energy debt issues have soared from 18% of calls to 30% of calls to National Debtline in the last six years. More than one in five (21%) Business Debtline clients have energy arrears – up from 16% six years ago.

The combination of high prices across essential goods and services, including energy, has led to a situation where many people simply do not have enough money coming in. Two in five (41%) National Debtline clients and over half (56%) of Business Debtline clients have a deficit budget – meaning their income is not enough to cover their essential costs.

The most common reason for financial difficulty among National Debtline clients is that their income is too low for their basic needs (16% of clients). For one in ten (9%), the cause of their debt was an increase in their outgoings – a four-fold rise since 2021, when this was the cause of financial difficulty for just 2% of clients. It is also worth highlighting that the majority of National Debtline clients are in work (37% in full-time employment and 21% in part-time employment), highlighting the sheer scale of the challenge many people face just to keep up with the essentials.

Our recent research[1] finds that:

- One in four people in energy debt (24%) cannot currently afford to repay their arrears.
- 21% said their supplier had not accepted an affordable offer of repayment.
- The same proportion (21%) have been threatened with enforcement action by their supplier, even though they had told them they were struggling to repay.
- A quarter (24%) are regularly losing sleep worrying about their energy debt.

The research revealed the drastic steps some households are already having to take to keep up with energy bills – raising questions about how households would cope with any increase in bills.

- More than one in five UK adults (22%) say they have cut back on food and other essentials in order to keep up with energy bills (an estimated 11.6 million people).
- One in ten (9%) – equivalent to 4.7 million people- have sold personal possessions, while 7% have used their overdraft and 4% of UK adults turned to high-cost credit in an effort to stay on top of high energy costs.
- Two thirds (66%) of UK adults say they will reduce how much they use the heating this winter.

Our view on the Ofgem approach to standing charges reform

We are pleased that Ofgem are taking the first step by changing the rules for suppliers on how they charge those who pay by different payment methods and reducing the standing charges for those who pay by prepayment meters and standard credit.

We cannot comment on whether the current standing charges reflect the actual costs of delivering energy by suppliers. We will leave others to debate this point. However, we acknowledge that these costs do have to be met somehow. In a climate where a significant minority cannot afford to pay their energy bills, this is an increasingly difficult question to answer.

We broadly support the principle of reducing standing charges. We believe that there are many factors to consider which will make any decisions on how to reform standing charges extremely complicated. There appear to be the potential for both winners and losers depending upon the policy choices made, but that a redistribution of standing charges to unit costs appears to be slightly progressive overall.

[1] All statistics taken from nationally representative research of 2,000 UK adults commissioned by National Debtline (run by the Money Advice Trust) and undertaken by Opinium. Fieldwork conducted 17-20 October 2023 - for more information, visit www.moneyadvicetrust.org/help-to-repay/

There will need to be further analysis carried out as to the characteristics of the groups affected and modelling done to show the profile of households that could lose out, before any decisions are made. It would help if Ofgem were to release the data regarding the architypes used in its analysis so far. The data within the paper is not presented in any detail at this stage and the process Ofgem have used to come to its initial conclusions could be more transparent.

We would suggest that Ofgem needs to consider each element of the standing charge including policy costs, operating costs and network and transmission costs, to decide whether it would be more appropriate for these costs to be moved to unit charges, or whether some elements such as legacy supplier costs should be removed altogether. It is not reasonable, in our opinion, to start from the assumption that all costs must be reallocated across consumer bills in some way rather than be down to suppliers to bear from their own resources, or to consider whether certain costs should be borne by government, perhaps through general taxation.

Ofgem needs to consider the impact of future net-zero policies on changes to energy usage, and the costs of electricity and gas for consumers in the light of its new net zero duty under the Energy Act.[2] Potential eco-savings need to be factored in, where it is policy for low usage savings to be encouraged or promoted through a change in use patterns. However, the standing charge limits the amount that people can reduce energy generally and could be a disincentive to do so.

As Ofgem says in the paper:

"*5.12 Shifting charging from unit-based to fixed charges may impact the incentives that customers have to use energy. Generally speaking, increasing the unit rate provides a stronger incentive to use less energy. Moving charges to standing charges rather than unit rates arguably weakens incentives for customers to reduce consumption."*

In addition, a cap on standing charges could result in benefits accruing to those who do not need any assistance, for example low users in their second homes, or people who have high usage due to extra costs of swimming pools and so on.

One element that appears to cause a sense of unfairness is the regional variation in standing charge costs, particularly in rural areas and in Scotland in particular. Whilst we understand that this is due to the higher costs of supply to remote areas, we believe Ofgem should consider levelisation of these costs across the UK.

[2] https://www.ofgem.gov.uk/publications/ofgem-welcomes-energy-act-getting-royal-assent#:~:text=The%20duty%20restates%20Ofgem's%20principal,to%20net%20zero%20by%202050.

Prepayment meters

We would suggest that Ofgem should look to alleviate the impact of standing charges on PPM customers in particular. These measures should be looked at immediately. The most egregious effects of the increase in standing charges have been felt by people who are generally in the most vulnerable and low-income groups.

Whilst the requirement to pay increased standing charges has been felt across all consumers, whatever method of payment is used, only PPM customers have to pay the standing charge before they receive any energy when they top up their meter. This has led, for example, to people being awarded a fuel voucher but finding that a substantial amount of their voucher has not given them a vital supply of energy but has gone on accrued standing charges. People who have self-disconnected or cut down the amount they top up their meter will find that they have accrued months of standing charges when they next top up, again meaning that their payment does not give them as much energy as expected, but just goes towards their standing charges.

Lower energy usage resulting in self-disconnection or very low amounts of top up payments on to the meter can be due to inability to afford to pay for energy, where people are endangering themselves and their health by not keeping their electricity running. People should be able to keep their fridges running, and have their heating on. There is a risk that people in these circumstances look like 'low users' within data and modelling, including for the purposes of determining standing charges policy. However, they are not really low users, but rather people who are forced by circumstances to use less energy than they need.

Whilst we recognise that any exemptions for PPM customers may increase charges for standard credit or direct debit customers, these groups do not suffer the same immediate effects. Their energy does not stop flowing until they pay back any standing charges arrears purely because of the way in which they pay for their energy.

While careful thought would need to be given to avoid increasing pressure on lower-income customers paying by standard credit or direct debit, we think there are a number of policy options Ofgem could consider for standing charges for PPM customers.

- Reallocating the standing charge to the unit rate for prepayment customers.

- Freezing standing charges in certain situations, such as preventing standing charges from accruing during periods of self-disconnection or a very low level of use.

- Consider seasonal charges such as an exemption on standing charges during the summer.

- Add accruing standing charges to arrears payments on the PPM account and set the meter to only collect affordable repayments on arrears or freeze repayments where unaffordable.

- Adjust the way in which top up payments are allocated so that the consumer receives energy up front and the standing charges are moved to the back of the charges on the meter.

- Consider whether the amount taken out for standing charges from a payment on the PPM be capped.

- Continue – and where needed, increase – supervision and enforcement work to ensure that vulnerable consumers are not using a PPM or have had a forcibly installed PPM in the new exempt categories.[3] For example, households which require a continuous supply for health reasons, and households with severe health issues including terminal illness or who have a medical dependency on a warm home due to illness.

Vulnerable high user groups

When considering moving some or all costs from the standing charge to unit costs, it is vital to consider an alternative failsafe for particular groups by way of additional bill support.

As Ofgem says in the paper:

"5.45 The difficulty in proactively identifying which customers are vulnerable adds a further element of risk to an un-targeted approach to moving charging to unit rates. Whilst existing tools such as the PSR register and smart meter data can help, it can be difficult to identify those customers who may have complex needs due to vulnerabilities. The impacts of self-disconnection, which may be severe, may not be obvious until serious detriment has materialised."

We understand it is generally the case that the PSR is not yet sufficiently comprehensive to identify people in need of extra help consistently or in all cases. We agree that it is difficult to identify people who have complex needs due to their vulnerabilities from the PSR alone. People may suffer serious detriment before their needs for extra help are identified.

Eligibility for the Warm Home Discount (WHD) could be taken as a proxy for eligibility for extra help. We recognise that recent changes to the eligibility criteria for WHD mean that some of the most vulnerable groups would not be included. This includes high energy users over pensionable age who have not claimed Pension Credit or people who are only eligible for disability benefits.

In some ways the standing charge smooths costs over the year, but a move to volumetric charges will mean that these costs are higher for those households over the winter at peak times.

[3] Prepayment meters consumer guidance | Ofgem

Common groups who may have higher energy use include the following.

- People who need to keep warm or need electricity due to a health condition, disability, or a terminal illness.
- Older people who may be more vulnerable to the cold.
- People who live in rural areas have higher network costs, and there is a regional disparity for Scotland in particular.
- Electric-only households such as people who live in flats with all electric heating perhaps through electricity storage heaters.
- People who live in poorly insulated, energy inefficient homes, typically who are more likely to be on a lower income in private rented accommodation.

We would suggest consideration of a cap on standing charges to put a final limit on what a household with unusually high costs due to medical costs and those on lower incomes with high energy needs are expected to pay towards standing charges.

Wider reforms

Addressing reforms for the standing charge alone is not a solution and there is a risk that the real debate on affordability more generally could get lost within this. We do not believe that the reallocation of standing charges costs between groups of consumers is adequate in addressing the fundamental issues of energy affordability. While we appreciate that solutions to this often lie outside Ofgem's immediate control, we would continue to urge Ofgem to do all it can to make the case to government for action on energy affordability and energy debt.

Other measures need to be considered as a matter of urgency to protect particularly affected groups of consumers and to address the affordability of energy more widely.

- A social tariff is vital to help ensure that people on lower incomes, and those who need to use more energy are able to afford this (and are protected from the impact of any reform of standing charges). We are disappointed that the promised consultation on a social tariff has not been published by the Government and hope Ofgem will continue to make the case for this as a matter of urgency.[4] Any social tariff model should mitigate the effects from standing charge reform on low-income consumers with high consumption.

[4] https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/reports-and-briefings/safe-at-home/age-uk-energy-public-policy-report-march-2023.pdf
https://www.nea.org.uk/news/solving-the-cost-of-living-crisis-the-case-for-a-new-social-tariff-in-the-energy-market/
https://www.citizensadvice.org.uk/about-us/about-us1/media/press-releases/social-tariff-now-essential-in-era-of-high-energy-bills/

- Substantially increase the amount of the annual Warm Home Discount payments and consider amending the eligibility criteria to boost its impact. Recent reforms have meant that some disabled households, potentially with higher heating costs, are no longer eligible.

- A temporary Help to Repay scheme as put forward by Money Advice Trust and a range of other charities.[5] This would provide eligible households with help to reduce what they owe in energy arrears through repayment matching and debt relief.

- Reform of the PSR and other data sources to improve the identification of need and to ensure that any targeted exemptions or mitigations for specific groups can be realistically put in place. The coverage of the PSR is disjointed, and inconsistent between suppliers and across utilities. We support the proposal for a universal PSR under consideration by the Department for Business and Trade in its "smarter regulation" consultation.[6]

- Acceleration of insultation, energy efficiency and retrofitting schemes for people in fuel poverty.

For more information on our response, please contact:

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[5] https://moneyadvicetrust.org/help-to-repay/
[6] Smarter regulation: strengthening the economic regulation of the energy, water and telecoms sectors - GOV.UK (www.gov.uk)

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