



Action for Warm Homes

National Energy Action (NEA) response to Ofwat's consultation on the draft methodology for PR24

September 2022

About National Energy Action (NEA)

NEA¹ works across England, Wales, and Northern Ireland to ensure that everyone in the UK² can afford to live in a warm, dry home. To achieve this, we aim to improve access to energy and debt advice, provide training, support energy efficiency policies, local projects and co-ordinate other related services which can help change lives. NEA is also working with Northumbrian Water Group (NWG) and other water companies to eradicate water poverty by 2030. The programme aims to establish an industry acknowledged definition of water poverty and a more consistent and joined up strategy to deliver positive outcomes for customers struggling with their water bills.

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Background to this response

National Energy Action (NEA) has worked for the last 40 years across the energy sector to support millions of low income and vulnerable consumers. We have played a key role with Ofgem and energy networks to develop recent price controls which have enhanced support for vulnerable customers at the same time as facilitating the move to net zero. NEA has also fed into forward work programmes for Ofgem and developed new or updated vulnerability strategies which have improved outcomes for the most vulnerable customers. We have influenced the shape of national support programmes across the UK for many years.

NEA has also recently helped galvanise key developments in the water sector. In May 2020, we called for a full review of social tariffs, their funding, eligibility criteria, and support levels. We subsequently worked closely with the Consumer Council for Water's (CCW) Independent Review of Affordability which aimed to provide greater support and more consistent outcomes to households facing financial difficulty, and we continue to contribute to the ongoing development of the Single Social Tariff. NEA believes the outcomes of the review provide the first opportunity in over a decade to change the landscape of water affordability support in England and Wales, identifying and retaining good practice and making improvements to make support fairer for all, and believe the momentum must be maintained if we are to make a stepped change in the numbers of households experiencing water poverty.

This combined experience has given us significant knowledge in understanding the areas a regulator can improve and/or focus on to deliver positive impacts for vulnerable customers, as well as those that are less effective. We therefore hope we are well placed to comment on Ofwat's consultation on their draft methodology for PR24, in order to ensure the best outcomes for the most vulnerable customers served by water companies.

Rather than respond to the questions posed in the consultation document, we have chosen to provide more general comments across five headings:

- Affordability and vulnerability
- Single Social Tariff
- Encouraging innovation
- Company performance
- Additional comments.

Summary of our recommendations

In summary, we have outlined the following ten recommendations for consideration:

1. Ofwat should reaffirm the importance of the work across affordability and vulnerability *and* reconsider including affordability and vulnerability as an additional theme to this price review.
2. Ofwat should require all areas of business plans to have a full impact assessment undertaken showing the impacts on customer bills, including those struggling, or at risk of struggling, to pay.
3. Ofwat should support the introduction of a customer-focused licence condition with the introduction of a vulnerability strategy.
4. Ofwat should reconsider their position on the actions that companies should take regarding a single social tariff, considering how this could be done within the current legislative and regulatory frameworks.
5. Ofwat should introduce a dedicated fund which companies can use for programmes focused on consumer vulnerability and water efficiency.
6. Ofwat should introduce a requirement for companies to assess the impact(s) of *all* innovation projects on households in vulnerable circumstances.
7. Ofwat should use the price control to confirm an industry measure of water poverty and create a reputational incentive that requires companies to submit an annual return on the levels of water poverty in their area under an agreed methodology.
8. Ofwat should reconsider the removal of ODIs/PCs for vulnerability and affordability, and consider introducing the following requirements:
 - a. Companies to report on PSR recruitment as a direct result of their own activities
 - b. Companies to report on an additional measure of experience, which specifically surveys customers on the PSR
 - c. Companies to report on the reduction of debt in situations of severe indebtedness
 - d. Companies to report reductions in the levels of water poverty in their operating areas
 - e. Companies to report on the number of value-adding conversations they have with defaulting customers.
9. Ofwat should introduce a performance reporting mechanism, which consistently publishes performance metrics on affordability and vulnerability on an annual basis.
10. Ofwat should place a requirement on NAVs to submit plans for improving affordability support.
11. Ofwat should include the impact assessment required under recommendation two in the required evidence to assess ambition for affordability.

Our response to this consultation

The remainder of this consultation response provides our thoughts across four headings:

- Affordability and vulnerability
- Single Social Tariff
- Encouraging innovation
- Company performance
- Additional comments.

Affordability and vulnerability

We recognise that Ofwat has changed their approach to affordability and vulnerability in comparison to PR19; instead of recognising this as an additional theme of the price control, Ofwat has instead attempted to embed action for customers in vulnerable circumstances throughout their methodology for PR24. While we acknowledge that this approach could work in theory, we have concerns that this will remove focus and dampen the importance of the work in this area, unless specific performance commitments or regulatory requirements are made.

We believe that a number of unintended consequences are at risk with this move, including, but not limited to:

- A lesser focus on delivering for customers struggling, or at risk of struggling, to pay their water bills, with an over-reliance on the outcomes of the development of the single social tariff
- Water companies viewing the reduction in performance commitments and Outcome Delivery Incentives (ODIs) as an indication that the importance of delivery in this area has reduced.

We recommend that Ofwat reaffirm the importance of the work across affordability and vulnerability *and* reconsider including affordability and vulnerability as an additional theme to this price review.

We accept that “the need for affordable bills” has been identified as one of the three challenge areas of focus for PR24, but this alone may not be enough to ensure companies remain focused on delivering for their customers, specifically for those in vulnerable circumstances, and it may not be strong enough to illustrate the gravity of the current cost of living crisis. **NEA recommends business plans have a full impact assessment undertaken showing the impact on customer bills, including those struggling, or at risk of struggling, to pay.** This impact assessment should also highlight how the company proposes to mitigate any potential detriment caused by their investment plans and provide evidence that their plans do not increase company profits at the detriment of their customers (currently suggested in the areas of focus outlined under ‘delivering greater environmental and social value’ but required across all areas of the business plan).

We have long called for Ofwat to develop a vulnerability strategy and associated licence condition. When Ofgem launched their first vulnerability strategy in 2013, this marked a step-change in the services offered by energy suppliers and networks for their customers and prompted substantial increases in customer service levels. This strategy has since been refreshed several times, and each time the principles are strengthened to improve services for customers in vulnerable circumstances. On the most recent refresh, it was decided that some principles would become licence conditions (specifically the ability to pay principles), as it was recognised that they were not being applied equally across the sector. We are pleased that Ofwat are developing a customer-focused licence

condition but would encourage Ofwat to learn from Ofgem's progress in this area and accompany this with a principles-based vulnerability strategy with areas of significant importance being detailed in the licence condition, to ensure an appropriate route for escalation and/or enforcement is provided, safeguarding customers in vulnerable circumstances. **We recommend that Ofwat support the introduction of a customer-focused licence condition with the introduction of a vulnerability strategy.**

Single Social Tariff

The development of a Single Social Tariff (SST) will ensure issues of fairness with the current scheme designs are addressed, making the eligibility, support levels, and levels of cross-subsidy consistent across all companies. We understand that the current approach being pursued requires changes to primary legislation to make it both mandatory and funded at the national level, and we accept that this takes time to achieve, hence we have shown support for the new scheme to be introduced at the start of AMP8. However, we understand that this timeframe causes some uncertainty for water companies during this business planning period.

We had therefore expected the PR24 methodology to provide some clarity to companies on how to proceed with their business plans and the development of the SST. Instead, the methodology requires companies to take a two-pronged approach: firstly to develop plans in line with the SST going ahead, and secondly, to undertake consumer research and develop plans as normal. This latter requirement is both time consuming and costly, especially if the resulting insights are redundant by the implementation of the SST.

We propose that Ofwat takes a different approach for PR24. With general consensus across the industry that this is the right thing to do for customers, Ofwat should consider how this can be achieved within the current legislative and regulatory frameworks and require a collective approach to customer research as is being applied in other areas of company planning, rather than require companies to proceed with the non-SST scenario. We believe this will reinforce Ofwat's support of the SST development and save the unnecessary spend of customer money on redundant research, which is especially important given the cost-of-living crisis and the need to keep bills as low as possible. This would also allow companies to focus their business plans on the affordability support which is additional to the social tariff. **We recommend that Ofwat reconsider their position on the actions that companies should take regarding a single social tariff, considering how this could be done within the current legislative and regulatory frameworks.**

Encouraging innovation

We feel it would be appropriate for Ofwat to introduce two additional market approaches to encourage innovative approaches to addressing affordability and vulnerability challenges:

- 1) The introduction of a dedicated fund, similar to the Gas Distribution Network 'use it or lose it allowance', which companies can use for programmes focused on consumer vulnerability and water efficiency; and,
- 2) The requirement for innovation projects to assess the impact of the project on customers in vulnerable circumstances, regardless of the project focus.

We understand that Ofwat has their innovation fund in place, and intends on continuing this fund into AMP8, but we still believe innovation could be better targeted at meeting the needs of

customers in vulnerable circumstances. The Ofgem ‘use it or lose it allowance’, known as the Vulnerability and Carbon Monoxide Allowance (VCMA), has been introduced to encourage programmes addressing consumer vulnerability and carbon monoxide safety; with the ever-increasing cost of living situation, a similar scheme could be introduced in the water sector to encourage programmes focused on consumer vulnerability and water efficiency – as often water efficiency programmes are targeted at the highest users of water, and not at those who would benefit the most from bill savings. This would encourage programmes with multiple benefits to customers and companies, with limited risk to customers, and we would recommend it was funded in the same way as the innovation competition, with all customers paying an equal amount of cross-subsidy. If introduced, it would be of vital importance to ensure there is enough headroom for companies to support vulnerable customers, and to accompany this scheme with a clear framework for water companies, indicating the activity areas which could be funded/permitted under this allowance. **We recommend Ofwat introduce a dedicated fund which companies can use for programmes focused on consumer vulnerability and water efficiency.**

We also wish to reiterate our calls for Ofwat to refocus innovation projects on vulnerability. We welcome Ofwat’s intention to retain their innovation competition, but of the projects funded in the first two rounds of the competition, very few were focused on delivering outcomes for customers in vulnerable circumstances, yet all projects can have an impact on vulnerable households. **We therefore recommend that Ofwat introduces a requirement for companies to assess the impact(s) of all innovation projects on households in vulnerable circumstances;** this will truly evidence that consideration of vulnerability and affordability is embedded in all company activity, while ensuring that any direct or indirect impacts are identified and mitigated against if there is a risk of detriment.

Company performance

Since commencing the work on water poverty in 2019, NEA has been calling for a single measure of water poverty to be agreed by the industry to ensure that all companies were working towards the same target for eradication. Water UK’s Public Interest Commitment for water poverty has progressed work in this area, with CEPA suggesting a methodology for calculating the prevalence of water poverty but did not recommend a metric. In addition, CCW recommended in their Affordability Review that the Single Social Tariff be targeted at households in water poverty under the 5% measure but did not recommend that this becomes the sole metric for calculating water poverty. **We recommend Ofwat use the price control to confirm an industry measure of water poverty and create a reputational incentive that requires companies to submit an annual return on the levels of water poverty in their area under an agreed methodology.** This will make progress more visible and will ensure that the multiple projects working towards eradication are all working towards the same goal for the benefit of water poor households.

We acknowledge Ofwat’s intention to reduce the number of Outcome Delivery Incentives (ODIs)/ Performance Commitments (PCs) and to use wider tools for delivery on affordability and vulnerability, but we still feel this risks a lesser focus on delivery in these areas. As outlined in our response to the January 2022 consultation ‘PR24 and beyond: performance commitments for future price reviews’, and as also raised in our response to Ofwat’s forward work programme for 2020-21, we propose this is reconsidered. **We recommend the following PCs are introduced on a reputational basis,** therefore not directly linked to financial rewards:

1. Companies to report on PSR recruitment as a direct result of their own activities (i.e., negating any records added as a result of cross-sector data sharing). We believe this would result in a more accurate measurement of the company's attempts to improve their records and would encourage more direct engagement with customers both during, and outside of, incidents.
2. Companies to report on an additional measure of experience, which specifically surveys customers on the PSR. We propose this would be conducted in a similar manner to C-Mex, surveying both PSR customers who have recently contacted their company, and a broader selection of PSR customers.
3. Companies to report on the reduction of debt in situations of severe indebtedness (i.e., where the level of debt exceeds the annual bill). There are many ways in which companies could address debt levels, therefore allowing flexibility in delivery, and this would remain an outcomes-based measure, therefore aligning to the future direction Ofwat wish to travel. This could be supported by a Price Control Deliverable (PCD) which requires companies to report the number of conversations they have with customers who default and still do not pay following a reminder – this PCD would strongly encourage value adding conversations, with the aim of reducing financial difficulty at the earliest possibility.
4. Companies to report reductions in the levels of water poverty in their operating areas. This PC could be supported by a range of PCDs, including, but not limited to, the numbers of income maximisation assessments undertaken, or the value of income generated/ realised for those customers, the levels of customers accessing affordability support in their region, the levels of debt written off for customers unable to pay, and the success rate of payment plans for customers in debt.
5. Companies to report the number of conversations they have with customers who default and still do not pay following a reminder. These conversations could provide water efficiency advice, debt advice, or could be general welfare/vulnerability checks – the specifics could be determined by Ofwat in their guidance notes for dealing with household customers in debt, but the conversation should be focused on adding value to the customer and aim to reduce financial difficulty at the earliest possibility.

We also recommend Ofwat introduces a performance reporting mechanism, which publishes performance metrics on affordability and vulnerability on an annual basis, particularly if the decision to limit the number of performance commitments and ODIs as part of PR24 stands. We believe this mechanism would encourage companies to improve their services and would also encourage innovative thinking in this space with all companies working from an industry baseline. As part of this mechanism, we would expect to see, at minimum, the industry measure of water poverty, levels of debt both by number of households and monetary values of arrears, numbers of households in receipt of affordability support, and a method for measuring the customer experience of households on the Priority Services Register and/or in receipt of affordability support.

Additional comments

We note that New Appointments and Variations (NAVs) are not required to submit business plans and data tables as part of the PR24 process. With the industry undertaking a substantial amount of work to address issues of fairness and the often referenced 'postcode lottery', it feels that this decision leaves a gap. As NAVs continue to gain market share, their lack of affordability support will become more apparent, and customers, through no fault of their own, will not be able to access support they desperately need. **We therefore recommend Ofwat reconsiders this aspect of the PR24 methodology, requiring NAVs to submit plans to address affordability, or, or at minimum, seek to reinforce NAV licences in respect to affordability and vulnerability schemes.**

As indicated on page two of this response, **NEA recommends that the requirement to have assess the impact of all business plan activities on customer bills, including for those struggling, or at risk of struggling to pay, should form part of the proposed assessment process for assessing 'ambition'**. Rather than an 'explanation' of how the company has taken account of views of affordability and those struggling to pay, the impact assessment would be more thorough and show the mitigating action taken when the decision to go ahead with a plan has been taken that places some customers at risk of detriment.

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.