

February 2019

Citizens Advice Scotland - Response to Ofgem's Targeted Charging Review: Minded to Position

About Citizens Advice Scotland

Citizens Advice Scotland (CAS) uses research and evidence to put consumers at the heart of policy and regulation in the energy, post and water sectors in Scotland. We work with government, regulators and business to put consumers first, designing policy and practice around their needs and aspirations.

CAS is the Scottish consumer advocate on energy network issues. Although we are separately funded organisations, we work closely with colleagues in Citizens Advice England and Wales in this area. Our response below focusses on Scottish specific points which we believe are important considerations for the TCR.

We thank you for the opportunity to comment on the consultation and our response is not confidential.

Please find a summary of our key points below:

- 1)** CAS welcomes Ofgem's work on the TCR and recognises the need for change
- 2)** CAS welcomes the broad rebalancing of charges between the domestic and non-domestic sector
- 3)** We raise a number of significant concerns with the fixed charge method that is being proposed and in particular the effect it may have on low income households – which has potential to exacerbate fuel poverty in Scotland.
- 4)** Further analysis and consumer research is needed to understand distributional impacts within the domestic sector in Scotland
- 5)** CAS believe that households in the North of Scotland who face the largest impact from the proposed changes need appropriate protection
- 6)** CAS does not think that Economy 7 users should face higher residual charges than other domestic users
- 7)** The impact from the review of 'access and forward looking charges' needs to be better understood before decisions on 'residuals' are made

The need for change

1. CAS welcomes Ofgem's work under the Targeted Charging Review and recognises the need to ensure that network costs are distributed fairly between users. It is commendable that households who have domestic generation, such as solar panels, are reducing their consumption from the electricity grid (a move which we would continue to welcome). However we feel that due to their reliance on the electricity grid as a back-up and as an export facility, it is right that they should pay a fair contribution towards the maintenance and upgrade of the network. We also believe that households who have their own generation may receive further support from changes being made to 'forward looking charges' or through the proposed 'Smart Export Guarantee' scheme¹. To summarise we believe that similar customers with and without onsite generation should pay the same towards residual charges.
2. CAS welcomes the broad rebalancing of charges between the domestic and non-domestic sectors. As shown in figure 5 of Ofgem's TCR consultation document the contribution of the domestic sector is proposed to reduce from 46.9% in the current charging structure to 38.5% under fixed charges and 42.9% under agreed capacity. While we welcome this rebalancing we also think there is a need to ensure that SMEs and microbusiness are not disproportionately disadvantaged in any changes to be made.
3. As discussed in more detail below, we think the distributional impact of changes within the domestic sector is an area of concern.
4. We also broadly support the change to solely collect residual network charges from users of the electricity network rather than from generators connected to the network. However, we think it is highly important that Ofgem holds generators to account to ensure that savings are truly passed down to end consumers. This must be a priority for Ofgem.
5. While a system wide analysis is included in the consultation document, CAS feels that decisions on residual charging should not be made until the impact from changes to access and forward looking charges are better understood.

Distributional analysis of impacts on domestic households – the need to protect low income households

6. In Scotland 24.9% of households are in fuel poverty² and energy prices were noted as the 2nd top concern for Scottish consumers³. While there are four key drivers to fuel poverty (energy bills, income, energy efficiency and how energy is used in the home) increasing bills have been largely to blame for consistently high fuel poverty rates in Scotland (see figure 1 below). Analysis shows that in 2015, fuel poverty rates in Scotland would have been at 8% (rather than 31%) if energy prices had risen at same rate as inflation between 2002 and 2015⁴.

¹ <https://www.gov.uk/government/consultations/the-future-for-small-scale-low-carbon-generation>

² <https://www.gov.scot/publications/scottish-house-condition-survey-2017-key-findings/>

³ Sourced from CAS 2018 consumer survey

⁴ <https://www.gov.scot/binaries/content/documents/govscot/publications/report/2017/11/new-definition-fuel-poverty-scotland-review-recent-evidence/documents/00527017-pdf/00527017-pdf/govscot%3Adocument>

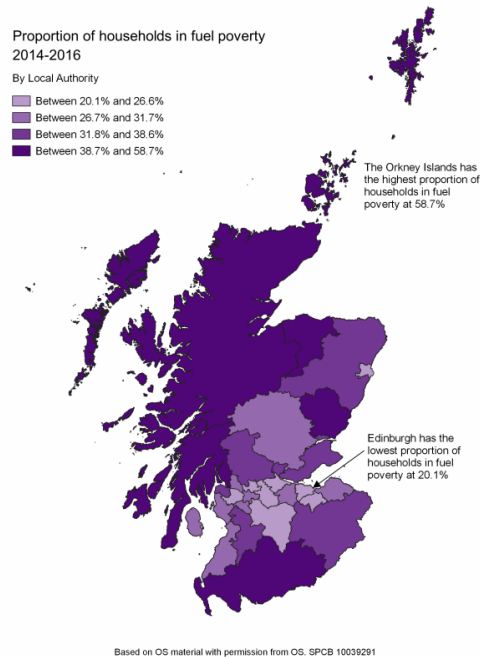


Figure 1 – Fuel Poverty rates by local authority area (2014-16)⁵

7. Given these high fuel poverty rates in Scotland, as noted below, CAS is concerned that any increase in residual charges for low income, low energy use households, will exacerbate fuel poverty in Scotland. If the proposed changes are taken forward then mitigating action will be needed.

8. While we agree with Ofgem's statement in the consultation document that "*vulnerable consumers are present in most domestic consumption groups*", we have concern about low income households - who are a sub group of vulnerable consumers. As shown in the review paper presented by Grid Edge Policy⁶ there is a broadly linear trend between energy consumption and income (although some variation will always exist). While this data is from England and Wales we expect a similar trend to exist in Scotland.

9. Ofgem set out in the consultation document that those households who use the least electricity could face a typical annual increase of £2 to £22. However in Grid Edge Policy's review⁷, the impact on bills is estimated to be higher. As can be seen in Table 1, the lowest income households, with the lowest energy use could see bills increase by £51. In contrast the highest income households, with the highest energy use could see bills decrease by £195 per annum (analysis for England and Wales).

10. CAS believes that given the high fuel poverty rates in Scotland, any increase in energy costs to low income households should be avoided. Further analysis to assess the impact of any change to residual charges on fuel poverty levels in Scotland should be completed before any final decision is made.

⁵ <https://sp-bpr-en-prod-cdnepe.azureedge.net/published/2018/9/3/Fuel-Poverty--Target--Definition-and-Strategy---Scotland--Bill/SB%2018-52.pdf>

⁶Sourced from Grid Edge Policy – Understanding the Impacts of Ofgem's Targeted Charging Review https://docs.wixstatic.com/ugd/140d4b_d97aba68981041978c5367c405c1eca1.pdf

⁷ Grid Edge Policy – Understanding the Impacts of Ofgem's Targeted Charging Review https://docs.wixstatic.com/ugd/140d4b_d97aba68981041978c5367c405c1eca1.pdf

2016

Household income	Number in sample	Percentage of sample	Change in Annual Energy Bill (£)								
			Mean	Standard Deviation	5th percentile	10th percentile	Lower quartile	Median	Upper quartile	90th percentile	95th percentile
All dwellings	4,111,300	100	0	16	48	43	31	11	-15	-54	-92
Less than £15,000	614,200	15	13	21	51	46	38	25	2	-34	-67
£15,000 to £19,999	331,310	8	8	20	51	46	36	21	-3	-41	-77
£20,000 to £29,999	846,550	21	7	20	49	44	33	16	-7	-43	-79
£30,000 to £39,999	728,120	18	2	18	48	41	30	13	-11	-49	-84
£40,000 to £49,999	560,290	14	-3	18	46	38	26	8	-18	-54	-89
£50,000 to £59,999	332,530	8	-7	16	44	36	23	5	-21	-59	-95
£60,000 to £69,999	207,990	5	-8	15	43	36	21	3	-25	-64	-103
£70,000 to £99,999	291,850	7	-15	11	41	34	20	-2	-31	-75	-115
£100,000 to £149,999	138,000	3	-26	3	38	30	11	-11	-48	-100	-148
£150,000 and over	50,880	1	-43	-8	36	26	7	-23	-71	-139	-195

Table 1 - theoretical changes in energy bill by income group for England and Wales assuming a £64 standing charge (Sourced from Grid Edge Policy)⁸.

11. Grid Edge Policy also modelled the distributional impacts of changes to a fixed charge on different customer archetypes (see table 2). These archetype groups were developed by the Centre for Sustainable Energy in 2014. We feel that this analysis is highly useful in understanding the distributional impact on different customer groups. As can be seen in Table 2 all low income archetypes (except low income electrically heated households) will face an increase in their annual contribution to residual charges with Ofgem's proposed fixed charge. Interestingly Grid Edge Policy's analysis shows that the largest archetype group – average mains gas heated households- will also see their bills increase by £5.

12. CAS believes that Ofgem should complete a similar analysis using updated customer archetypes (that include 2nd home owners, domestic generation etc.) to assess the impact of proposed changes. As noted later in this response we think this new analysis should be tested with consumers to understand their attitudes and to ensure that changes proposed align with their views.

Archetype Group	%	Estimated Annual Price Change - £	% Annual Price Change
Low-income electrically-heated	4%	-37 (2)*	-3.4% (0.2%)*
All other electrically-heated	7%	-82 (-43)*	-5.3% (-2.8%)*
Low-income non-metered fuel-heated	2%	8	1.3%
All other non-metered fuel-heated	4%	-15	-1.7%
Low income, out-of-work single adults in small 1-bed social rented flats (London)	4%	29	6.5%
Young working adults in rented flats (London)	4%	17	3.1%
Low-income single adults (lone parents or elderly) in social rented houses	5%	21	4.0%
Younger working families in medium-sized rented houses	11%	7	1.0%
Average' mains gas-heated households	33%	5	0.8%
Wealthy working families in 3-4 bed semi's owned with mortgage	9%	-11	-1.3%
Asset-rich, 'empty-nesters' in detached houses in less urban areas	10%	-3	-0.4%
Wealthy working families in larger detached houses in less urban areas	6%	-23	-2.4%

*Values in brackets are estimated values for a higher standing charge of £103 for Economy 7 customers

Table 2- change in energy bill in £ and percentage for the average (mean) customer in different archetype groups – as defined by the Centre of Sustainable Energy (CSE). Percentage change based on SVT tariff cap electricity bill for relevant usage level. (Sourced from Grid Edge Policy)⁹

Regional variation – the need to support households in N. Scotland

⁸ https://docs.wixstatic.com/ugd/140d4b_d97aba68981041978c5367c405c1eca1.pdf

⁹ https://docs.wixstatic.com/ugd/140d4b_d97aba68981041978c5367c405c1eca1.pdf

13. CAS also has some concern that some households in the North of Scotland will see a disproportionate impact of changes to residual charges. As noted in Ofgem's *Regional Differences in Network Charges*¹⁰ households in the North of Scotland pay some of the highest networks charges for electricity. For a household in the North of Scotland with a typical single rate usage of 3100kWh/y they pay £143 per year whilst a household in the South of Scotland with the same usage pays £116.

14. These higher network costs, which largely are a result of higher distribution costs, mean that the impact of changes to residual charges (which are proposed to vary by DNO region with the fixed charge model) on low energy users in the North of Scotland, may be particularly high. This is illustrated in Figure 13 of Ofgem's consultation document which shows that domestic low consumption users in the North of Scotland will see the largest increase in charges per year - £29 compared with an increase of £3 per year for users in London with the fixed charge model.

15. CAS believes that households in the North of Scotland, where fuel poverty rates are typically above 50% (see figure 1), should receive the appropriate support –such as an increase to the 'Hydro-benefit Replacement Scheme' - which reflects any changes being proposed to residual charging.

The need for further consumer research

16. While we recognise that Ofgem has undertaken some consumer facing research through a consumer panel, we suggest that more research is needed given the magnitude of changes proposed. While the consumer panel showed that those consumers engaged supported the principle that households across GB should pay the same for residual network charges, we feel that further consumer research may be needed to test consumer opinions based on the broad archetype groups (and the impact on each) presented in this response.

Economy 7 users should not be segregated

17. CAS welcomes Ofgem's headline figures of reducing Economy 7 user's residual charges by £43 in the North of Scotland and by £69 in the South of Scotland under a fixed charge method. However CAS believes that Economy 7 users should not be segregated as a category for higher charges. For a typical consumption Economy 7 user, the fixed charge could be £103 pa compared to £64 pa for typical consumption single rate users. This means that households who are off the gas grid and rely on electric heating in Scotland will continue to pay a premium for network charges above households who have access to mains gas heating.

18. In Scotland 83% of households are connected to the gas grid.¹¹ Households off the gas grid must rely on alternative heat sources such as electricity. 12% or 292,000 households in Scotland use electricity for heating and the latest figures show that 52% of households in

¹⁰https://www.ofgem.gov.uk/sites/default/files/docs/2015/10/reg_charges_final_master_version_23_october_2015.pdf

¹¹ <https://www.gov.scot/binaries/content/documents/govscot/publications/statistics-publication/2018/12/scottish-house-condition-survey-2017-key-findings/documents/scottish-house-condition-survey-2017-key-findings/scottish-house-condition-survey-2017-key-findings/govscot%3Adocument>

Scotland with electric heating are in fuel poverty¹². Ofgem data¹³ (for GB) also shows that 70% of households with electric heating use heating systems with the ability to store heat and are therefore likely to be Economy 7 users.

19. As highlighted in the CAS' recent publication *Hard Wired Problems*¹⁴ electric heat users face a number of issues and require specific support needs. The report found that those who rely on electric heating often experience significantly higher heating costs (up to 3 times as expensive as mains gas for whole house heating), lower incomes and widespread disengagement from both the energy market and support services. As a result, this group often requires additional, holistic support to lower costs and resolve problems. It is also the case that households with electric heating already pay an additional premium for environmental levies. Ofgem reported on a study that showed that by 2020, households with electric heat will pay 19% of social and environmental levies but will only receive 7% of the benefits¹⁵.

20. Given this context CAS believes that Economy 7 users should not be segregated for higher network charges. Given that the smart meter roll out will also facilitate the use of smart tariffs it is also questionable as to whether Economy 7 tariffs will be an enduring piece of the energy landscape. As highlighted by Citizens Advice research on Time of Use tariffs¹⁶ it is also questionable whether customers who engage in the market and use electricity in a flexible fashion (such as economy 7 users) should be financially penalised through higher residual charges. The impact that these customers have on the network will not be higher than a typical single rate high energy user and in certain circumstances may lead to whole system benefits to the electricity network.

If you have any questions about points raised in the response please don't hesitate to get in touch.

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¹² <https://www.gov.scot/binaries/content/documents/govscot/publications/statistics-publication/2018/12/scottish-house-condition-survey-2017-key-findings/documents/scottish-house-condition-survey-2017-key-findings/scottish-house-condition-survey-2017-key-findings/govscot%3Adocument>

¹³ <https://www.ofgem.gov.uk/ofgem-publications/98027/insightpaperonhouseholdswithelectricandothernon-gasheatingpdf>

¹⁴ <https://www.cas.org.uk/publications/hard-wired-problems>

¹⁵ <https://www.ofgem.gov.uk/ofgem-publications/98027/insightpaperonhouseholdswithelectricandothernon-gasheatingpdf>

¹⁶ <https://www.citizensadvice.org.uk/about-us/policy/policy-research-topics/energy-policy-research-and-consultation-responses/energy-policy-research/the-value-of-time-of-use-tariffs-in-great-britain/>