Consumer Scotland's response to Ofgem's Call for Input on the debt-related costs allowance in the price cap

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1. Introduction

Consumer Scotland is the statutory body for consumers in Scotland. Established on 1st April 2022 under the Consumer Scotland Act 2020, we are independent of government and accountable to the Scottish Parliament.

Consumer Scotland uses data, research and analysis to inform our work on the key issues facing consumers in Scotland. As the statutory body for consumers we work with business, the public sector and consumer champions to put consumer rights, needs and interests at the heart of markets, services and policy.

We welcome the opportunity to respond to Ofgem's Call for Input on the allowance for debt-related costs in the price cap.

2. Our response

Questions 1-3

For questions 1 – 3, Consumer Scotland does not have a position on whether the methodology adopted for the debt-related costs allowance in the price cap for 2022/23 resulted in an over or underspend, or to propose a specific methodology that should be adopted for 2023/24.

Primarily, as a consumer organisation, we would encourage Ofgem to adopt an approach to debt allowance in the price cap that is underpinned by fairness for consumers with consideration for affordability.

We would encourage Ofgem to adopt an approach which delivers, as far as possible, an affordable cost for consumers through the price cap mechanism, whilst also minimising the risk of a high burden of bad debt which will increase future costs for consumers.

This would mean that the allowance of debt-related cost is proportionate to supplier risk whilst maintaining the most affordable prices for consumer possible. For this reason, we are also generally supportive of the float and true-up approach adopted for the COVID-19 adjustment[1], which allows the market to continue to function whilst work is undertaken to determine the actual costs that suppliers incurred.

We would encourage Ofgem to take an approach that delivers parity of debt allowance within the price cap between payment types, including parity between direct debit and standard credit consumers.

Consumer Scotland welcomes the recent wider cost levelisation work to ensure that there is parity of cost between prepayment meter consumers and those on direct debit. As Ofgem's call for input acknowledges, the most recent cap period allowed for debt-related cost which represented 6% of typical dual fuel standard credit bills, 1% of typical dual fuel direct debit bills and 0.4% of dual fuel PPM bills.

Whilst Consumer Scotland understands that this is calculated on the basis of debt risk between payment types, this structure does not reflect a principle of fairness.

Consumer Scotland's evidence highlights that standard credit customers are more likely to experience affordability challenges when compared with direct debit consumers. With wider considerations of financial vulnerability, Consumer Scotland would suggest that standard credit consumers are more likely to be financially vulnerable when compared with direct debit consumers.

Our recent data has shown:

- Forty-six per cent of standard credit consumers reported it was difficult to keep up with their energy bills compared with 30% of direct debit consumers and 62% of PPM consumers
- Forty-five per cent of standard credit consumers reporting they had cut back on food shopping to afford their energy bills compared with 33% of DD consumers and 53% of PPM consumers
- Twenty-three per cent of SC customers said they had to borrow money from friends or family in comparison to 9% of DD consumers and 27% of PPM consumers
- Sixteen per cent of SC consumers said they had reduced payments or fallen behind on their energy payments compared with 6.3% of DD consumers

In terms of our evidence, as well as wider financial vulnerability,[2], standard credit customers are often more likely to be closer to prepayment customers in terms of their behaviour and affordability. In future, we would like to see parity of debt-related allowance between Direct Debit and SC consumers. This change to the debt-related cost allowance has been supported by wider consumer groups and charities. Recently, Fair by Design called for parity of cost for those on standard credit including the removal of extra charges that low income consumers face for paying on receipt of bill[3]. One step towards fairness of costs between payment types is fairness of debt-related cost distribution.

However, within any change to the distribution of debt-related cost allowance between payment types, we would not want to see any increase in the debt-related cost allowance for prepayment meters. We would support maintaining debt-related costs for PPM customers at a similar rate to the current arrangements (i.e., 0.4%), given PPMs are provided to prevent high build-up of bad debt alongside the financial vulnerability of PPM consumers.

Questions 4-10

We would encourage Ofgem to incorporate the impact of market developments within the debt allowance but with due regard for affordability

Consumer Scotland agrees that there is a need to consider the impact of recent market developments. This includes the Energy Bill Support Scheme (EBSS), the extension of the Energy Price Guarantee (EPG) to the end of June 2023[4], and changes to the practice around involuntary prepayment meter installation. However, we would like to highlight that although the EBSS/EPG interventions are likely to have lowered debt-related costs incurred by suppliers, this has to be viewed within the wider context of the cost of living crisis.

Our recent research[5] has shown that although the government support prevented a worsening crisis, it maintained a baseline of low levels of affordability among consumers. One-third of consumers reported that we not managing well financially, 35% reported that it was difficult to keep up with energy bills and 68% reported that they were rationing their energy use. Therefore, there may be more customers in debt due to the wider cost of living crisis.

Consumer Scotland supports changes to practice around involuntary prepayment meter installation, particularly the moratorium on PPMs and development of a Code of Practice. We acknowledge that this is likely to have increased suppliers' debt-related costs and potentially resulted in debt beyond what was assumed by the modelling in the price-cap.

Similarly, new responsibilities on suppliers in the Code of Practice[6], such as ten attempts at consumer contact, are likely to be additional to previous assumptions, and will therefore have an effect on the allowance where the costs incurred are considered to be debt-related administration.

However, as above, the increased debt burden due to the moratorium may have been off set, to some extent, by the decreased debt risk as a result of the EBSS/EPG. On that basis, we would favour an approach to the debt-related costs allowance which recognises that government support interventions have reduced the debt risks for suppliers and therefore sets a future direction that improves price protections for consumers, limiting any unnecessary costs on bills.

We would support the expectation of best practice debt collection across all payment methods, not only PPM.

Consumer Scotland welcome the recognition in the Call for Input that an efficient supplier should use other mitigations in line with debt management best practice. Whilst this is quoted within the context of changes to the process for involuntary prepayment meter installations, Consumer Scotland propose that debt management best practice should apply to all debt accrued across all payment methods.

We would support the consideration of discretionary credits on reducing the levels of debt burden for suppliers as well as the value of debt-write offs from energy trusts.

Whilst we would expect Ofgem's supplier Request for Information to capture information on the supplier-led schemes, such as the value of debt write-offs from energy trusts, it is important also to consider how non-repayable discretionary credit from other sources, such as charities and the devolved administrations, is likely to impact on debt-related costs. Within Scotland, the following non-repayable discretionary credits may have had an impact on levels of debt and need for debt-write off by suppliers:

- Fuel Insecurity Fund: Since 2021, the Scottish Government's Fuel Insecurity Fund has been used to direct consequentials[7] from the UK Government's Household Support Fund[8] to vulnerable households – applications for energy debt support are administered through the Home Heating Support Fund. Energy debt write-offs in the 2022-23 iteration of the fund totalled £6.08m, with an average pay-out of £733. Ninety-three percent of payments from the Home Heating Support Fund in this period were made to suppliers in the regulated market[9].

- Social Housing Fuel Support Fund: The second round of the Social Housing Fuel Support Fund[10], another initiative funded through the Fuel Insecurity Fund, issued 15,986 fuel vouchers to July 2022, at a total value of £783,314. Figures for the third round of the fund, which is currently underway, are due to be published in July 2023[11].

Questions 11-15

Consumer Scotland has not taken a view on questions 11 – 15, but we are comfortable with Ofgem working towards an October 2023 cap adjustment, if that is the decision taken.

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[1] Price Cap – Decision on the true-up process for COVID-19 costs | Ofgem

[2] Consumer Spotlight on Energy 2 | Consumer Scotland

[3] Fair-BY-Design-Payment-Systems-the-Poverty-Premium-May-2023.pdf (fairbydesign.com)

[4] Energy Price Guarantee - GOV.UK (www.gov.uk)

[5] Consumer Scotland (2023) Consumer Spotlight 2

[6] Involuntary PPM - Supplier Code of Practice | Ofgem

[7] In May 2023, the Scottish Government announced its own £10m extension of the scheme.

[8] Household Support Fund doubled to help most vulnerable tackle cost of living - GOV.UK (www.gov.uk)

[9] Stats provided by Advice Direct Scotland who deliver the Home Heating Support Fund

[10] Stats provided by the Scottish Federation of Housing Associations who deliver the Social Housing Fuel Support Fund

[11] Stats for another Fuel Insecurity Fund initiative delivered by Home Energy Scotland were unavailable at the time of writing.