Energy Action Scotland response to the Energy Price cap: Additional debt costs review consultation.

__Energy Action Scotland Response__

Introduction

Energy Action Scotland is the national third sector membership organisation dedicated to ending fuel poverty in Scotland. Energy Action Scotland has been working with this remit since its inception in 1983, 2023 is our 40th anniversary, and we have campaigned on the issue of ending fuel poverty and delivered many practical as well as research projects to tackle the problems of cold, damp homes.

Fuel poverty is driven by four main issues, these being high energy costs, low disposable incomes, poor energy efficiency of homes and how energy is used in the home. In Scotland consistent with the definition within the Fuel Poverty (Targets, Definition and Strategy) (Scotland) Act 2019 there are over 1 in 3 households estimated to be in fuel poverty.[1] Almost 1 in 4 of Scotland's households endure extreme fuel poverty, simply unable to afford anything like the level of energy to maintain and protect their health and wellbeing.

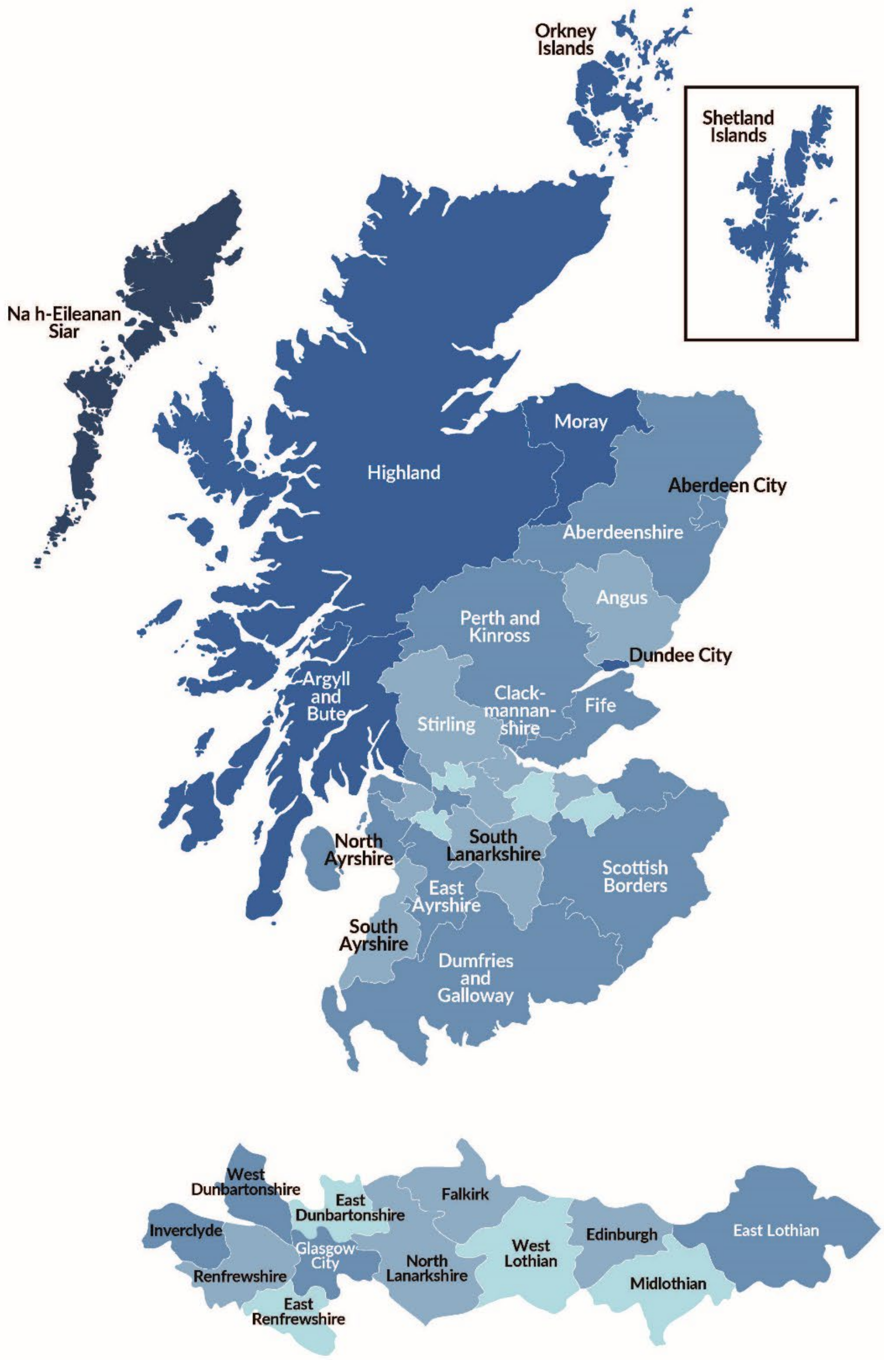
Fuel poverty is not evenly distributed in society and factors including geography and climate impact on communities whose residents may further be affected by medical and social conditions that magnify disadvantage. We are concerned when the distribution of energy industry costs impacts disproportionately on households who are least able to achieve the levels of heat and power sufficient to maintain health and wellbeing.

Energy Action Scotland's response focuses primarily on those areas that it considers may impact most on fuel poor and vulnerable consumers.

We believe that in the current climate of persistent high energy costs and spiraling domestic energy debt it is counterintuitive to further deepen the burden on those least able to pay. We favour a Government led solution that is tax payer funded which we believe is fairer and more progressive than further burdening households with charges in their energy bills. It is widely acknowledges that apply costs to energy costs either through standing charges or price capped unit rates is regressive in that it impacts disproportionately on those with the lowest incomes, living in the poorest accommodation.

[1] Scottish Government, Scottish House Condition Survey 2021, published 31 May 2023 footnote fuel poverty section

FUEL POVERTY BY LOCAL AUTHORITY



Na h-Eileanan Siar	61%
Highland	51%
Argyll and Bute	50%
Moray	49%
Dundee City	48%
Shetland Islands	48%
Orkney Islands	47%
West Dunbartonshire	45%
Dumfries and Galloway	44%
Inverclyde	44%
Scottish Borders	44%
North Ayrshire	43%
East Ayrshire	42%
Aberdeen City	40%
Glasgow City	39%
Aberdeenshire	38%
Perth and Kinross	38%
East Lothian	37%
Fife	37%
Clackmannanshire	36%
South Ayrshire	35%
Angus	34%
Falkirk	34%
Renfrewshire	34%
South Lanarkshire	34%
Stirling	33%
Edinburgh, City of	32%
North Lanarkshire	31%
East Dunbartonshire	30%
Midlothian	29%
West Lothian	28%
East Renfrewshire	20%
Scotland	**37%**

Ref Scottish House Condition Survey fuel poverty estimates as at 1 April 2023

Background to our response

Energy Action Scotland is extremely concerned about the record levels of debt and arrears, by Ofgem's definition, in the market, recently reaching £2.6bn. In Scotland alone this must equate to a figure in the region of £300 million. Over £150 for every single household in the country. The growth in the value of domestic energy debt demonstrates that an increasing number of households are struggling to afford their ongoing costs of energy and are falling behind. With the majority of the £2.6bn figure coming from arrears, there is a clear need for energy suppliers to ensure that affordable repayment arrangements are being created. The overall figure of debt and arrears does not recognise the full extent of the debt risk in the energy sector, as many households are not captured by the definitions of debt which energy suppliers report. We therefore expect that the problem is far greater than it is depicted in this consultation.

The Money Advice Trust in recent survey work noted that more than one in five people (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). Two thirds (66%) say they will reduce how much they use the heating this winter. Meanwhile millions of people have sold personal possessions (9%, 4.7 million), used their overdraft (7%, 4 million) and turned to high-cost credit (4%) in an effort to stay on top of rising energy costs.

Debt can cause physical and mental harm to households[2], as they resort to extreme forms of self-rationing to maintain some level of control over energy bills. It also puts at risk supplier resilience, which could mean further harm to consumers if this risk is not addressed.

During winter 2023/24 Scotland reported increases in Winter Mortality and Excess Winter Mortality[3] which were higher than expected even within the context of falling life expectancy and increases in Infant Mortality[4]. This was the worst in 30yrs[5]. The impact of high and unaffordable energy costs increased the impact on low income households and households with underlying health conditions that required them to be in homes that should have been warmer and for longer.

[2] Money and Mental Health
[3] National Records of Scotland, Winter Mortality in Scotland, 24 October 2023 https://www.nrscotland.gov.uk/statistics-and-data/statistics/statistics-by-theme/vital-events/deaths/winter-mortality/winter-mortality-in-scotland-2022-23
[4] National Records of Scotland, Births, Deaths and Other Vital Events - Quarterly Figures: Third Quarter, 12 December 2023, https://www.nrscotland.gov.uk/statistics-and-data/statistics/statistics-by-theme/vital-events/general-publications/quarterly-births-deaths-and-other-vital-events/3rd-quarter-2023
[5] BBC Scotland, Scotland's Winter Death Toll the worst in 30 years, 24 October 2023 https://www.bbc.co.uk/news/uk-scotland-scotland-politics-67206579

Summary of our response:

The quantum of debt in the energy market has recently reached new highs. Ofgem, in this consultation, is proposing to increase the debt allowance in the price cap to ensure that suppliers can fund their activities, particularly regarding servicing debt. While this action is possibly necessary (due to the duties placed on Ofgem through the Domestic Gas and Electricity [Tariff Cap] Act 2018), it does not serve to solve the problem of mounting debt and will likely further increase the level of debt in the market, as it will mean that energy becomes even less affordable for households. It will further burden already indebted households with further costs in what is now little more than a vicious cycle.

Ofgem has sought a voluntary agreement with energy suppliers at the same time as releasing this consultation. This new agreement, signed by almost all energy suppliers covering 95% of the market, contains only two new provisions to help with debt. Whilst any new provisions are important and welcome, they will not have a material impact on the level of debt in the market. Energy Action Scotland recognises that it is largely out of Ofgem's remit to introduce policies that can reduce the overall level of debt. This consultation cannot in itself provide a solution to the record levels of debt. Ofgem though is the sector regulator and have responsibilities to consumers and must therefore consider what it is able to do, within its powers, to tackle levels of debt in the market on an enduring basis. We believe that this is an urgent consideration and that this should be addressed prior to decisions on additional costs to already struggling and barely struggling households.

A fairer approach to managing debt

Whilst we believe that introducing a new debt allowance is neither fair nor sustainable we appreciate that it may yet happen. If it does then it should be done on the fairest, most equitable manner. A manner that doesn't exacerbate the factors causing the proliferation of domestic energy debt. It therefore must go further than simply applying the most cost reflective route for minimal effort.

Since debt allowances in the price cap scale alongside wholesale costs, the absolute level of debt allowance has recently come down as wholesale prices have fallen. However, the way in which debt-related costs are allocated mean that some consumers, especially standard credit consumers, are paying significantly more than households on direct debit to pay for debt-related costs. Standard credit is the payment method where most of the debt costs faced by suppliers arise from, and the share of bad debt costs paid for by standard credit households is therefore a reflection of their cost to serve on an aggregate basis. However, since it is clear households on standard credit are most likely to be unable to afford their ongoing energy costs, we believe it is counter-intuitive to place the highest proportion of debt-related costs on standard credit households.

Applying an additional debt-related allowance to the price cap will undoubtedly hurt those households with the lowest incomes. It will push some households into fuel poverty, whilst pushing fuel poor households into even deeper fuel poverty and sadly in some cases destitution. We recognise Ofgem's view that the price cap must allow cost recovery based on the expected costs of a notionally efficient supplier, otherwise there is an increased risk of market exit(s). However, we feel this must be at worst done in a way to ensure the least-worst outcome for households with the lowest levels of financial resilience.

In absolute terms, there are more households who are fuel poor on direct debit than the other two payment methods combined. However, this does not mean that fuel poor households as a collective would be better off with an allocation of debt-related costs that favours direct debit customers. Households that pay by prepayment are most likely to be fuel poor, with standard credit the second most likely payment method to be fuel poor and direct debit the least likely to be fuel poor.

In this context, we note that Ofgem is proposing to recover costs equally over direct debt and standard credit customers, with zero recovery over PPM customers. We are also note that the proposal to recover through the unit rate only. We believe the proposed approach is the least worst option. We remain concerned for households with unavoidably high levels of consumption including those with essential medical needs and households where electricity is the energy input for heat.

Maximise the benefit for already indebted households

We recognise enduring support to tackle levels of debt in the energy market is a matter which requires government intervention. We feel it is important to stress here that such support is desperately needed. Debt levels have risen to a record levels and there is no national plan to manage this debt. This is putting households at risk and also putting the economic viability of energy suppliers at risk. When suppliers have failed in recent times this has resulted in higher costs for energy consumers. We believe that current debt levels are an underestimate as they fail to factoring in a significant proportion of households who pay by direct debit, but whose direct debit payment level is lower than the cost of their ongoing energy consumption. These households, in addition to households who pay using credit facilities such as credit cards – in some cases moving energy debt out of the market and becoming credit card debt – are not captured in the £2.6bn debt figure.

SCOPE, a national charity working with disabled people, estimates average levels of debt of £1800 amongst those that it supports. This is double the levels it saw in 2022.

The purpose of a debt-related allowance is to provide suppliers with the ability to recover costs for writing off debt, which is unlikely to be repaid. To add an additional allowance into the price cap should therefore correlate with an increased level of debt write-offs from energy suppliers. There should, therefore, be transparency over the level of these write offs so that stakeholders can see the impact that this significant extra funding for debt-related activity is having. As proposals stand, energy suppliers will receive income associated with debt yet households in debt will see no reduction in their individual debt levels. Perversely heavily indebted households may see their debts increase as they further struggle to afford energy burdened with this additional debt allowance.

The need for a plan to address domestic energy debt

Adding further charges to the cap will only serve to produce more debt in the market. But we understand the perception that the cap must allow suppliers to recover costs that would be incurred by a notionally efficient supplier. We recognise that there is a level of concern around suppliers' financial resilience. Market exits could result in a greater cost for consumers than the costs imposed by an additional debt allowance.

This consultation is itself a measure of the rising cause for concern. The fact that there is a need for an additional allowance demonstrates that debt risk is greater than ever. Ofgem has sought a voluntary agreement with energy suppliers at the same time as discussing the need for an additional debt related allowance. This new agreement, signed by almost all energy suppliers covering 95% of the market, contains only two new provisions to help with debt. While these new provisions are important and welcome, they will not have a material impact on the level of debt in the market.

It is important to recognise that this consultation cannot provide a solution to the record levels of debt. Ofgem must therefore consider what it is able to do, within its powers as the regulator, to tackle levels of debt in the market on an enduring basis. It equally should have an obligation to ensure that the measures it takes do not result in further detriment or harm to vulnerable households.

To our knowledge there is little evidence of this progressive and consistent support to help people repay or reduce their debt levels. Other sectors have demonstrated that there are other approaches to reducing debt.

Frazer Scott, CEO Energy Action Scotland

16 January 2024

Notes

1 For more information visit: www.eas.org.uk

2 Energy Action Scotland works alongside our sister charity National Energy Action to more fully reflect experiences across the UK.