National Energy Action (NEA) supplementary response to the Business, Energy and Industrial Strategy (BEIS) Select Committee Inquiry on Energy Pricing and the future of the Energy Market

1. About National Energy Action (NEA)

1.1 NEA[1] works across England, Wales and Northern Ireland to ensure that everyone in the UK[2] can afford to live in a warm, dry home. To achieve this, we champion and deliver energy efficiency programmes, aim to improve access to energy and debt advice, provide training and co-ordinate other related services which can help change lives[3].

2. Our supplementary evidence

2.1 Since submitting our original written evidence, there have been two significant changes in the energy market which have a material impact on energy pricing. This supplementary evidence addresses these two issues: Ofgem's changes to the price cap methodology[4] and the UK Government response to the price cap increase.[5]

3. Ofgem changes to the price cap methodology

3.1 On the 4th of February 2022 Ofgem released a suite of decisions relating to the design of the default tariff price cap. These decisions included changes to the wholesale price methodology calculation, as well as ensuring that the price cap was fit for purpose regarding reformed ECO and Warm Home Discount schemes, and the increased Supplier of Last Resort costs. As part of these decisions, Ofgem decided that:

- There would be an additional £41 allowance for unexpected standard variable tariff costs - double the amount set out in the initial consultation.
- There would be an additional £8 for 'backwardation' costs - these costs were not considered at all in consultation phases.
- No reduction in avoided Contracts for Difference (CfD) costs, compared to a £20 saving in the consultation. This was explained as being because some suppliers hedge against their CfD cost exposure. NEA however contends that this doesn't seem a reasonable justification – the purpose of CfDs is to pass savings back to consumers at times of high wholesale prices and this hedge acts as a barrier in being able to credibly highlight renewables are reducing costs to customers during the current energy crisis.
- There would be an additional £12 to account for shaping imbalances - while these were in the range of the consultation estimate, suppliers should be less exposed to these risks if they had been at a more advanced stage with the smart meter programme or had been quicker to embrace half hourly settlement.
- Supplier of last resort costs will be repaid immediately and over the same period as usual – 15 months, instead of delaying payment or spreading payment over a longer period, as NEA and others had requested.

3.2 These changes will have an impact on the households that NEA supports. Every additional pound on an energy bill can make the difference between not heating their home or only one room. In addition to the changes above, there are increases to the costs of the Green Gas Levy of £2.69 per gas meter from April 22. These costs are exceptionally regressive as they are recovered on a fixed basis (through the standing charge) meaning all customers pay the same irrespective of their income, usage or payment type. The original reason given for this was there was no way to recover these costs on a usage or 'volumetric' basis. However, Supplier of Last Resort Costs for gas will be recovered on a usage basis, and NEA would expect the same to be achieved relatively easily for the Green Gas Levy and all the new allowances for the cap noted above, in particular the Supplier of Last Resort electricity costs.

3.3 NEA has also noted the allowance for smart metering for prepayment customers is set at negative as customers have been overpaying in the current period due to an overestimated number of smart PPM installs during covid. Despite this, the cost saving for smart meters are less than consulted upon, despite the fact that many legacy prepayment customers have not yet been offered a smart meter. For prepayment meters, the allowance is set at -£7.47, compared to -£10.46 in the consultation. NEA was disappointed in this development as we have previously found[6] that smart prepayment in aggregate could be saving customers a lifetime benefit of over £5bn to households and more than £1.4bn to energy suppliers, facilitating a reduction in 0.2THh/year in gas use, and 0.41TWh/year in electricity use, amounting to 130,000 tonnes of CO2 saved per year, while contributing 10,000 jobs to the economy.

3.4 In all, the price cap continues to set the maximum charges for prepayment users at a higher rate than for those with credit users. However, this was not always the case. Previously, Ofgem ran a price cap from 2017 to the end of 2020 for customers using prepayment meters (the Prepayment Meter Price Cap). Ofgem then combined that tariff with single Default Tariff Cap from 1 January 2021. This decision was contested by NEA at the time as we were given guarantees from the UK Government and Ofgem that this wouldn't happen (see Annex 1). Unfortunately this commitment was not honoured, and prepayment customers have had their protection subsumed into the wider cap, ultimately meaning that they have had to pay higher policy costs, particularly for smart metering and more for wholesale costs. If these households had stayed on the more beneficial prepayment price cap, NEA estimates that they would have been between £60-100 better off per customer or in aggregate £270m better off per year from April. As a result, the recently announced mammoth rises are now most stark for PPM customers, despite many of these households already being indebted and more likely to be living on the lowest incomes. NEA estimates that prepayment customers are going to face additional energy costs of more than £3bn per year from April (£200m more compared to DD or SC customers). This outcome could have been partially offset had the decision not taken to roll the bespoke PPM cap into the wider cap.

4. Government response to the increased price cap

4.1 In February, the energy regulator Ofgem confirmed average energy bills for Direct Debit and Standard Credit customers across Britain could soon reach up to £1971, an increase of over 54% compared to bills today. The rises are even higher for over 4.5 million customers on prepayment meters, up to £2,017, an increase of over £708 compared to bills today despite many of these customers already being in severe debt.

4.2 This means that the cost of heating an average (gas heated) home will have doubled in 18 months. NEA estimates that the number of households in the UK living in fuel poverty will also soar from 4 million to 6.5 million households across the UK in six months from October 2021 to April 2022.

4.3 In response to the increased level of the price cap, the UK Government released plans for three new policies to support households:

- A £200 rebate to all households, paid in the Autumn, and recouped from bills with £40 instalments over 5 years. This will be paid through electricity bills
- Council tax rebates for bands A-D, averaging £150 and covering 80% of homes
- £144 million of discretionary funding for billing authorities to support households who are in need but are not eligible for the Council Tax Rebate, known as the Discretionary Fund.

4.4 NEA believes these proposals are woefully inadequate compared to the scale of the challenge. The £200 energy bill rebate will have to be repaid by households through their energy bills, which is an inappropriate way of supporting the poorest households, and risks piling upwards pressure onto bills that are predicted to skyrocket even further in October, with some saying that prices could reach £3000 for the average household. The council tax measures, while better in some ways, also fall well short. The sum of money is overshadowed by price increases and could be subsumed by increases in council tax rates, and NEA remains unconvinced that the hundreds of thousands of low-income households that are out of scope of the rebate (because they either live in higher banded homes or are already exempt from council tax) will be able to access the discretionary support. This leaves a gap of over £500 per year in April 2022, compared to

October 2022, for households that use prepayment meters even when the new energy crisis measures are considered. The outcome of this will be devastation to health, wealth and wellbeing' for millions of the poorest households of no further action is taken.

4.5 Additionally, NEA is concerned that not all households that use legacy prepayment meters will have access to the £200 bill rebate support yet will still have to pay it back through the levy. In a similar scheme, the General Electricity Rebate, 10% of households using legacy prepayment meters were able to access support. Drawing on these numbers as an estimate, this could mean that between 200-250k households with legacy prepayment meters could struggle to access the rebate.

4.6 The recovery of costs is also an issue. The Government plans to recover the costs through an increase in the standing charge for electricity. From April, this will be exceptionally high, at almost £200 per year in some regions. An additional £40 per year on the standing charge would be particularly painful for prepayment users, who will find it much harder to maintain a positive balance (this is because if their meter runs out of credit and they are unable to top up, the standing charge accrues as debt which needs to be cleared before positive credit can be achieved again). NEA is therefore worried that the large increases to PPM customers' bills will mean more people are off supply for longer periods of time.

4.7 NEA therefore recommends that the Government reform the £200 energy rebate, exempting the 2 million legacy prepayment households from repaying the rebate through a levy. This would be easy to administer – there is a separate price cap level for legacy prepayment users, and would come at a relatively low cost to the treasury (~£400m).

4.8 This action, on its own, will not be enough to help fuel poor households through the energy crisis. Government must provide additional deep targeted support as NEA set out in our original submission.

Annex 1 – Letter from Lord Henley to Lord Grantchester, 2018

Lord Grantchester

House of Lords

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22 June 2018

Dear Lord Grantchester,

I am very grateful for your continued interest in the actions of Government in protecting consumers, and for your support for the Domestic Gas and Electricity (Tariff Cap) Bill.

When we last met, we discussed protections for vulnerable consumers.

Firstly, we're working on information sharing to help better target assistance for those in fuel poverty.

On 17th May the Government laid the Digital Government (Disclosure of Information) Regulations,[1] before Parliament. That affirmative statutory instrument is designed to enable specific public bodies to share information to improve the provision and targeting of public services to benefit individuals and households. This includes the ability to share information for the alleviation of fuel poverty. The Regulations are scheduled for debate in both Houses on 25 June.

The new powers will enable the Government to share information with energy suppliers, so they can more readily identify households in need and provide support to those who are eligible. This support is specified in the list of fuel poverty measures in the Act and amending Regulations. It includes the Warm Home Discount (WHD), Ofgem's Safeguard Tariff and the Energy Company Obligation (ECO).

Secondly, on the matter of whether Ofgem's Safeguard Tariff will remain in place alongside the new price cap proposed by the Bill, I can confirm that Ofgem is proposing to keep the Safeguard Tariff in place if the new price cap is materially higher (i.e. gives less protection) than the level of the Safeguard Tariff. Ofgem have also committed to ensuring that vulnerable consumers are on the cap that gives them the highest protection, to ensure these consumers do not lose out when the wider price cap comes into effect. As I am sure you're aware, the existing Pre-payment Meter (PPM) Cap will be unaffected by this Bill and will be retained subject to a review of its duration by the Competition and Markets Authority (CMA) in 2019.

Thirdly, you also raised whether powers were required to allow a further price cap for vulnerable consumers to be brought after this cap has ceased. I can confirm that Ofgem already has the

[1] Link to Draft Digital Government (Disclosure of Information) Regulations 2018: https://www.legislation.gov.uk/ukdsi/2018/9780111169445/pdfs/ukdsi_9780111169445_en.pdf

power to protect vulnerable consumers in this way as evidenced by the extension of the pre-payment meter cap to Warm Home Discount customers by licence modification.

You may recall the comments made by Dermot Nolan, Ofgem CEO, to the Committee during the Bill's pre-legislative scrutiny on the ongoing support Ofgem may provide to vulnerable consumers upon the removal of the price cap. When asked whether a price cap or other protection may be needed for vulnerable consumers upon the removal of a market-wide price cap, Mr Nolan responded "*In my view, yes…I would envisage a very possible situation in which if a full, market-wide price cap was removed, Ofgem would continue with the price cap for vulnerable consumers*"[2].

I hope you find these points useful. I would, of course, set these out clearly in my response to any debate on these matters at Report on 27 June.

Yours sincerely,

THE RT HON LORD HENLEY

PARLIAMENTARY UNDER SECRETARY OF STATE

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[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] A major recent focus for the charity has been NEA's Health and Innovation Programme (HIP) which was a £26.2 million programme to improve energy efficiency within fuel poor and vulnerable households in England, Scotland and Wales. Launched in April 2015 by NEA as part of an agreement with Ofgem and energy companies to make redress for non-compliance of licence conditions, it remains the biggest GB-wide energy efficiency programme implemented by a charity which puts fuel poverty alleviation at its heart. For more information on HiP visit: https://www.nea.org.uk/hip/

[4]Overview of 4 February 2022 Price Cap decisions, Ofgem, 2022 https://www.ofgem.gov.uk/publications/overview-4-february-2022-price-cap-decisions

[5]
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1052719/Energy_Bills_Rebate_updated_factsheet_v2_.pdf

[6] Maximising the Smart Meter Rollout for Prepayment Customers, NEA, 2021v

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[2] See Page 9 of the BEIS Select Committee Oral Evidence Session from 10th January 2018: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/business-energy-and-industrial-strategy-committee/prelegislative-scrutiny-of-the-draft-domestic-gas-and-electricity-tariff-cap-bill/oral/76719.pdf