

## **ESNZ Committee inquiry on fairness of customer energy bills: a response from Consumer Scotland**

### **1. Introduction**

- 1.1 Consumer Scotland is the statutory advocacy body for consumers in Scotland. Established in 2022, we advocate for consumers in Scotland, and are accountable to the Scottish Parliament. Further information is available on our website.<sup>1</sup>
- 1.2 We welcome the inquiry on fairness in customer energy bills. We are aware that there are specific inequalities in how energy costs are impacting consumers. Our recent energy tracker briefing outlined the affordability challenges being experienced by certain groups of consumers in Scotland.<sup>2</sup>
- 1.3 It is important that consumers in vulnerable circumstances do not experience increased harm due to being unable to afford their energy bills. We have previously highlighted the need for additional targeted support for consumers struggling with energy affordability and energy debt.<sup>3</sup> We would emphasise that many consumers who use fuels other than gas or electricity to heat their homes are also struggling. These issues are likely to require action from both Ofgem and Government.
- 1.4 Beyond the immediate term response however, there is a longer term need to consider how inequalities can be addressed through market reform and policy. The objective should be to achieve a fair, inclusive energy market which reduces inequalities in billing and affordability. In this context, the reform of specific segments of the regulated retail energy market in isolation is unlikely to be as effective as a more systematic approach.
- 1.5 There is an opportunity to design an inclusive future retail energy market which is able to embed the experiences and expertise of consumers facing increased difficulty or disadvantage. This could enable the creation of a more innovative and inclusive market which works better for all consumers, whilst also providing a potential avenue to reduce vulnerability and enable a just transition to net zero.

### **2. What are the justifications for allowing or removing standing charges from energy bills?**

- 2.1 A proportion of the costs of energy supply are fixed and do not vary with the amount of a commodity that is supplied. If these costs were absorbed purely through volumetric charges, these fixed costs would be felt disproportionately by some consumers, whilst other consumers would avoid contributing an equitable share.

- 2.2 The justification therefore for allowing standing charges on energy bills is to ensure an equitable recovery of these costs.
- 2.3 Consumer Scotland has outlined our analysis on standing charges in our response to Ofgem’s call for input on standing charges.<sup>4</sup> However, we have provided additional information below to inform the Committee’s inquiry, which is broader in scope than the Ofgem consultation.
- 2.4 It is reasonable for the costs of the gas and electricity system in Great Britain to be paid for by the users of those systems. Efficiently incurred fixed costs must therefore be recovered from customers somehow. For end users, in practice this either means imposing a standing charge, or adding those costs to volumetric charges. Removing standing charges would not reduce the overall costs of the system; rather, it changes how those costs are recovered from end users, and the distribution of that cost recovery.
- 2.5 The challenging question is: how should fixed system costs be shared across consumers in a way that is fair? Ofgem’s analysis<sup>5</sup> highlights that placing more of the fixed costs of the system onto volumetric charges would mean that some consumers would avoid contributing an equitable contribution to the fixed costs of supply, whilst placing a disproportionate burden of those costs on other consumers. The former group would include some better off households with second homes or very energy efficient properties, whilst the latter group would include some vulnerable consumers with high energy needs. For example, disabled consumers who rely on high volumes of electricity for essential medical equipment.
- 2.6 The question about how system costs should be shared should not be conflated with the wider energy affordability question. The risk of trying to address broader affordability issues via reforming standing charges is twofold. First, the majority of ‘winners’ of reform are unlikely to see a meaningful difference made to overall energy costs; and second, that the affordability issue is simply shifted across different types of consumer.
- 2.7 Rather than trying to address affordability issues via the standing charge, the broader costs issue should be considered in two stages:
- First, determine the principles by which system costs should be shared across consumers, and use these principles as the basis on which to set standing and volumetric charges. Ofgem already does this, for example through its extensive Targeted Charging Review (TCR)<sup>6</sup>

- Second, design and implement appropriate energy affordability policy that protects consumers who most need support with their bills. Much of this role sits with Government
- 2.8 On this basis, Consumer Scotland supports Ofgem’s current approach to the sharing of fixed system costs. However, there are two important caveats to our support:
- First, this approach should be reviewed regularly and transparently – it is legitimate that analysis on the equitable way to share system costs depends on the make-up and quantum of those costs
  - Second, and more importantly, this approach has to sit alongside a more comprehensive set of government and regulatory policies to ensure that energy bills remain affordable for low income and vulnerable consumers
- 2.9 Consumer Scotland would also wish to highlight that any intervention on standing charges also needs to have regard to the distributional impact on consumers in Scotland of costs rebalancing.
- 2.10 For example, consumers in Scotland are likely to have higher heat demand due to the increased energy requirements over the course of the year. This is supported by National Energy Efficiency Data (NEED) which shows that the median gas consumption for dwellings in Scotland has been consistently higher than in England and Wales over the last decade, and 7.8% higher in 2021.<sup>7</sup> This is at least in part due to climate.
- 2.11 Scotland also has a higher proportion of consumers who use traditional forms of electric heating than the Great Britain average.<sup>8</sup> As higher than median electricity consumers, such consumers would lose out if a greater proportion of system costs were placed on volumetric charges than is currently the case. Electric heating users are considerably more likely to be fuel poor in Scotland compared with users of other heating fuels.<sup>9</sup>
- 2.12 In general terms, Consumer Scotland is supportive of a future energy market which offers a greater choice of tariffs, including innovative and inclusive energy services. These might make use of different tariff structures, or make greater use of assets to enable all consumers to participate in and take advantage of flexibility.<sup>10</sup> Reform of the retail energy market offers the opportunity to design a market which recognises and responds to the needs of all consumers, including those having a more difficult experience of the current market.

**3 Should companies be allowed to provide cheaper bills to those who choose to pay by direct debit?**

3.1 Consumer Scotland recognises that suppliers' billing costs are lower for consumers who pay by direct debit (DD) compared to consumers who pay by other means.<sup>11</sup>

3.2 However, Consumer Scotland's analysis is that these differences in billing costs should be socialised across consumers. Under these arrangements, DD consumers would not receive cheaper energy than non-DD consumers as a consequence of the payment method. We recognise that this presents an implementation challenge for Ofgem, in that it requires all suppliers to be made whole through extensive use of cross-subsidies.

3.3 Our assessment of the most effective approach to achieve fairness for consumers on this issue is based on analysis which shows that consumers who pay for their energy by prepayment meter (PPM) or standard credit (SC) are disproportionately more likely to be in vulnerable circumstances, have low income, and be in fuel poverty than consumers who pay by DD.<sup>12</sup> Switching to a DD payment is often not an option that is available to many PPM or SC consumers.

3.4 A potential disadvantage of full levelisation is that it may dissuade consumers from transitioning from SC to DD. However, there are other incentives for moving to DD for those consumers who are able to; more fundamentally, this potential disadvantage is outweighed by the equity case for levelisation.

**4 Are pre-payment tariffs necessary to deter fraud and theft and, if so, are the rules in forcibly switching people to pre-payment properly policed?**

4.1 A moratorium on forced installations of PPMs was introduced for all domestic gas and electricity suppliers in February 2023 and was lifted from November 2023 for suppliers who met the restart criteria set out and assessed by Ofgem.

4.2 In the interim period, Ofgem strengthened its Code of Practice for the involuntary installation of prepayment meters and made the Code part of suppliers' licence conditions.

4.3 Consumer Scotland welcomed the new Code of Practice, whilst making a number of recommendations for where it could be strengthened.<sup>13</sup>

4.4 It is critically important that the new Code of Practice is subject to rigorous ongoing monitoring, evaluation, and review of efficacy by Ofgem and suppliers, to ensure that it is fit for purpose and that it is improving consumer outcomes.

4.5 At the current time however, it is too early to be able to assess the impact of the new Code of Practice on supplier behaviours in relation to involuntary installation of PPMs, and associated reforms to the support offered to consumers at risk from self-disconnection.

**5. Should there be greater use of discounts on energy for those who live closer to energy infrastructure?**

5.1 Community benefits are a well-established and integral feature of investment in onshore wind in Great Britain, and are increasingly becoming a feature of the grid-scale solar PV and offshore wind sectors. They are an industry-led, voluntary initiative, designed to encourage and support a positive relationship between renewables developers and host communities.

5.2 Funded by billpayers, the funds provided can be used to finance anything the community deems appropriate and necessary for the area. This can include but is not limited to targeted energy affordability schemes, such as the local provision of fuel vouchers.

5.3 The UK Government has also recently been considering how it can speed up the delivery of electricity transmission infrastructure in Great Britain. It has proposed that impacted communities should be compensated by electricity billpayers for the visual impact of new electricity transmission infrastructure, for a period of ten years.<sup>14</sup> Unlike extant community benefits arrangements for renewable electricity generation, Government has proposed that this compensation should be provided directly to end users as an electricity bill discount.

5.4 Reforms currently under consideration by the UK Government through its review of electricity market arrangements (REMA) programme<sup>15</sup> could allow the market to reward demand located under the same Grid Supply Point (GSP) as excess generation, through the provision of lower wholesale prices.<sup>16</sup> Smart local energy systems<sup>17</sup> also hold the potential to enable lower cost 'local power for local communities', in a way that incentivises investment and behaviour change that helps keep system costs down for all.<sup>18</sup>

**6. Is it right to expect those in more remote areas of the country to pay higher amounts in standing charges?**

6.1 Ofgem's "Regional Differences in network charges" report provides useful context to consideration of the above.<sup>19</sup> It highlights wide-ranging regional differences in

electricity consumption; for example, average consumption levels for households in the north of Scotland are significantly higher than is the case elsewhere in Great Britain. The report also found that regional differences in electricity network charges are a principal driver of regional differences in electricity retail prices. To a lesser extent, the same was also found to be true of network charges for gas prices.

6.2 Qualitative research with consumers in Scotland has revealed that consumers are accepting of these differences once they are better informed of the reasons that underpin them, and appreciate that it reflects the different geographies of the network areas being served. The fact there are logistical reasons why the variation exists left a majority of participants feeling that while regional variations are not preferred, they are explained and justified by these factors.<sup>20</sup>

6.3 The UK Government has legislated to provide targeted billpayer cross-subsidy to electricity consumers in the north of Scotland, through the Hydro Benefit Replacement Scheme and the Shetland Cross-Subsidy, to reduce the network costs differential between the north of Scotland and other electricity distribution regions in Great Britain, and to protect consumers in Shetland from bearing the full costs of their unique circumstances as electricity consumers.<sup>21</sup>

## 7. **How should a social tariff be implemented to address inequalities in billing?**

7.1 The purpose of targeted financial support in any given market should be to alleviate the extent to which some consumers face affordability challenges in respect of their energy bills.

7.2 With energy prices remaining high in a historical context, the proportion of households who are struggling to afford their energy bills, and the proportion who are in fuel poverty, is also high. A priority for the UK Government should be to set out plans to provide a more comprehensive set of policies to improve energy affordability for those in the greatest need of support. There remains a need to support consumers struggling most, and an opportunity to consider how to improve the overall design of the energy market to better consider future affordability.

7.3 We have outlined below two key considerations regarding the inequalities that arise from the existing market design and the current system of affordability support. These are:

- inequalities in the application of the Warm Home Discount (WHD)
- barriers to data sharing

## **Inequalities in the application of the WHD**

- 7.4 The WHD is the main mechanism for delivering energy bill support to low income households in Great Britain. It delivers energy bill discounts of £150 to eligible households.
- 7.5 WHD legislation currently covers the period until April 2026. However, the unprecedented nature of the energy crisis has prompted considerations around the use of WHD architecture as a way to target and distribute additional support to energy consumers.
- 7.6 There are however particular issues to consider regarding how WHD operates in Scotland which may lead to differences in outcomes between consumers in Scotland and those in the rest of Great Britain.
- 7.7 Two groups of consumers are eligible for WHD. The first group (known as 'Core Group') are low income pensioner households in receipt of the guarantee element of pension credit. For this group, WHD operates in Scotland in the same way as it does in England and Wales.
- 7.8 Arrangements for the second group differ in Scotland from those in England and Wales (this group is 'Broader Group' in Scotland and 'Core Group 2' in England and Wales). The reason for this variation is that the data used to determine eligibility in England and Wales (produced by the Valuation Office Agency) has no equivalent in Scotland.
- 7.9 This means that, in England and Wales, households that meet the eligibility criteria for WHD – i.e. households in receipt of a qualifying low income benefit and living in a property with high energy need as identified by the VOA – receive their energy bill discount automatically from their supplier.
- 7.10 In Scotland, because the equivalent data on property energy need does not exist, eligibility is based on a less targeted set of socioeconomic characteristics (typically, being in receipt of a means tested benefit and having young children or a disability). Households that meet those socioeconomic criteria then have to apply to their supplier for a discount.
- 7.11 These differences in scheme operation therefore create inequalities in the types of consumer who are eligible in Scotland compared to England and Wales. For example, a low income couple living in a high energy need property might qualify for support in England but not in Scotland.
- 7.12 Moreover, the 'by application' nature of the scheme in Scotland creates inequalities between consumers in Scotland. Some eligible consumers can miss out because they

are unaware of the scheme, they don't apply within the relevant application window (which can be as little as a week for some suppliers), or because the scheme is over-subscribed by the time their application is submitted. The scheme operates on a 'first-come, first-served' basis, with eligibility criteria set in such a way that the number of eligible recipients is greater than the number of funded payments.

- 7.13 Given these issues, it is important that any future development of a revised, comprehensive policy to provide energy bill support to consumers across Great Britain recognises the challenges within the current arrangements for consumers in Scotland, and identifies an approach to achieve fair and consistent outcomes for consumers across Great Britain.

#### **Barriers to data sharing**

- 7.14 Regardless of mechanism, targeted financial support is likely to require data matching across multiple agencies in order to reduce administrative costs and maximise efficacy.
- 7.15 Presently, there are key challenges to data matching across devolved and reserved competencies. It is important that energy consumers in Scotland do not experience adverse outcomes in billing and in affordability support compared to consumers in England and Wales. If this is to be achieved, the single energy market in Great Britain must be able to interact effectively with bodies in Scotland delivering areas of devolved policy.
- 7.16 Data sharing remains a significant challenge and opportunity for the future design of the retail market. Specific examples of these unique challenges around data sharing include:
- Data sharing between agencies working on the Priority Services Register (PSR) with Social Security Scotland, for matching targeted financial support or PSR work to recipients of disability benefits, where there may be options for Department of Work and Pensions data – such as on recipients of Personal Independence Payment – in England and Wales
  - PSR data and barriers to sharing between electricity distribution network operators (DNOs) and the water industry, which is devolved in Scotland
- 7.17 More broadly, as we look to improve consumer outcomes across billing and the wider energy market, there is a need to ensure that data sharing works effectively, and utilises the same pathways (i.e. significant public interest data sharing and Digital Economies Act 2017 legislation) across Scotland as England and Wales, with no additional friction for consumers.



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- <sup>1</sup> [Consumer Scotland](#)
- <sup>2</sup> Consumer Scotland (2023) [Energy Tracker: Insights from latest survey, Autumn 2023](#)
- <sup>3</sup> Consumer Scotland (2023) [Letter to the Chancellor from Consumer Scotland Chief Executive](#)
- <sup>4</sup> Consumer Scotland (2024) [Response to Ofgem’s Call for Input on Standing Charges](#)
- <sup>5</sup> Ofgem (2023) [Standing Charges: Call for Input](#), ch5
- <sup>6</sup> Ofgem (2019) [Targeted Charging Review: Decision and Impact Assessment](#)
- <sup>7</sup> UK Government (2023) [National Energy Efficiency Data-Framework \(NEED\): consumption data tables 2023](#)
- <sup>8</sup> Ofgem (2015) [Insights paper on households with electric and other non-gas heating](#)
- <sup>9</sup> Scottish Government (2023) [Scottish House Condition Survey: 2021 Key Findings](#), ch3
- <sup>10</sup> Citizens Advice (2023) [Powering up participation: A guide to making smart energy technology more inclusive](#)
- <sup>11</sup> Ofgem (2018) [Default tariff cap decision, Appendix 8](#)
- <sup>12</sup> Ofgem (2023) [Levelisation of payment method cost differentials: a call for evidence](#)
- <sup>13</sup> Consumer Scotland (2023) [Response to Ofgem's call for evidence on prepayment rules and protections](#)
- <sup>14</sup> UK Government (2023) [Community benefits for electricity transmission network infrastructure](#)
- <sup>15</sup> UK Government (2023) [Review of electricity market arrangements](#)
- <sup>16</sup> Ofgem (2023) [Assessment of locational wholesale pricing for Great Britain](#)
- <sup>17</sup> Energy Systems Catapult [Smart Local Energy Systems](#)
- <sup>18</sup> For example: UKPN (2022) [Urban Energy Club: NIA project report](#)
- <sup>19</sup> Ofgem (2015) [Regional Differences in Network Charges](#)
- <sup>20</sup> Citizens Advice Scotland (2020) [Consumer Insights on the Future of the Gas and Electricity Distribution Networks in Scotland](#)
- <sup>21</sup> UK Government (2022) [Hydro Benefit Replacement Scheme and Common Tariff Obligation: statutory review 2022](#)