

Levelling the playing field — why everyone should help vulnerable customers

In a fair competition, everyone plays by the same rules. But in the UK energy market, some suppliers have to provide direct support to customers on lower incomes, while others do not. This distorts competition, adds around £40 a year to most household energy bills, and lumps most of the cost onto those least able to pay

Ever since the UK energy market was privatised, some energy suppliers have been legally obliged to provide support directly to customers free of charge, or at reduced cost. They do this by giving financial help (e.g. money off bills) and providing energy efficiency measures (e.g. loft insulation).

The aim is to help in carrying out Government policies to reduce fuel poverty and cut carbon emissions (insulation means that customers use less gas for heating). The cost of doing this has gone up over time - from tens of million pounds a year across the industry, to hundreds of millions. It is paid for by all the customers of each obligated supplier – it is factored into their energy prices.

Currently, the main two supplier obligations are called the Warm Home Discount (WHD) and Energy Company Obligation (ECO). Together, WHD and ECO add around £40 a year to most household energy bills.

- WHD is an obligation to provide a bill rebate of £140 a year to customers on certain benefits. It adds around £12 to the annual bill of each customer of an obligated supplier.
- ECO is an obligation to provide energy efficiency measures such as insulation. It is currently estimated to cost around £640 million a year, adding around £30 to the bill of each customer of an obligated supplier.

Currently, only the larger energy suppliers are legally obliged to provide WHD and ECO. Smaller and medium-sized suppliers are exempt.

- Suppliers are obliged to provide WHD only once they reach 250,000 customer accounts.
- Even when suppliers reach 250,000 customer accounts, they don't have to meet the full obligation straightaway. It is phased in, at an increasing rate, until they reach 500,000 when they become liable for the full amount.

On average, the customers of smaller and medium-sized suppliers are richer than those of obligated (larger) suppliers. That is because better-off people are on average more engaged with the market and therefore more likely to switch.

So, these richer customers are less likely to receive direct support, through schemes such as ECO and WHD, and they avoid paying for it. Whereas poorer customers, who are more likely to receive this type of support, are also the ones who end up footing more of the bill.

In a further twist, the problem is only going to get worse. Poorer customers who receive the benefits are less likely to switch because they fear losing those benefits. Whereas more and more richer customers will happily switch to smaller suppliers.

This is all a perverse effect of the way that direct support is currently structured. Taxes which fall disproportionately on those who are less able to pay are called regressive taxes and are generally considered to be unfair. We believe that WHD and ECO are both the equivalent of regressive taxes.

The scale of the unfairness in the market is increasing. There are only 12 obligated suppliers. In total, there are now more than 60 suppliers in the UK retail energy market. That means only around one in five suppliers provide WHD and ECO. The market share of exempted suppliers (7%) roughly translates to 1.5 million customers who do not have to pay to support those who are more in need.

The unfairness inherent in the smaller supplier exemption is self-reinforcing and getting worse. The cost advantage it provides attracts more suppliers to the market, but these suppliers do not want to serve vulnerable customers. The number of customers who escape the costs of providing schemes such as the Warm Home Discount and the Energy Company Obligation is rising. The increasing costs of direct support are being shouldered by a smaller number of customers. The small supplier exemption is outdated and should be removed by changing the law immediately.

