Sustainability first

Viewpoint

The independent charity and think tank shaping sustainability policy and regulatory agendas for UK utilities, for the benefit of consumers, citizens and the environment.

Consumer Vulnerability:

Given Covid-19 and Net Zero, what should the medium to longer-term approach be to ensuring affordability of essential utility services?

Back in 2009, the Queen asked London School of Economics how "financial wizards" failed to head-off and "foresee the timing, extent and severity of the financial crisis". The then response from eminent economists was, "In summary your majesty while it had many causes, [it] was principally a failure of the collective imagination of many bright people..."[1].

As we start to think about how we respond to the longer-term financial impacts of Covid-19, and linked to that how we can best ensure that essential services such as water, telecoms and energy are affordable for citizens in the future, we must challenge ourselves not to fall into this trap again. That is the trap of 'group think' and 'collective failure of imagination' when it comes to exploring the potential scenarios, options and the solutions.

The full and longer-term impact of this pandemic on customers' ability to pay their utility bills, and therefore access essential services, is of course not yet known and won't become clear for many months. For water companies with half yearly billing cycles, this is especially the case. What is known is that increasing numbers of households are facing a decline in income, maybe for a short time, possibly on a more enduring basis. At the same time, lockdown at home, health and hygiene challenges, and remote working means greater domestic usage of water, telecoms and energy. For those customers who pay according to usage, this will result in higher bills unless action is taken.

We will see an increase in the *breadth* (the total number of customers struggling to afford their bills) and *depth* of poverty– how much debt or difficulty individuals are in. There will be regional differences in affordability levels and potentially certain segments of society such as young people, those with larger families, and disabled households, impacted more than others. Importantly, action taken on affordability in one sector will impact debt levels in another.

These are the facts. Aka a rocky road ahead and the need for a collaborative solution that recognises the interdependencies.

But there's not just the impact of Covid-19 to consider when thinking about the way forward. As our new Sustainability First Briefing on the *Social and Distributional Impacts of Decarbonisation and Climate Adaptation in the UK* highlights, climate change impacts, the path to zero-carbon and the smartening of our water and energy networks *will* have distributional impacts. There will be winners and losers from upcoming changes with some customer segments and communities in our society benefitting and others potentially worse off financially.

At present it seems consumer groups, regulators, and government are united in praise for the positive steps taken by utilities during this crisis. There is support from Citizens Advice and National Energy Action (NEA) for energy suppliers abiding by the BEIS principles – these are commitments made by companies to identify and prioritise customers at risk, and support those who are financially impacted either directly or indirectly by Covid-19. There were similarly initial words of welcome from the statutory watchdog Consumer Council for Water (CCW), for water company action.

We've seen a lot of good company practice. For example, use of payment breaks, halting of debt collection processes, extension of prepayment meter (PPM) non-disconnection periods (times when customers can't be cut off) and top-up credit provided (though not without practical difficulties for non-smart PPMs). Companies such as EDF Energy and Cadent Gas have also set up or extended hardship funds and

[1] http://wwwf.imperial.ac.uk/~bin06/M3A22/queen-lse.pdf

emergency grants to individuals / community projects.

While it seems that in practice some support is not always easily available to customers, or being provided consistently by all companies (indeed the same consumer groups and the Guardian newspaper have already flagged problems) as 'industries', water, energy and telecoms/internet services provided a timely commitment to help relieve the immediate financial burdens on customers.

As with any crisis though, Covid-19 is shining a spotlight on what works well within these sectors, but also where there are weaknesses.

On the positive side we should recognise that GB utilities are pretty good at responding to short-term crises, and while their approaches have not always been strategic, to varying degrees many have demonstrated a more public purpose ethos. Despite all the challenges, for the most part, water and energy continue to flow, and every day I marvel (let's hope I'm not tempting fate here) that our telecommunications systems are still functioning. Much vilified utilities have received relatively little credit for this in mainstream media, and I was sad to hear that some frontline staff have faced abuse for carrying out their essential works.

There has been a real desire as well from distribution and transmission companies to play a direct and indirect role in supporting the communities they serve. Schemes such as the collaborative community fund, supported by Anglian, Thames Water, Affinity, South East Water and UK Power Networks and jointly commissioned PWC research, have also demonstrated that when there is a will to do so (and less concern about competition rules) companies can collaborate at pace in the interests of consumers.

We should also acknowledge the strength of our system that does not allow customers who can't afford their water bills to be disconnected. In the US, an estimated 15 million household are without water – 'shutoff' - facing increasing hardship, unable to wash their hands, leading to both individual and societal health concerns. This is not to underplay the problems faced by water customers who aren't disconnected but are still forced to ration use and face the stresses of, and fallout from, debt collection proceedings.

But the crisis has also further opened the cracks in consumer protections.

In particular, the inadequacy of our patchwork policy framework to support customers who struggle to afford their utility bills. And then there is the shame that remains in our country with tens of thousands of customers still self-disconnecting their energy, unable to heat their homes or water to cook their food.

Lockdown has exacerbated existing problems which have been flagged by consumer groups for many years: customers have low awareness of the support available to help them with their bills; even when they are aware of support they can find it hard to access; lack of consistency of financial support available between different companies even in the same sector makes it hard for advisors to communicate what help is available to those that most need it; companies require better training and access to data to effectively identify and support customers in financial difficulty; a range of parties lack access to up to date information about the changing help available and customers don't like asking for financial help from their creditors, but this is what they are being asked to do.

There is lots of good industry practice in supporting customers in financial difficulty, flagged by Citizens Advice[2] and we at Sustainability First,[3] but this is not uniformly applied.

In telecoms, the UK's major internet service and mobile providers, namely BT/EE, Openreach, Virgin Media, Sky, TalkTalk, O2, Vodafone, Three, Hyperoptic, Gigaclear, and KCOM have committed to: working with customers who find it difficult to pay their bill as a result of Covid-19; to remove data allowance caps on

[2] https://www.citizensadvice.org.uk/Global/CitizensAdvice/Energy/Covid-19%20Good%20practice%20for%20Energy%20Suppliers%20(180320).pdf

[3] Sustainability First's Energy for All Innovate for All report includes a good practice guide on tackling affordability which draws on cross-sector learning. https://www.sustainabilityfirst.org.uk/inspire

In addition, our report for UKWIR with CEPA on defining water poverty explores different approaches to reducing water poverty - https://ukwir.org/bq-defining-water-poverty-and-evaluating-existing-information-and-approaches-to-reduce-water-poverty

all current fixed broadband services; and "to offer some new, generous mobile and landline packages to ensure people are connected and the most vulnerable continue to be supported". However, currently with no dedicated statutory consumer watchdog and a seemingly publicly silent Communications Consumer Panel there is less transparency about what is happening in practice when customers can't afford their bills.

Existing solutions to support customers struggling with their bills are also unlikely to be fit for purpose longer-term

In responding to the immediate financial challenges faced by customers, water and energy suppliers have understandably drawn from their existing toolbox of consumer vulnerability solutions. After all a timely response was needed. But these solutions will likely not be fit for purpose for the medium to longer term. Payment breaks and PPM top-ups are designed to provide short-term relief not as enduring solutions. They are predicated on the idea that the customer is encountering a temporary problem and that things will return to normal soon. Where debt still accumulates approaches risk storing up problems for customers and businesses in the future. The bill still has to be paid.

In reality, even in 'normal' circumstances there is insufficient financial support to assist all that need it. **With Covid-19 it is not unrealistic to expect debt levels to soar making this even more challenging and the gap between help and need more of a chasm and less acceptable.**

Citizens Advice[4] reports that nearly four out of 10 (38%) of households have reported lost income because of this crisis. 6.3 million employees have been furloughed via the Job Retention Scheme – nearly a quarter of all employees, and the DWP has seen an unprecedented number of people applying for Universal Credit. The Office for Budget Responsibility has warned that unemployment could rise to two million in the second quarter, indicating that economic uncertainty is unlikely to be short-lived. This is against a context of over seven million people saying they have no savings to fall back on, whilst 10% of all adults in Great Britain reported they couldn't cover their costs for longer than a week if they lost their main source of income.

Water companies are exploring how they can adapt their existing social tariffs to provide more ongoing support – increasing the number of customers they help and changing the eligibility criteria to capture those hit by the crisis. But given the differences in willingness to pay (WTP) in different regions and the varying levels of poverty, they are in different places on this. Some are much closer to their WTP thresholds (the amounts customers agreed to pay). There is of course already a postcode lottery with the amount and kind of support available, and eligibility criteria varying by water company. This is on top of regional variation in water bills to start with including the £50 taxpayer subsidy for South West Water customers and significant variations in customer bill cross-subsidy levels. The system clearly needs improving.

The notion of bill cross-subsidy is based on an assumption that the majority of customers find their bills affordable and therefore can and are willing to help the minority. But if the number of customers struggling becomes a more sizeable proportion of the overall customer base, the approach becomes less workable. We also do not yet know how Covid-19 will influence customer willingness to pay for social schemes. Whether customers will become more sympathetic to cross-subsidy or if in fact there will be decline in charitableness as people tighten their own belts.

Going forward two key actions will likely be needed on a new scale if customers are going to be able to afford these essential services: some kind of **debt write-off** for customers who can't afford their bills in the short-term but can afford ongoing payments once we return to a 'new normal'; and/or **ongoing financial support** for those who can't afford their bills on a more enduring basis. This could take many forms in terms of who pays for support, how is delivered, and who gets it – in the case of the latter, ranging from a focused

[4] Lockdown Lifeline - Ensuring adequate support across the benefits system during Covid-19 - https://www.citizensadvice.org.uk/about-us/policy/policy-research-topics/welfare-policy-research-surveys-and-consultation-responses/welfare-policy-research/lockdown-lifeline-ensuring-adequate-support-across-the-benefits-system-during-the-covid-19-pandemic/

minority to dare I say it, in the interests of fairness and simplicity, everyone.

There are three obvious options on the table for who pays for any increase in financial support. 1. Customers pay, via a cross subsidy – historically Government's preferred option. 2. Government or rather citizens via taxation 3. Companies from profits. Or perhaps a combination of these.

In Australia, in response to Covid-19, the Federal Government has considered the option of underwriting all water and energy bills for six months for customers directly impacted by Covid-19, though how this will work in practice is not yet clear. At present, responses vary across different states, with Queensland directly paying $100 grants to residential and small business utility bill payers, and the Northern Territory halving bills for small business customers for a six-month period. With government encouragement, retail and wholesale utility providers are also informally collaborating to set up consistent financial hardship policies for customers.

The expectation is, that if the customer can't pay for a vital service, in the end the government will foot the bill. In some circles this is seen as opening the door towards some kind of minimum basic income, or minimum energy or water allowance for all, that acknowledges the changing role of the state, the new challenges that societies face and the essential nature of these services.

In GB, the legacy of distrust of utilities may make it harder to have an open discussion about who is best placed to pay for additional support and the way forward. A story in the Sunday Times that water companies had asked for 'a financial bailout'[5] or some kind of financial leeway such as a higher rate of return was quickly denied by WaterUK and Ofwat[6]. Government is understandably reluctant to write a blank cheque to utility companies who are seen by many as having a track record of giving hefty dividends to their shareholders, benefiting from 'unfair profits', and selling 'rip-off energy supply tariffs'. Given many customers reluctance to approach companies when they are in difficulties, it is also questionable as to whether companies are the right entities to provide support.

In the energy sector, the industry association Energy UK has suggested that government could back a loan scheme for energy suppliers up to £100m, given that some smaller suppliers in particular may not be able to absorb bad debt even in the short-term. Other suggestions include deferring network policy costs until a later date to help maintain liquidity for suppliers. There is also early thinking on a debt clearance scheme that would share the costs of outstanding debt between government and companies.

A range of options have been put on the table by consumer groups to supplement existing support schemes. These include extending the Warm Home Discount, reducing standing charges, freezing VAT on fuels, the reintroduction of the general electricity rebate, and adjustments to the tariff caps (a legal mind-field). But none of these is truly new, and longer-term **we need to do more than stick yet more plasters on a system which is fundamentally not fit for purpose**.

More generally there have been calls to widen eligibility and access to the benefits system to ensure everyone who needs support can get it and to review support for groups who risk facing a disproportionate impact due to coronavirus.

Robert Shrimsley in the Financial Times[7] stated "the people at the centre of UK government don't talk about the exit strategy…they talk about learning to live with this". If this is the case, we are left with the following equation:

Pandemic risks + climate impacts + distributional impacts of smart technologies and the transition to net zero + existing failings in the system to support

[5] https://www.thetimes.co.uk/article/now-water-bosses-want-coronavirus-bailouts-9v99fftbp

[6] https://www.waterbriefing.org/home/company-news/item/17142-covid-19-ofwat-and-water-uk-reject-suggestion-that-water-companies-have-asked-for-financial-bailout

[7] Robert Shrimsley – Culture wars are infecting the Covid-19 Strategy. Financial Times 21/04/2020

customers in financial difficulties = a need for a new approach to tackle changing affordability challenges.

So what then is a practical way forward? Short term/medium term

In the short-term companies and regulators will inevitably need to work within the current policy structures, using existing tools to support customers in financial difficulty. It will be important to provide immediate relief to customers during this period of uncertainty and as winter approaches, with rising energy bills, the need for workable solutions will be ever more urgent. In particular, strong leadership is required to:

Across all sectors:

1. **Improve the consistency of financial support provided**: there are lots of examples of good industry practice available. Regulators need to ensure that all utilities are held to account to adopt a minimum good level of service and honour the commitments made. This is long -overdue but now all the more important.
2. **Work together to research and share understanding of the changing impact of the crisis:** Advice agencies should regularly publish insight on the customer experience. Citizens Advice's weekly briefings are a good example of this. Regulators should have a sharper focus on company social monitoring reporting such as debt repayments. Companies and sectors should work together to better understand the financial impacts of this crisis on their customers. Water companies can for example learn from the insight from energy's monthly billing cycles about the likely impact on debt levels, industry can conduct collaborative research and better use publicly available data. This will help improve the design and targeting of support.
3. **Adopt flexible approaches:** we don't yet know the medium to longer-term impact of this crisis on affordability levels or consumer attitudes towards intervention. Customers arguably need to be encouraged to pay when they can so as not to store up debt problems for the future. While we would usually advocate companies take proactive action to prevent affordability problems, given the likely scale of the challenge it may be more sensible to wait until the scale of the challenge is clearer before designing more permanent solutions.
4. **Prioritise data sharing** initiatives that can help industry and third parties proactively identify customers in financial difficulty.
5. **Develop a central up to date portal of support available for customers** who are struggling to afford bills which can be used by frontline advisors.

In the water sector:

6. **Measure water poverty and develop a strategy to eradicate it:** the water industry should continue/restart its good work in this area. This includes UKWIR and Water UK's activity. This needs to be done collaboratively with excellent project's such as Northumbrian Water's research with NEA. The baseline figure of customers in financial difficulty may be uncomfortable but this and a strategy to tackle water poverty is needed now more than ever.
7. **Conduct a thorough review of water social tariff guidance** in consultation with water companies and stakeholders to make the support across England and Wales fairer for all. Particular consideration should be given to alternative options for funding social tariffs schemes. This should include an impact assessment of the current approach to willingness-to-pay as the basis for funding and the resulting designs of social tariffs.

In the energy sector:

8. **Define the roles of different parties in the energy sector in tackling fuel poverty:** Bring suppliers, distribution and transmission companies and key stakeholders together to discuss and agree roles for each party in tackling fuel poverty. The role of distribution and transmission companies, in particular, is ill-defined and inconsistent and there is a risk of the regulatory framework being at odds with the preferences of stakeholders and customers flagged in research informing RIIO-2 business plans.
9. **Prioritise prepayment –** it is imperative that Ofgem prioritises solutions to tackle prepayment self-disconnection and self-rationing and there should be a renewed focus on rolling out smart

prepay. Surely it is time to finally end energy disconnection.

In telecommunications:

10. **Improve the transparency of internet service and mobile providers'** performance in supporting customers in financial difficulties and provide assurances that the quality of protections consistently reflects the essential nature of these services.

Medium to longer-term we need different affordability solutions

In recent parliamentary questions Alok Sharma stated "*We are all agreed* that we do not want anyone to go without a basic necessity such as energy supply." If this is the case, longer-term we need to be bolder, more innovative and open to a better way of doing things. We need to challenge ourselves as to how we can genuinely end self-disconnection and deliver other 'basic necessities' including broadband, as it has proven to be.

Mark Carney in the Economist[8] states, "After the covid crisis, it's reasonable to expect people to demand improvements in the quality and coverage of social support…People's economic narratives will change… After decades of risk being downloaded onto individuals, the bill has arrived, and people do not know how to pay it…" This suggests that not only will a new approach be needed but it will be expected by the public.

Nobody in their right mind would ever have sat down and designed the financial support system we have in our utilities sectors. We need a simpler, more coordinated, more cost-effective approach to ensure all customers can afford and therefore access essential services. We also need to make sure that a focus on ensuring affordability in these difficult financial times doesn't come at the expense of making progress on net zero and environmental improvements. If this happens, it may lead to exponential affordability challenges in the future.

To do this will require bringing together sectors, getting to the heart of welfare policy. It is a debate that should include consumers and citizens, possibly a Citizens Jury, as Involve and Nuffield have recently suggested[9], about the kind of society we want to live in. This is particularly important given the lack of trust in utilities, their essential role in modern life and the importance of transparency and legitimacy.

Such a debate will get to the heart of discussions about fairness and the role of the state and companies – who pays, who should receive help, and who should deliver it. It will be complex. It won't be easy. There will be vested interests on all sides.

This isn't about trying to be 'too clever' as the Institute for Government[10] has warned, but simply about negotiating and developing a system that is fit for purpose for a more sustainable, fair and efficient future.

At Sustainability First we propose to host a series of webinars in the summer of 2020 to help kick-start this discussion. These webinars are intended to provide a forum for organisations and individuals to present and discuss new ideas about how we might ensure all consumers and citizens have access to essential water, energy and communication services.

If you have a proposal or would like to join our 'Build Back Better' webinars, please get in touch with zoe.mcleod@sustainabilityfirst.org.uk. The webinar series is intended to be the beginning of a journey to openly explore the options. Together we hope we can help to prevent a 'collective failure of imagination' when it comes to exploring the potential affordability scenarios and the solutions for the future.

Zoe McLeod, Sustainability First

Sustainability First is carrying out extensive work on how to ensure recovery from the pandemic is smart, fair and green. More details can be found in our Bridging corona to a sustainable future work programme.

[8] Mark Carney, The World After Covid-19, Putting values above valuation. 18/04/2020

[9] https://www.involve.org.uk/resources/blog/news/nuffield-council-and-involve-call-greater-transparency-and-public-involvement-uk

[10] https://www.instituteforgovernment.org.uk/publications/bailout-business-coronavirus