Response to Ofgem's consultation on additional debt related costs

2nd November 2023

About Fair By Design

Fair By Design is dedicated to reshaping essential services such as energy, credit, insurance and payments so that they don't cost more if you're poor – also known as the poverty premium. Fair By Design collaborates with regulators, government and industry to design out the poverty premium. Our Venture Fund provides capital/funding to grow new scalable ventures to innovate the market and design out the poverty premium. Ascension manages the Fair By Design Fund. Fair By Design is managed by the Barrow Cadbury Trust on behalf of a group of foundations.

In the context of the energy market, we believe that households on low incomes/living in poverty should not incur a poverty premium based on the way they pay for their energy.

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

For more information about this response please contact Maria Booker:
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Background

The default tariff cap ('the cap') came into force on 1 January 2019. The cap ensures that default tariff customers pay a fair price for their energy that reflects the efficient underlying cost to supply that energy.

Given growing levels of energy debt Ofgem has been carefully monitoring the evolution of debt-related costs relative to price cap allowances.

Ofgem has seen evidence of a gap between costs and the existing cap allowance in cap period 8-10a (April 2022 - June 2023). Ofgem is therefore issuing a policy consultation on whether they should adjust the price cap to account for these deviations between costs and allowance. Ofgem considers that it is in the interest of customers to allow suppliers to recover efficiently incurred costs, as suppliers going out of business ultimately increases costs for all consumers.

Summary

Fair By Design's response is driven by the desire to get rid of premiums that those on low incomes pay due to how they pay for their energy. We have therefore only responded to Qs 13-16.

Questions

13 Do you have any views on which payment method allocation option would be preferable?

Our preference is for option 1: equal allocation of credit costs on direct debit and standard credit, while allocating zero cost to PPM. This is equivalent to the cost split used in the COVID-19 true-up.

We do not think that any of the additional debt allowance should be allocated to PPM customers for the reasons Ofgem states. The evidence suggests that most PPM debt is accrued originally on credit meters (data from suppliers is based on current payment method not point of billing which means PPM customers could be showing a debt from before they switched to a PPM). Bad debt which originates from PPMs is primarily from the Additional Support Credit (ASC) being added to the meter which is never repaid. From October 2023 ASC has been recovered through a new allowance.

We agree that this option accounts for the fact that, at an individual level, a standard credit customer who pays their bill is no more responsible for higher debt-related costs associated with being on a standard credit meter than a direct debit customer who also pays their bill. Option 1 also recognises the limitations of the raw data not being based on the point of billing.

We would like to understand more about the interaction with Ofgem's "minded to" decision on the levelisation of charges for different payment methods when the decision is published in a few weeks time.

14 Do you agree with us allocating other debt-related costs (debt-related administrative and working capital costs) uniformly across payment method?

Yes

15 How should we apportion any debt-related costs allowance over the unit rate and standing charge elements of the cap only?

Our preference is for Option 2: allocate any debt-related costs allowance to the unit cost. Standing charges have risen significantly since 2021 and are of real concern to consumers on low incomes. One participant in a focus group we held in April 2023 told us how she was still paying standing charges for gas even though she was told it was unsafe to use her gas appliances and had stopped using them. We welcome the work Ofgem has started in response to concern about standing charges. We would like to see any debt-related cost allowance allocated to the unit rate only. This will avoid penalising low-income consumers who are trying to use the bare minimum of energy (often to the detriment of their health). Option 2 also recognises that debt scales with consumption.

16 How should we apportion any debt-related costs allowance between fuel and meter types?

We believe that any debt-related costs allowance should be allocated evenly between gas and electricity. There is no clear evidence or data to govern an unequal split. The way costs are allocated drives prices that most consumers find far too complicated to understand. We would therefore advocate for simplicity unless there is a clear rationale for a more complex solution.

For the same reasons, we would like to see the same unit rate uplift for both single and multi-register meters. This would mean that consumers would pay for this allowance in line with their consumption.