

# Policy position paper: Affordability in the regulatory period 2021 -2027



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## Overview

Prices changes during the next regulatory period 2021 – 2027 may have a bearing on paying customers, particularly those on low income. CAS has recently conducted research using Fraser of Allander Institute to understand how potential price change scenarios may affect aspects of affordability.

Research was conducted in two stages. Stage 1 forecasted household income in the period to 2027 using central, high and low scenarios. Stage 2 sought to identify what proportion of Scottish households would be likely to spend more than 3% of income on water and sewerage under four charge scenarios between 2021/22 and 2027/28 (2%, 2.5%, 3% and 3.5%).

The research identified how the proportion of households spending more than 3% of net income on water and sewerage varies across household characteristics; and how the proportion of all households identified as spending more than 3% of income are distributed by characteristic. Characteristics used are: Council Tax band; income; tenure; benefits; and household composition.

## Sensitivity Analysis

The research's methodology is based on a sample of 6,200 Scottish households using the Households Below Average Income (HBAI) and the Family Resources Survey (FRS) surveys of 2016/17 and 2017/18, which includes data across household characteristics, as listed above.

In order to estimate the likely affordability of water and sewerage charges in future years, assumptions have been made about how household income and housing costs may grow and how the distribution of households by type may change to reflect demographic and household formation patterns<sup>1</sup>. As with every projection, the numbers that are being used for estimating specific factors in future years (e.g. CPI inflation, income growth, housing costs) we assume that they will follow the current stable patterns of the Scottish economy, and for that reason it is difficult to predict the exact impact of an extreme future occurrence, such as Brexit.

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<sup>1</sup> Household formation patterns includes the likely future growth of income by type, the likely changes to tax policy and the likely changes to housing costs, mainly rent and mortgage costs.

## Key findings

- Under all scenarios (central/high/low) and under any water charges' increase, fewer households are projected to spend more than 3% for water costs p/w, than the 12% finding of 2016.
- Income is by far the most effective determinant of whether or not a household is likely to struggle to afford their water charges.
- Council Tax bands are a less reliable proxy for affordability with less than a fifth of households actually spending above 3% and receiving Council Tax Reduction, and therefore reduced water charges.
- Lowest income decile households will be significantly affected by increases in water charges (7 out of 10 consumers within the lowest decile), and this percentage could rise to 76% in 2027/28 after applying the four pricing scenarios.
- No household in the top half of the income deciles spends more than 3% on water charges.
- Under all scenarios and even under the 3.5% scenario, the proportion of households that struggle with water charges falls between 2021/22 and 2027/28. The reason being that for a small subset of households (who are just above the 3% threshold regarding water charges in 2021/22), their income is forecast to grow by slightly more than 3.5% over this period to 2027/28, resulting in a reduction of households paying above the 3% threshold.
- There is no significant margin between a 2% increase and a 3.5% increase in terms of impact on consumers.

Considering existing discount policies such as CTR and reductions on low incomes (such as Housing Benefit, Tax Credits, Universal Credit, and Income Support), the research paper acknowledges that the existing charging structure, based on Council Tax bands, does a reasonable job of protecting some of those households that face difficulties paying for their water and sewerage charges. However, given the fact that the structure of the existing system is inflexible and households paying more than 3% are dispersed through the bands, there are limitations on how additional short term measures, based on Council Tax banding or benefit eligibility, will more effectively target financial support to low income households.

The following section explores the key findings in more depth, categorised by the household characteristics used in the research.

### 1. Council Tax Band

The report reveals that, for the year 2021-22, the proportion of households paying over 3% p/w for water and sewerage charges is higher in bands E-H than in bands A-D (fewer than 10%), under all scenarios. Specifically, the proportion of households paying above 3% and living in Council Tax band G properties exceeds 20%. This is consistent with our previous analysis in 2015/16, where it showed that the increasing likelihood of consumers paying above 3% p/w, as we move through the bands, reflects the fact that their water charges increase accordingly. And given the fact that average household income also increases through the bands, this reveals significant income dispersion within each band (i.e. a large proportion of relatively low income households living in higher banded properties). There is little difference in

the proportion of vulnerable households across the four price scenarios in 2021/22, as the marginal differences have been applied in just one year. However, due to the cumulative effect of charges through the period, this difference becomes more visible in 2027/28<sup>2</sup>.

## **2. Tenure**

The research shows that the proportion of households spending more than 3% for water costs p/w in 2021/22 and in 2027/28 is highest within the social rented sector (15%), reflecting lower than average incomes in this tenure type. Surprisingly, the social rented sector's proportion is not significantly higher than the other sectors such as private rented sector and owned sector.

## **3. Income decile**

The vast majority of households that paying more than 3% p/w falls within the lowest decile of income: almost 7 out of 10 households in this decile (68%) in 2021/22, moving to nearly 8 out of 10 (76%) in 2027-28. Taking account of the fact that effectively zero households in the top half of the income distribution spend more than 3% for water services p/w, it is clear that income is the strongest indicator of water affordability issues in Scotland.

## **4. Household composition**

The proportion of households likely to struggle to afford water charges is calculated through the consideration of benefit units (a benefit unit is a single adult or couple plus any dependent children). Interestingly, among all households in 2021/22, single pensioners have the lowest prevalence of spending more than 3% (around 5% of households), due to reasons such as tendency to occupy lower banded properties, lower housing costs and the effect of the single person discount. Couples with children and singles with children are most heavily impacted, and together consist of nearly 1/4 of all households that pay more than 3% p/w for water charges. By 2027/28, the proportion of households paying above 3% for water and sewerage charges p/w has fallen uniformly for all benefit unit types.

## **5. Economic status**

The proportion of households that may struggle to afford water services is higher in households where one or more adults are not in work or where one or both work part-time (14-15% in 2021/22), than in households where all adults are in full-time work (3% in 2021/22). The research concludes that households' water vulnerability is correlated with economic status. Specifically, the most impacted household category by far in 2021/22 is the *Workless head or spouse unemployed*, which consists of more than half of the total number of households (55%) paying more than 3% p/w, while the *Economically inactive* category (workless people due to study, disability/illness etc.) is comparatively low (14%), due to the tendency of these households to have higher incomes as they probably qualify for other disability benefits and exemptions from water charges. In 2027/28, the same household proportions across all categories continue to exist showing minor differences.

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<sup>2</sup> See page 17, charts 4.1 and 4.2 of the research report

## **6. Benefits**

Considering the proportion of households spending more than 3% for water costs p/w by benefit type in 2021/22, the largest proportion (35%) consists of households in receipt of Job Seekers Allowance. This finding is very similar to CAS' research in 2017/18 and strengthens the argument that households, where those of working age are not in work, tend to be particularly vulnerable in terms of water charges. Moreover, the proportion of households in receipt of additional benefits such as Child Benefit or low income benefits is significantly lower than JSA recipients (11%).

By 2027/28, the proportion of households in receipt of each benefit has declined uniformly across all categories. However, under the 3.5% charge scenario, the JSA proportion is proportionately higher in comparison with the same price increase on the other benefits.

Of those households that receive Council Tax Reduction, the proportion that may struggle to afford their water charges is in line with that for the general population at 9%-10%. However amongst households, which it is estimated are eligible for Council Tax Reduction, the proportion is actually much higher. The implication is that there are households who could be eligible for Council Tax Reduction but either do not claim it, or who do receive it but did not declare so in the survey.

### **CAS provisional policy position**

CAS acknowledges and supports the provision of funding to meet the future demands placed on Scottish Water such as circular economy, net zero emissions targets, resilience, etc. as well as to maintain and enhance services to its customers. However, within the next regulatory period, as well as meeting funding requirements, there is also a need to adequately protect customers who struggle to pay their charges. In the longer term, CAS believes that water and sewerage charges should be affordable for all Scottish consumers. This will require a review of existing affordability policies to identify ways of providing more targeted support to low income households. Moreover, CAS supports further research into the affordability of water and sewerage charges among diverse categories such as households in the lowest income decile, households that are consisted of couples with children, households where the head or the spouse are workless and households that are eligible for JSA benefit.

CAS recognises that more permanent and effective policy that offers adequate financial support to vulnerable consumers will take time and consideration. So, in addition to the interim and longer term recommendations within our 2018 report 'Charting the Waters' (Appendix), we would welcome further policy measures, as set by the Scottish Government, to increase financial relief for low income households during 2021-27, such as freezing water and sewerage charges or increasing financial support for those in receipt of Council Tax Reduction so that they do not pay above inflation rate increases.

## **APPENDIX**

### **Interim recommendations (2018-2021)**

#### **1. Agencies should work collaboratively to increase the number of eligible consumers receiving the Council Tax Reduction**

Discounts for water charges are automatically applied if a household receives Council Tax Reduction. However it is estimated that the proportion of eligible households which apply for Council Tax Reduction could be as low as 62% - 69% overall, and 54% - 61% for pensioners.

In line with our recommendation in 'Charting a New Course' CAS would welcome the Scottish Government, front line agencies, the Department for Work and Pensions and local authorities working collaboratively to consider how to encourage more eligible consumers to apply for Council Tax Reduction.

CAS has launched a tool to increase CTR uptake and we would welcome further support of this by the Scottish Government, local authorities and Scottish Water to generate greater awareness of additional financial support and ensure it reaches those who need it.

#### **2. Additional measures to increase financial relief should be available under the Water Charges Reduction Scheme**

A further reduction in charges for consumers in receipt of the Water Charges Reduction Scheme will provide vital additional support to low income households. Additionally, it will provide additional support to households on Council Tax Reduction that may not spend more than 3% of their weekly income on their charges, but are likely to be on a low income.

CAS welcomes any further policy measures, as set by the Scottish Government, to increase financial relief for low income households during 2021-27.

#### **3. Simplifying the process for Universal Credit recipients to apply for Council Tax Reduction**

In line with our recommendation in 'Charting a New Course', we would welcome collaborative working between the Department for Work and Pensions, Scottish Government and local authorities to create universal policy whereby the data local authorities receive from the Department for Work and Pensions on Universal Credit recipients is used to automatically submit a Council Tax Reduction application.

This would make it easier for consumers in receipt of Universal Credit to apply for Council Tax Reduction, which could support an increase in the number of households benefiting from a reduction in water and sewerage charges.

## **Long term recommendations (2021-27)**

### **4. Using income as the proxy for discounts**

Further research is required on how to more effectively target those paying more than 3% on water and sewerage charges p/w based on their income, and clear policy on whether or not those in higher Council Tax banded properties should be eligible for additional financial relief.

We would welcome such a system being developed and implemented for SRC period 2027-2034. This will provide more targeted financial support to those consumers that need it most and is a more accurate proxy upon which to base charges relief than Council Tax banding.

### **5. A review of the Water Charges Reduction Scheme**

A review should focus on how successful the proposals have been in providing additional financial support to all households that qualify for Council Tax Reduction and may struggle to afford their water and sewerage charges.

### **6. Research to better understand affordability in higher Council Tax bands should be conducted**

Further research is required into the affordability of water and sewerage charges among pensioner households living in higher Council Tax banded properties and spending more than 3% of their weekly income on water and sewerage charges: how they view their ability to pay, as well as how many of these households are already in receipt of the Water Charges Reduction Scheme.

In addition, and informed by the research findings, the Scottish Government should formulate clear policy on whether or not financial support should be made available to higher Council Tax banded properties, where they spend more than 3% of their weekly income on their water and sewerage charges.