

National Energy Action (NEA) response to Ofgem Consultation on Strengthening Retail Financial Resilience and Statutory Consultation on Strengthening Direct Debit Rules



Action for Warm Homes

About National Energy Action (NEA)

NEA¹ works across England, Wales and Northern Ireland to ensure that everyone in the UK² can afford to live in a warm, dry home. To achieve this, we aim to improve access to energy and debt advice, provide training, support energy efficiency policies, local projects and co-ordinate other related services which can help change lives.

Background

Over the last year, energy prices have increased significantly, with the default tariff price cap being set at £1042 for the winter period of 2020/21, and now being set at £1971, almost doubling in the space of just 18 months. Ofgem's Chief Executive recently told the BEIS committee that he expects the price cap to rise again in October, reaching £2800³/year for the average direct debit customer. That is an increase in approximately 170%.

Since that intervention, the UK Government announced a series of measures⁴ in an attempt to mitigate the energy crisis for household who are the most vulnerable to the impacts of fuel poverty. This will largely mitigate the impact of the expected October price increase, but with energy prices already extraordinarily high, NEA still expects millions of households to struggle to keep warm this winter.

At the same time, Ofgem has looked to alter the methodology behind the price cap in order to reflect the greater levels of risk that energy suppliers face as a result of significant volatility in wholesale electricity and gas markets. While NEA is pleased that Ofgem has listened to some of our concerns, and limited quarterly changes to wholesale prices only, we are concerned that for the most part, the proposed changes will create additional costs in the price cap in the short term, exacerbating affordability issues this winter, regardless of their impact on bills in the longer term (through reducing supplier failures).

Our Response – Financial Resilience

NEA has consistently raised concerns about the balance in Ofgem's decision making when considering additional costs this winter against optimising costs in the future. This tension has been present in the provisional decision to move towards a quarterly price cap (which analysts predict will result in a price cap increase in January), as well as the changes in methodology for the wholesale elements of the cap. This tension is again apparent in the measures proposed to increase financial resilience in the market.

In general, NEA broadly agrees with the need to increase financial resilience, in particular through better protecting credit balances. Over the last year, in some cases because credit balances have not been ringfenced, our clients have been unable to access their balances if their supplier exited the market, often for many months. This problem was sometimes particularly acute – many households saved additional money into their energy account ahead of a winter during which they knew was going to be more expensive to heat their home. They were told that their credit balances would be protected in case of any supplier failure. However, where suppliers did fail, many households did not receive their balances for many months, after the heating season had finished. This left many without the means to pay for their energy, leading to energy debt. Our experience has shown that our clients often turned to energy rationing. These experiences are well documented in the Citizens Advice report 'Back from the Brink?'⁵.

We hope that the changes proposed in this consultation will ensure that this delay to receiving credit balances into new accounts is shortened, if not eliminated in the future. This should be one of the main desired outcomes when Ofgem drafts the licence conditions, if the changes are taken forward.

In principle, NEA supports the proposals, on the condition that they do not lead to an increase in the level of the price cap. NEA has consistently sought assurances from Ofgem that the price cap would not be increased as a result of changes to rules regarding resilience, but Ofgem, as of yet, have offered "no guarantees". This is in spite of the impact assessment (see table below) that was commissioned alongside this policy consultation showing that there would

be no negative price impacts from any of the proposals to disengaged customers (i.e. those who protected by the price cap), and indeed showing that disengaged customers would see various positive price impacts. If these changes were to increase the price of energy during an energy crisis, the outcome would be disastrous for consumers.

Table 7: Net benefits to each group in 'Partial Effectiveness' equilibrium view (£m/year)

	Customers of failed suppliers		Engaged customers with other suppliers		Disengaged Customers		Total Consumers	
	Low	High	Low	High	Low	High	Low	High
Cost of Insurance - CCB	(2)	(0)	13	22	34	46	45	68
Cost of Insurance - RO	(4)	(4)	7	7	27	28	30	31
Hedging	3	27	16	126	22	179	41	332
Additional Tariff Increase	(30)	(21)	(44)	(28)	0	0	(75)	(49)
Switching Costs	39	77	3	4	4	6	45	87
Admin Costs of Policy	0	0	0	0	0	0	0	0
Total	6	79	(6)	130	87	258	87	467
(£ per affected customer)	3	34	(1)	12	6	17	3	16
Total (social equity weighted)	6	76	(6)	125	90	269	90	469
(£ per affected customer)	2	33	(1)	10	6	17	3	16

Energy demand becomes very elastic at low incomes and high prices. This winter, we can expect both incomes and prices to be stretched well beyond what can be considered 'normal', with a skyrocketing wholesale price and real incomes squeezed by inflation. Every pound that the price cap increases by is likely to result in less time without heat in the home, and more time in the cold for the poorest in the country. The result of that, is not just miserably living at home, but the development and exacerbation of health conditions. Ultimately tens of thousands of households across the UK die each year because they cannot keep warm at home.

Our Response – Strengthening Direct Debit Rules

Over the last year, NEA has consistently seen bad practices emerge from across the energy market where it comes to the setting of direct debits. It has become not unusual for our clients to see their direct debits increased by their suppliers, with little or no justification (i.e. there has been no change in usage, and prices have not yet changed). We have also seen direct debits changed, when there has been a price increase, but far and above what could be reasonably expected.

NEA therefore welcomes the proposals to tighten the language in the supplier licence conditions, removing the "all reasonable steps" condition, and therefore moving towards an absolute obligation. This condition currently gives suppliers the chance to derogate themselves from the intent of the licence, and unfortunately this seems to be happening too frequently.

This winter will see the biggest rise in energy price that has been seen since Ofgem was instated the regulator of the market, with some analysts estimating a £1250 increase in price for the average customer. Ensuring direct debits are set correctly is therefore of utmost importance. NEA therefore urges Ofgem to move quickly with the implementation of this licence change, so that it can be in place before October 1st.

After this winter, prices will likely, at some point, drop significantly. If this happens, then this licence condition must work both ways, where direct debits drop in line with price, and do not remain high after prices fall. Any breach of the condition should be seen as serious. Principles based regulation relies on strong enforcement of such breaches, and therefore **NEA urges Ofgem to actively enforce this condition, both during this winter and beyond.**

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

² NEA also work alongside our sister charity Energy Action Scotland (EAS) to ensure we collectively have a UK wider reach.

³ Ofgem evidence to the BEIS Committee, 24th May 2022 <https://committees.parliament.uk/oralevidence/10331/pdf/>

⁴ Cost of Living Measures Factsheet, HMT, 2022 <https://www.gov.uk/government/publications/cost-of-living-support/cost-of-living-support-factsheet-26-may-2022>

⁵ Back from the Brink? How Consumers are still reeling from the energy market meltdown, Citizens Advice, 2022, <https://www.citizensadvice.org.uk/about-us/our-work/policy/policy-research-topics/energy-policy-research-and-consultation-responses/energy-policy-research/back-from-the-brink-how-consumers-are-still-reeling-from-the-energy-market-meltdown/work/policy/policy-research-topics/energy-policy-research-and-consultation-responses/energy-policy-research/back-from-the-brink-how-consumers-are-still-reeling-from-the-energy-market-meltdown/>