



**OFGEM**

**REVIEWING THE POTENTIAL IMPACT OF COVID-19 ON THE DEFAULT TARIFF CAP: CAP PERIOD SEVEN WORKING PAPER**

**APRIL 2021**

[Fair By Design](#) welcomes the invitation to respond to Ofgem's consultation on reviewing the potential impact of COVID-19 on the default tariff cap.

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

For more information about this response please contact Carl Packman:

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**ABOUT FAIR BY DESIGN**

Fair By Design is dedicated to reshaping essential services, such as energy, credit and insurance, so they don't cost more if you're poor.

People in poverty pay more for a range of products including energy, through standard variable tariffs; credit, loans and credit cards with high interest rates; and higher insurance premiums, through postcodes considered higher risk. This is known as the poverty premium. We collaborate with industry, government, and regulators to design out the poverty premium.

Our Venture Fund provides capital to help grow new and scalable ventures that are innovating to make markets fairer.

The Barrow Cadbury Trust manages our advocacy work, and Ascension Ventures manage the Venture Fund.

## OUR RESPONSE

Each winter at least 11,400 people in the UK die due to a cold home.<sup>1</sup> Over the last five years, there have been an average of 35,562 excess winter deaths each year. National Energy Action estimates that approximately 30% of these are attributable to the impact cold homes have on those with respiratory and cardio-vascular diseases and the impact cold has on increasing trips and falls and in a small number of cases, direct hyperthermia.<sup>2</sup>

During the “Beast from the East” in winter 2017/18, this figure exceeded 17,000 who died because they were unable to keep warm.<sup>3</sup> These needless deaths are sadly just the ‘tip of the iceberg’ and many more people are suffering with poor physical and mental health due to inadequately heated homes. The resulting impact on health services is acute; costing the NHS between £1.4bn and £2bn every year, in England alone.<sup>4</sup> In too many homes people have to choose to eat or heat. People across the UK are adopting desperate coping tactics simply to keep warm.

In our joint report with National Energy Action<sup>5</sup> we quoted someone with lived experience who had to make this unenviable choice:

*“In the winter when I need to put more [heating] on then I do find it difficult to keep up with the other bills, if I want to, you know, eat and keep warm.”*

Another person spoken to for the report said:

*“I’m always struggling. I have done for the last 10 years. I’m always struggling with my bills. That’s an on-going thing, we’re always struggling to pay the bills, you know. But I do pay them.”*

These words show just how important it is that Ofgem sets the appropriate policies as we go into the winter months.

It matters that people pay a fair price for their energy, but it also matters that people can pay an affordable price to heat their home. It’s important for their welfare and safety, as well as reducing other knock-on costs to the NHS and elsewhere.

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<sup>1</sup> <https://www.ofgem.gov.uk/ofgem-publications/164300>

<sup>2</sup> This is in line with estimates made by the World Health Organisation (WHO) - [http://www.euro.who.int/\\_\\_data/assets/pdf\\_file/0003/142077/e95004.pdf](http://www.euro.who.int/__data/assets/pdf_file/0003/142077/e95004.pdf)

<sup>3</sup> In 2017/18, excess winter deaths exceeded 50,000 across the UK, and NEA estimates that 17,000 people died because they were unable to keep warm enough at a reasonable cost [https://fairbydesign.com/wp-content/uploads/2020/02/02\\_NEA\\_WHD\\_doc\\_v04\\_Front\\_8pgs\\_DOWNLOAD.pdf](https://fairbydesign.com/wp-content/uploads/2020/02/02_NEA_WHD_doc_v04_Front_8pgs_DOWNLOAD.pdf)

<sup>4</sup> Ibid

<sup>5</sup> Ibid

## **The impact of Covid-19**

Excess winter deaths were on the increase even before the Covid-19 pandemic. We anticipate that the impacts of the pandemic and lockdown will exacerbate those issues this year.

Looking at the evidence that Ofgem has presented in its working paper, we can see that Covid-19 has reduced customers' financial resilience and this should absolutely be taken into consideration when reviewing the default tariff cap and the cap for prepayment meter customers.

As Ofgem has noted:

- Unemployment is predicted to be higher than in 2020;
- The government furlough scheme will close at the end of September, which could increase the likelihood of some customers being unable to pay their bills;
- Reports from Citizens Advice in December 2020 have shown that 2.1 million households were behind on their energy bills at the time of the publication, 600,000 more than in February 2020;
- In 2020 around one in five consumers were worried about paying bills or their supply and a third of PPM customers were worried about topping up.

On the assumption that things will get worse for these energy customers' financial resilience before they get better, we think Ofgem has been correct to make sure that customer's interests are protected (as stated in the working paper).

## **The Default Tariff Cap**

The Default Tariff Cap will be extended until the end of 2021 providing protections for energy customers from excessive prices. Since its introduction in January 2019, the cap has saved customers around £1 billion a year, equivalent to around £75-100 a year for typical households on default energy tariffs.<sup>6</sup>

Despite the protections provided by the cap, additional protections are needed to ensure people have access to the household heat they need at a price they can afford. Schemes like the Warm Home Discount provide a lifeline for people who, even with price protections in place, need additional support to make sure they are comfortable in their homes.

Fair By Design – in agreement with National Energy Action – believe that additional developments are needed to support households most in need:

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<sup>6</sup> <https://www.gov.uk/government/news/11-million-households-to-make-savings-as-government-extends-cap-on-energy-bills>

- The UK Government work with utility companies on accessing the shielded patients list as a first step to provide targeted support, such as granting emergency top-up support, to the most vulnerable customers, and
- Section 36(3) of the Digital Economy Act be further expanded to allow local authorities, public sector health bodies, and energy network companies to undertake direct data matching access with the Department for Work and Pensions (DWP), independent of licensed gas and electricity suppliers. This way, schemes like the Warm Home Discount can be automatically obtained by customers (instead of on a first come first serve basis as is the case now).

### **Considerations of any adjustment to the cap**

In scope for this Ofgem working paper is whether any adjustments need to be made for period 7 of the cap to take into consideration additional costs due to Covid-19. Also, who should bear the costs of this adjustment if there is clear evidence of additional costs.

While we agree that energy suppliers' activities need to be sustainable during this period, we think there is reasonable evidence (shown above, relating to the financial resilience of energy customers) to show that higher costs for energy customers must be avoided.

We draw the conclusion that no further additional burdens should be placed on already struggling households, even if there is a material increase in the costs for suppliers to serve particular customers.

This is particularly the case for struggling PPM customers.

This is because any additional financial burdens on this group of consumers is likely to have much more detrimental impacts on them and create knock-on costs elsewhere (e.g. the NHS, as stated above).

As Ofgem states in the working paper:

“Low-income households have not been able to build any financial resilience (on average) during the COVID-19 pandemic ... Almost half of the population have experienced declines in household earnings of at least 10%, but declines are most severe in the bottom pre-pandemic income quintiles. We could expect that these low-income households would have low financial resilience in 2021 or even in 2022.”

On balance the resilience of suppliers is going to be much greater than that of customers, particularly low income customers. Therefore this must be taken into consideration on who must bear any additional costs to serve.

At the moment, the price cap rising has been justified on the grounds that the cost to serve customers has increased (e.g. through wholesale energy price changes).

That has meant default tariffs have risen evenly for everybody. We at Fair By Design believe that every effort should be made to curb price rises for those least able to afford it.

Rising bills for everyone (including those who are struggling) during this period might be more justifiable if we could guarantee that schemes (such as the Warm Home Discount) could balance out the rising cost of bills for low income households. This is because further protections through schemes would cover the impact of the changes.

But at the moment we don't believe we have this balance. Many energy customers do not have access to schemes like the Warm Home Discount despite being eligible. This means that one way to plug the affordability gap for struggling households is not yet available for all of those deemed applicable for it.

We know that the other way to plug the affordability gap is through consumer switching. However we also know that those who are the least well off (and those that have been the most affected, financially, during the pandemic) are also those least likely to switch suppliers. This is for multiple reasons, many of which completely unavoidable when we dig deeper, informed by listening to experts by experience on switching barriers.<sup>7</sup> It is just not an option for everyone.

We conclude that other considerations must be found instead. We support a period of cross-subsidisation from better off bill payers to those identified as being the least financially resilient. Such a cross-subsidy would cover the increased costs for those on PPMs since this is a useful proxy for those on low incomes who would struggle to manage with higher bills in the winter months.

### **Additional remedies to lower energy-related debts**

We echo our colleagues National Energy Action in calling for the following items to be addressed as a way of helping build up the financial resilience of energy customers now and into the winter months (which either relate directly to Ofgem's activities, or which Ofgem should similarly be calling for):

- Government should bring forward Breathing Space and extend the respite period offered and provide funding for payment matching schemes to accelerate the repayment of utility debts. The UK Government should also make contributions for payment matching schemes.
- Consistent 'Ability to Pay' and debt collection principles should be implemented across all essential household bills

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<sup>7</sup> For a detailed discussion on this, see pp.23-27 of our recent report on the poverty premium with the Personal Finance Research Centre at the University of Bristol: <https://fairbydesign.com/wp-content/uploads/2020/11/The-poverty-premium-A-Customer-Perspective-Report.pdf>

- Maintaining enhancements to Universal Credit and improving the application process. Delays in accessing universal credit payments have a material impact on utility debt build up. This relationship should be investigated by BEIS in conjunction with DWP.
- The UK Government, working with Ofgem, should encourage better UK wide working and engage with the Northern Ireland Executive and Utility Regulator (UR) to ensure vulnerable energy consumers in Northern Ireland benefit from a comprehensive and consistent response from the energy industry to COVID-19.

### **Payment flexibility**

In the unwelcome scenario where Ofgem’s decision on adjustments to the cap result in households (including struggling households) paying higher bills, innovation will be needed to help those customers shoulder the burden of those costs.

One of these innovations could be on payment flexibility: the ability for customers to be flexible on when they pay their bills, and on the amounts they pay at different times. This kind of innovation is currently being rolled out across consumer markets such as in utilities<sup>8</sup> and rent payments.<sup>9</sup>

While we do not think payment flexibility would entirely solve the problem of fair and affordable energy costs, it could be a tool to help customers manage higher bills at winter times without penalising them. Also to help suppliers properly serve customers who experience financial detriment at various times.

Request to Pay<sup>10</sup> works as an overlay on top of existing payments infrastructure to allow consumers to manage and settle bills between businesses and organisations.

How it works: for each ‘request’, the payer of a particular bill will be able to pay either in full, pay in part, ask for more time, or decline to pay and begin a dialogue with the requester (e.g. a supplier). This gives more control to the person being asked to pay, and also gives the biller (e.g. a supplier) all the information they will need to reconcile the payment when it arrives.

The benefits for customers is that effectively you can underpay and overpay at different times. This is helpful for households who have ‘lumpy incomes’ (for example those on zero hours contracts) to manage their expenditure in an efficient way over the year.

For energy customers in particular, it could help them overpay in the summer months (when bills should be lower) and underpay in the winter months to help with potential affordability challenges.

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<sup>8</sup> <https://www.requesttopay.co.uk/>

<sup>9</sup> <https://www.fincap.org.uk/en/evaluations/evaluation-of-the-supported-rent-flexibility-pilot>

<sup>10</sup> <https://www.requesttopay.co.uk/>

In relation to what is in scope for the present Ofgem working paper, if any decision results in higher bills for customers then this innovation could potentially help spread increased payment in a way that is better to meet the needs of consumers. However, of course, such an innovation need not be linked to this decision alone. Ofgem should consider Request to Pay as something that can be integrated into suppliers' own payment methods today (especially since we know the winter months are always more expensive for energy customers).

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