StepChange response to Ofgem consultation on additional debt-related costs allowance

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Summary

StepChange Debt Charity is a specialist not-for-profit provider of debt advice and debt solutions supporting people across the UK. In 2022 over half a million (580,913) people contacted StepChange seeking debt advice or guidance with their problem debt, a 20% increase on 2021. 187,278 people completed full debt advice through our online and telephone service, a 9% increase on 2021.

In 2022, 30% of StepChange clients who pay an electricity bill were in arrears, averaging £1,272. 25% of those paying a gas bill were in arrears, averaging £874. Based on H1 2023 data, we estimate that one in four (24%) of StepChange advice clients has a pre-payment meter (PPM).

We welcome this consultation, which highlights that the ability of suppliers to deliver high standards of responsible debt collection and the energy funding model for suppliers are closely connected.

In the light of sharply increasing energy costs and levels of energy arrears, we are disappointed that the government and Ofgem have not acted urgently to provide temporary support to help people struggling with energy debts and make progress towards implementing a social tariff for energy. While the Winter 2023 Voluntary Debt Commitment sends a welcome message about the importance of supporting those struggling with energy debt this winter, in practice it offers very little practical support and is not a substitute for concrete policy commitments by government and Ofgem.

The mandatory PPM moratorium and Ofgem's subsequent revisions to consumer standards in license conditions and guidance reflects a welcome increase in expectations of outcomes for consumers struggling with energy debt. We fully support these higher standards. However, this consultation highlights that supplier funding is closely connected to suppliers' ability to meet high consumer standards. Put simply, providing forbearance and affordable repayment, and pausing debt collection from those in arrears in vulnerable situations, carries a cost to suppliers that must be accounted for somewhere in the funding model.

We note that Ofgem's analysis is that a minority of the present exceptional level of energy arrears is accounted for by the mandatory PPM moratorium (approximately £25 million each month against £2.6 billion) but that Ofgem expects 'further significant costs' to arise in the second half of 2023 from the moratorium. The clarifying and strengthening of safeguards against inappropriate mandatory PPM installation will presumably increase costs to suppliers that resume installation of mandatory PPMs.

It is very likely the true cost of responsible debt collection in the energy market has not yet become clear. Questions raised in this consultation, like the prospects of a specific levy mechanism for 'do not install' (DNI) customers, strongly indicate that the present price cap model does not enable suppliers to adequately protect customers in vulnerable situations. In fact, the proposals reflect the reality that the cost of supporting vulnerable and fuel poor customers is passed back to the same households through bills in a regressive way.

We strongly believe more holistic reform of the energy funding model is needed to deliver affordability to those at risk of fuel poverty, provide sufficient protection and assistance to those struggling with energy debts, and to properly meet the cost of responsible debt collection.

We do not have sufficient evidence to comment on the detailed price cap design questions raised in this consultation. However, we note some of the proposed options are likely to be significantly less detrimental

for fuel poor households than others. Our view is that in each case Ofgem should pursue the approach that maximises the benefit for, and minimises the cost to, fuel-poor households.

Responses to consultation questions

1. Do you consider that we should make a temporary adjustment to the price cap to account for additional debt-related costs?

No, we believe Ofgem and the government should pursue an alternative approach that based on a 'Help to Repay' model that would not only support suppliers to deal with bad debt but also helps customers with arrears to repay affordably. This temporary support should be complemented by a prompt process to consult on a social tariff, including a more holistic funding solution to ensure good outcomes for those struggling with energy debt.

The moratorium on mandatory PPM installation and subsequent revision of license conditions, followed by an urgent update to consumer standards in license conditions and the industry Winter 2023 voluntary debt commitment, each reflect gaps and weaknesses in consumer protections for those struggling or unable to pay for energy. These failures became more acute and obvious when energy costs increased significantly in a short space of time 2022, prompting action on longstanding issues.

This consultation has come about because, as standards of debt collection have been increased closer to a responsible level in the domestic energy market, it has also become clear that the true cost of responsible debt collection (and debt write off where appropriate) has not been accounted for in the price cap, requiring a series of adjustments by Ofgem. Yet, despite welcome progress through strengthened license conditions, our clients continue to experience poor practice among suppliers: at the time of this response, StepChange has also shared with Ofgem a summary of client experiences in the previous six months based on over 200 case studies of poor practice recorded by advisors. This includes failing to take account of vulnerability, failing to offer or accept affordable repayments and excessive contact, among other problems. Below are three brief examples illustrative of the experience of many clients:

> *The client's energy arrears had built up due to her late mum moving into her home in the last two months of her life. Due to her mum's terminal cancer, the client had the heating on all the time. The client's supplier has twice set up direct debits without her permission, taking payment for regular usage as well as arrears. The client told StepChange that her energy supplier had not been receptive to the situation, nor that the client has mental health issues. This experience compounded the client's existing mental health issues while she was also grieving. (April 2023)*

> *The client has arrears with her energy supplier, which suggested her direct debit be increased to £114 from £82 per month. The client cannot afford this as she only receives a state pension. She offered to pay £92 but this was declined, and her supplier told her to call StepChange. The client is stressed by the prospect of paying this amount as she would struggle to pay for food and other bills as a result. (August 2023)*

> *The client, who is vulnerable and dealing with several mental health conditions, has being receiving multiple calls a day from their energy supplier chasing debt. The client has informed the supplier of their vulnerabilities, but – despite subsequent assurances from the supplier that it would make contact less frequently – it continues to call repeatedly. The client has reported feeling*

that so much pressure has been put on them by the frequency of the calls that it has led them to attempt suicide on two occasions. (July 2023)

Our experience as a free debt advice provider supporting clients in vulnerable situations strongly suggests that there is considerable progress to make by suppliers to fully implement responsible debt collection practices. New standards requiring debt repayments to be affordable will reveal more cases where repayment must be lowered or stopped, crystallising more bad debt. This in turn raises questions about whether the current price cap is compatible with high consumer standards in the energy market.

We are disappointed that, despite broad consensus among consumer groups and suppliers that a new approach is needed, urgent progress has not been made towards a funding model, including a social tariff, that will support high standards of consumer protection in the energy market. The implication of the proposals for those like our clients is that they will continue to face low standards of support while paying more for their energy. We consider it a far better approach to recognise that the existing model does not deliver meet the essential criteria of delivering energy affordability or protect consumers against harmful debt collection practices and needs change.

Alongside a number of consumer organisations, we have noted with serious concern the high proportion of our clients who are struggling with energy debts and Ofgem's announcement that energy debt has reached a record level of £2.6 billion. We have urged the government to work urgently with Ofgem to introduce a temporary 'Help to Repay' scheme for people struggling with energy debt at the Autumn Statement, providing support to financially vulnerable households to repay energy arrears incurred during this period of high prices via repayment matching and debt relief, alongside concrete commitments to progress longer-term work on a social tariff.

2 Do you think that suppliers cost due to the moratorium on involuntary PPM installation should be included in the adjustment?

We do not have sufficient evidence to quantify the variation among specific suppliers in compliance prior to the mandatory PPM moratorium.

We note this question indicates an understanding that responsible practice should be designed into the price cap and supplier funding arrangements. This raises questions about the ambiguous position of additional commitments made in the UK Energy Winter 2023 voluntary debt commitment, including the implication of new policies for the use of High Court enforcement and County Court Judgements. If these steps are meaningful, they are likely to carry costs to suppliers. Without any adjustment to funding arrangements, it is not clear how much meaningful change to supplier policies can be expected.

3 Do you agree that any adjustment should be made using the existing price cap mechanism, rather than a bespoke levy or other new mechanism?

No, for the reasons stated above, we believe a new alternative funding mechanism should be introduced.

4 Do you have any views on whether it would be appropriate to explore a specific levy mechanism for DNI ('do not install') customers? This would be separate to any adjustment for additional debt-related costs.

We agree that the uneven distribution of DNI customers across suppliers should be given consideration in future energy price mechanisms. We note that this issue reflects the extent to which fundamental challenges linked to wide-reaching consumer vulnerability have not been fully considered in the design of present energy price regulation. We recognise Ofgem must explore solutions to get the best outcomes for

DNI customers in the short-term but strongly believe the domestic energy price framework requires a more comprehensive and holistic overhaul, addressing problems of affordability and wider consumer protection, to deliver good outcomes for customers in vulnerable situations.

5 Do you agree that we should make an initial float adjustment in April 2024, followed by a later true-up? Do you agree it should be included within the cap for a 12 month period? Do you agree that this allowance should be temporary only?

N/A

6 Should the debt-related costs allowance, if introduced for the April 2024 price cap, be subject to a later true-up, and if so, when should this adjustment occur?

N/A

7 Do you agree that we should carry out only one wider debt-related costs true-up?

N/A

8 Should the float allowance be uprated to account for inflation, or should we make no additional adjustments?

N/A

9 Do you agree with the proposed overarching methodological approach for estimating the existing debt-related costs allowance, and using it to determine whether there has been an over or under-allowance for debt-related costs in 2022/23?

N/A

10 Do you have any other suggestions of alterative methodologies or other factors we should consider for how to calculate the debt-related costs over or under-allowance in 2022/23?

N/A

11 Do you agree that we should consider each debt-related cost (bad debt, debt administrative costs, and working capital costs) in scope of this review?

N/A

12 Which, if any, of the benchmarking options do you favour?

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

The trade-offs discussed in this section of the consultation reflect the reality that all options create additional costs for people already struggling with bills and none will work perfectly for suppliers (because cross-subsidy can only happen within suppliers rather than through external mechanisms across the market). This illustrates why the present price cap model is not supporting good outcomes for the most vulnerable consumers.

Ofgem should pursue the option that has the least cost impact on fuel poor households. Our understanding is that this option 1 (equal allocation on direct debit and standard credit, and zero cost allocation to PPM).

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

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

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

We are unable to comment in detail on questions 14 to 16 as we do not have any way of judging the distributional impact of the options. Our view is that in each case Ofgem should pursue the approach that has the least cost impact on fuel poor households.

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