

TRADE AND INDUSTRY COMMITTEE INQUIRY

DEBT AND DISCONNECTIONS

Memorandum submitted by Ofgem

1. Ofgem welcomes the opportunity to contribute to the Committee's inquiry. Ofgem shares the Committee's concerns about the problems faced by customers who are unable, rather than unwilling, to pay their fuel bills.

INTRODUCTION

2. Disconnection of gas or electricity must be handled very responsibly by energy suppliers otherwise major distress can be caused for customers, and everyone is aware of the tragic circumstances of the Bates case. Reducing debt and disconnection is therefore a priority area in Ofgem's Social Action Plan.

3. However the ability, as a final resort, to disconnect customers is desirable so long as it is operated responsibly. The gas and electricity suppliers are very unusual in providing extensive credit to millions of customers. The threat of disconnection is a cost effective approach to enabling suppliers to persuade customers who are able but unwilling to pay to do so. An absolute ban on disconnections would increase the levels of non-payment and the costs associated with debt recovery. This appears to have been the experience in the water industry. As a result those who pay their bills regularly (which includes many of the fuel poor) would have to pay more to cover the bad debts incurred by others who simply refuse to pay. The extent of this would steadily worsen, as the incentive to pay energy bills reduced. This would not be in the interests of customers generally.

4. For the last two years, and working in partnership with others, Ofgem has been encouraging the industry to tackle the issues of debt more broadly—by seeking to prevent the build-up of debt in the first place and thereby reducing the need for disconnection.

5. Earlier this year Sir John Mogg, Ofgem's Chairman, specifically challenged the industry to do more to identify and prevent disconnection of vulnerable customers. Industry responded to this challenge by producing for consultation proposals for an additional safety net to protect vulnerable customers from disconnection. Ofgem was pleased the industry responded quickly and positively to the challenge. We are currently considering the responses to the consultation issued in April. The important challenge now for the industry is to deliver the commitments it has made to handle vulnerable customers more carefully.

THE ISSUES IN CONTEXT

6. Given that disconnection is the final stage in a debt recovery process, to reduce disconnections suppliers have to be proactive in managing the process as a whole.

7. Overall the level of disconnections at around 20,000 a year in total is a very small proportion of the number of gas and electricity customers. By contrast there are about 1.2 million customers repaying debts for each fuel type which highlights the fact that disconnection is very much a last resort but also that there is a need to consider the

process in the round. The regulatory framework for dealing with debt and disconnection is set out in supply licences (see Annex 1).

8. In seeking to address this issue the first step has to be for suppliers to work to avoid customers getting into debt in the first place. When a customer does get into debt suppliers are required to offer a payment plan and accept repayment at a rate the customer can afford.

9. Should the customer fail to repay the debt, often the second step is installation of a pre-payment meter to recover the debt. Only if a pre-payment meter cannot be installed is a supplier allowed to consider disconnection of a customer in payment difficulties.

10. Furthermore suppliers are already required by their licences to avoid disconnection in winter of customers who are known to be of pensionable age, disabled or chronically sick.

11. The new industry proposals, produced in response to Ofgem's challenge, involve establishing a further safety net, with more effort and procedures in place to identify vulnerable customers. They have also committed not to disconnect this group of vulnerable customers at any time.

12. The different stages in this process are considered in turn below.

MANAGING DEBT

13. As noted above, it is really important that suppliers take adequate preventative measures to avoid the build up of debt. Working jointly with energywatch, Ofgem have published good practice guidelines for suppliers to follow on the prevention of debt and disconnection. The guidelines focus on six key areas: minimising billing errors; identifying customers in difficulty; provision of energy efficiency improvements; flexibility in debt recovery; the offer of sustainable solutions to customers in extreme hardship; and help for customers who are unable to manage their own affairs. Suppliers have developed strategies based on the guidelines, and Ofgem will be reviewing progress at the end of this year.

14. Under the terms of their licence suppliers are required to issue codes of practice on payment of bills and guidance for the assistance of customers who may have difficulty in paying. These codes are designed to ensure that customers in payment difficulties are offered a range of help, to avoid the need to disconnect. The licence condition sets out specific issues that must be covered in the codes of practice such as the requirement to offer payment by instalments (for example, under Fuel Direct) and to ensure that debt repayments take account of the customers' ability to pay.

15. The supply licence also requires a pre-payment meter to be provided to a customer in payment difficulties where it is safe and practicable to do so. This should therefore always be considered as an option before disconnection.

16. As at March 2004 there were 3.6 million customers with an electricity pre-payment meter and 2.1 million with a gas pre-payment meter. However, of these only 0.5 million electricity and 0.7 million gas customers were repaying a debt.

17. As noted above, at March 2004 there were around 1.2 million customers repaying debts in both gas and electricity, although it is not known the extent to which these are the same customers. This is of the order of 5% of customers in each fuel.

DISCONNECTIONS

18. The number of domestic disconnections for debt over recent years is set out below.

	2000	2001	2002	2003
Electricity	300	375	995	1,361
Gas	16,500	26,088	21,780	15,973
Total	16,800	26,463	22,775	17,334

Note: The fall in disconnections in 2003 is partly due to British Gas stopping disconnections in the final quarter. This situation continued into the first quarter of 2004 when 189 electricity and only 632 gas customers were disconnected. There may therefore be an increase again as disconnection procedures are resumed by British Gas.

19. As noted above there are currently regulatory restrictions relating to disconnection of known pensioners during winter ("the winter moratorium"). In the case of Mr and Mrs Bates this did not apply because they were disconnected before the winter period. Normally when customers are disconnected for debt they are reconnected very quickly (two thirds of customers are reconnected within 14 days).

20. There are some circumstances in which it is not possible to install a pre-payment meter. In particular in relation to gas, to change the meter requires all gas equipment in the home to be checked. This is difficult to undertake, particularly if the customer is not present. This accounts for the higher rate of gas disconnections. Also some customers may have physical difficulties in dealing with a pre-payment meter, either because they cannot easily get out of the home to obtain credit, because it cannot be suitably sited, or because the customer would not be able to operate such a meter easily.

VULNERABLE CUSTOMER PROPOSALS

21. Following the Bates case, Sir John Mogg wrote individually to all suppliers challenging them to do more to identify and help prevent vulnerable customers from being disconnected.

22. In response to this challenge, working with the Energy Retail Association (ERA), suppliers have produced proposals for a vulnerable customer safety net^[23]. Ofgem and the ERA issued a joint consultation on 26 April on these proposals. These include a definition of "vulnerable", guidance from the Information Commissioner on circumstances where suppliers may inform social services if they are concerned for a customer's welfare, and additional checks a supplier must undertake if it suspects a customer may be vulnerable. Under the proposals, if a customer meets the definition of vulnerable, they will not be disconnected.

23. Ofgem welcomed the fact that the industry responded swiftly to the challenge it had set by producing proposals for consultation which showed a real commitment to identify and protect vulnerable customers. Over 20 responses were received and have been placed

on Ofgem's website. While most respondents welcomed the focus that was being given to this issue, a number of important suggestions were made which Ofgem expects the companies to incorporate in their proposals. These include the point that Social Services are only one of a number of possible agencies that can provide assistance and that suppliers should look to make arrangements in partnership with as broad a set of agencies as possible.

24. Issues were also raised by many of the consultees as to the appropriate scope of the "vulnerable" group. For example a number of the respondents questioned the position where someone other than the bill payer is vulnerable in the household. Ofgem's view is that suppliers need to look at the circumstances of the household as a whole. If it is clear that there are fit and able people in the house who can resolve the problem then the presence of a vulnerable person should not be an automatic protection against disconnection—but Ofgem would expect companies to be sensitive and take a cautious approach where there is any doubt.

25. Many respondents also sought to have the definition extended to cover other specific groups—all pensioners or children or those on low incomes. Ofgem is concerned that these are very broad groups—for example, there are seven million pensioner households—and to extend the definition more broadly in this way could leave suppliers with no cost effective way of recovering debt from a large group of customers. Moreover not all pensioners, for example, require protecting in this way.

26. Looking ahead Ofgem has made it clear that the big challenge now is for the companies to deliver. What matters at the end of the day is whether this proposal has a real effect on the thousands of individual decisions which suppliers take in this area each week. It will be a major challenge for the suppliers in terms of training staff to identify vulnerable customers and put reliable processes in place to handle their needs sensibly. But we welcome the commitment that they have shown to dealing with this issue to date.

27. Ofgem will be monitoring closely the implementation of these new arrangements and will visit each of the suppliers in the autumn to review progress. Ofgem hopes energywatch and other consumer groups will tell us if they find instances of the arrangements not being followed.

28. Ofgem considers that this is an area where a self-regulatory approach is appropriate—for it to succeed it is dependent on the goodwill and commitment of the companies. Ofgem is committed to avoiding unnecessary regulation, in line with the principles of better regulation. However if it finds substantial evidence that suppliers are not meeting the commitments they have made then it would be willing to consider a more formal regulatory approach.

CONCLUSION

29. The energy industry is unusual in providing significant credit to customers on low incomes. A challenge for the suppliers is how to encourage customers to give due priority to payment of their fuel bills and repayment of any debts that arise, whilst treating vulnerable customers sensitively. The threat of disconnection for non payment is an important incentive on customers to pay their bills. This is a cost effective way for suppliers to reduce build up of debt, and thereby of minimising the costs to consumers as a whole.

30. Of course, disconnection of such an important service must not be undertaken lightly. There are substantial constraints in suppliers' licences in relation to how this power can be exercised. Ofgem welcomes the commitment shown by the industry towards developing a self-regulatory solution. The challenge now for the industry is to reflect as appropriate on the responses received to the consultation before finalising their arrangements, and then to move swiftly to completing the implementation of the new procedures ahead of the coming winter.

Annex 1

STATUTORY FRAMEWORK

1. Ofgem's principal objective is to protect the interests of gas and electricity consumers. Ofgem also has to have particular regard to the interests of individuals who are disabled or chronically sick, of pensionable age, on low incomes or residing in rural areas. Ofgem must also have regard to the Social and Environmental guidance issued by the Secretary of State.

2. The right to disconnect for non-payment is provided in Paragraph 7 to Schedule 2B of the Gas Act, and Paragraph 2 to Schedule 6 of the Electricity Act. These provide that where a customer has not, after 28 days following demand for payment, paid all charges due, the supplier may, on giving at least seven working days notice, either install a prepayment meter, or disconnect the premises. The Rights of Entry (Gas and Electricity Boards) Act 1954 applies in the case of entry under warrant.

3. Condition 35 of the Electricity and Gas Suppliers' Licences requires suppliers to prepare and submit to Ofgem^[24] for approval a code of practice concerning the payment of charges by its domestic customers including appropriate guidance for the assistance of those customers who, through misfortune or inability to cope with gas or electricity provided on credit terms, may have difficulty in paying such bills. For such customers in payment difficulties the code of practice must include arrangements for:

- providing energy efficiency information;
- accepting payments deducted at source from social security benefits ("Fuel Direct");
- detecting when there is a problem;
- making repayment arrangements which must take into account the customer's ability to pay (which has to be properly ascertained); and
- where customers fail to repay debts on this basis, providing a pre-payment meter (where it is safe and practicable to do so).

4. Condition 35 (3) of the Electricity and Gas Suppliers' Licences states that, in the case of customers with payment difficulties, the licensee shall not cut off supply unless it has followed the procedures which it is required to cover in its Code of Practice (as described above).

5. Condition 35 (4) of the Electricity and Gas Suppliers' Licences states that licensees should, as far as practicable, avoid disconnecting customers with payment difficulties who are of pensionable age or who are disabled or chronically sick between October and March. Condition 37A of the Gas Suppliers' Licences specifically forbids disconnection of customers with payment difficulties who are of pensionable age, either living alone or with other pensioners, during that period.

23 http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/6893_8804.pdf

24 Under Condition 27 the supplier must also consult energywatch about its code of practice and must, at least once a year, draw the code to the attention of its customers. The supplier must also ensure that, so far as reasonably practicable, it complies with the code.