

Consultation Response

Price cap - Statutory consultation on changes to wholesale methodology

Office of Gas and Electricity Markets (Ofgem).

June 2022.

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About this consultation

Ofgem launched this consultation to seek the views of stakeholders on their proposal to change the methodology of the default tariff price cap. The core component of their proposal is to move to quarterly price cap changes, allowing for cap changes four times a year, rather than the present biannual changes which routinely take place in October and April. Ofgem are also proposing a shorter notice period of 25 working days between setting the cap level and it taking effect as well as alterations to the wholesale methodology to include backwardation costs.

Key points and recommendations

- Age UK reinforces its strong opposition to Ofgem’s proposal for quarterly price cap changes as it represents an unacceptable risk to consumers.
- Quarterly cap changes pose a significant threat to the health and wellbeing of vulnerable older consumers as it opens the door to dangerous winter price rises.
- Energy bills are generally higher during colder periods, and we believe the winter cap change would be consistently more expensive for a typical consumer.
- Ofgem’s present proposal for a price cap change on January 1st means prices could increase during the coldest period when older people need their heating most.
- Our recent research showed that many older households on the lowest incomes report routinely turning down or turning off their heating in response to rising bills.
- A January 1st cap change risks a cascade of winter self-disconnections from the 1 million older households reliant on a prepayment meter (PPM).
- Ofgem must abandon its plans for quarterly cap changes and enact triannual changes instead – avoiding any price increases during the winter months.

About Age UK

Age UK is a national charity that works with a network of partners, including Age Scotland, Age Cymru, Age NI and local Age UKs across England, to help everyone make the most of later life, whatever their circumstances. In the UK, the Charity helps more than seven million older people each year by providing advice and support. It also researches and campaigns on the issues that matter most to older people. Its work focuses on ensuring that older people: have enough money; enjoy life and feel well; receive high quality health and care; are comfortable, safe and secure at home; and feel valued and able to participate.

Response

We welcome the opportunity to respond to this consultation¹. Ofgem's energy price cap is designed to ensure default tariff customers pay a fair price while ensuring suppliers can charge the efficient cost level for energy. While Age UK is cognisant of the issues faced by energy suppliers in the last few months, we are committed to ensuring that the needs of older consumers, particularly those in vulnerable circumstances, are foremost in the minds of policy makers and Ofgem.

Since late last year Age UK has responded to a range of Ofgem proposals for energy market reform. Motivated by the wholesale energy price crisis and related supplier failures, Ofgem's proposed modifications are intended to improve the long-term sustainability of the energy market. Chief amongst its suggested reforms are alterations to the price cap methodology, including a move to quarterly cap changes – meaning the default tariff price cap would change four times a year instead of the present two.

Age UK has consistently reinforced the risk this reform poses to older consumers². Annual energy bills for the typical customer are likely to remain above £2,000 well into 2024³ and longer-term trends suggesting even by 2030 it is unlikely we will see prices fall to pre-2021 levels⁴. With this seemingly permanent move towards higher prices, the ramifications of Ofgem's decision could prove devastating for vulnerable consumers for years to come. Having overviewed Ofgem's latest arguments our position remains the same – quarterly cap changes present an unacceptable long-term risk to vulnerable older consumers.

Ofgem's present proposal is for a winter cap change, expected to fall on January 1st. This would represent a significant risk to older consumers during the winter as prices are likely to increase at the start of the coldest period of the year. Older people are more likely to live with health conditions which require more heating or energy use⁵, making them particularly vulnerable to the impact of living in a cold home. The latest industry assessments suggest the 2023 Q1 quarterly cap change will represent an increase in consumer costs, tipping the typical customer's annual bill over £2,900 from January⁶. Ofgem's own analysis shows that energy bills are generally higher during colder periods as demand increases⁷. It is our view that the winter cap change would be consistently more expensive.

Our recent research into the impact of price rises showed that many of the lowest income older households report routinely turning down or turning off their heating in response to rising bills⁸. A January cap change risks vulnerable older consumers self-rationing their energy use and a cascade of winter self-disconnections from the 1 million older households reliant on a prepayment meter (PPM)⁹.

Had Ofgem been able to enact quarterly cap changes last year it is plausible that the typical household would have seen an increase in their energy bills of around 54% on New Year's Day 2022¹⁰. Prior to the Government's announcement of additional financial

support, Age UK estimated that 2 million older households would not have enough income to cover their essential spending in 2022-23¹¹. Spiralling energy prices and increases in the wider cost of living have proved completely overwhelming for older consumers this spring. But if Ofgem had dumped higher energy prices onto consumers back in January it would have presented a nigh-on impossible task for older households struggling on low and modest incomes. This would have inevitably fuelled an epidemic of self-disconnections with many going through the coldest periods foregoing meals, not heating their homes, and avoiding the use of day-to-day appliances as temperatures dropped.

Ofgem's proposals risk this scenario playing out in the future. As a result, Age UK proposes an alternative – triannual cap changes. This would mean the price cap would be changed three times a year instead of the proposed four, with a change in mid-November, March, and July¹². This approach would avoid price increases during the winter while still allowing Ofgem to make more regular cap changes which more appropriately balance consumer and supplier risks. Alongside a triannual cap change, Ofgem's current and proposed reforms would be adequate to mitigate supplier risks while ensuring sufficient consumer protection. It is our view that the temporary cap reopener and new proposals for reducing the two-month notice window to just 25 days, combined with triannual cap changes, would be sufficient to comprehensively alleviate supplier risk, alongside many of the wider reforms Ofgem have already implemented.

Proactive enforcement of existing rules, an improved regulatory framework, better data sharing, and higher standards to market entry would also help to avert future supplier failures. Ofgem must ensure greater emphasis is placed on these reforms rather than pursuing changes which could undermine consumer safeguards.

Ultimately, Ofgem must avoid falling into the trap of crisis thinking which leads to a long-term undermining of existing consumer protections. With the price cap set to be extended beyond 2023 it is essential it is fit for purpose and continues to provide price protections over the winter months. We strongly encourage Ofgem to recognise that quarterly cap changes present a completely unacceptable long-term risk to vulnerable consumers. The regulator must pursue a triannual cap change approach and abandon its plans for quarterly changes.

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- ¹ Ofgem, 2022. Price cap - Statutory consultation on changes to the wholesale methodology. Ofgem. [Online]. Accessed: <https://www.ofgem.gov.uk/publications/price-cap-statutory-consultation-changes-wholesale-methodology>. [Accessed 28/05/22].
- ² Age UK, 2022. Consultation on Medium Term Changes to the Price Cap Methodology. Age UK. [Online]. Available at: <https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/consultation-responses-and-submissions/safe-at-home/consultation-response---consultation-on-medium-term-changes-to-the-price-cap-methodology-ofgem.pdf>. [Accessed 28/05/22].
- ³ Cornwall Insight, 2022. Hopes fade for a significant price cap drop in 2023 and 2024. Cornwall Insight. [Online]. Available at: <https://www.cornwall-insight.com/press/hopes-fade-for-a-significant-price-cap-drop-in-2023-and-2024/>. [Accessed 22/05/22].
- ⁴ Cornwall Insight, 2022. Energy prices to remain significantly above average up to 2030 and beyond. Cornwall Insight. [Online]. Available at: <https://www.cornwall-insight.com/press/energy-prices-to-remain-significantly-above-average-up-to-2030-and-beyond/>. [Accessed 22/05/22].
- ⁵ BEIS, 2021. Annual Fuel Poverty Statistics in England, 2021 (2019 data). Department for Business, Energy, and Industrial Strategy. [Online]. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/966509/Annual_Fuel_Poverty_Statistics_LILEE_Report_2021__2019_data_.pdf. [Accessed 05/08/21].
- ⁶ Cornwall Insight, 2022. Price Cap predictions soar as EU sanctions on Russia cause volatility in the wholesale market. Cornwall Insight. [Online]. Available at: <https://www.cornwall-insight.com/press/price-cap-predictions-soar-as-eu-sanctions-on-russia-cause-volatility-in-the-wholesale-market/>. [Accessed 13/06/22].
- ⁷ Ofgem, 2021. Adapting the Price Cap Methodology for Resilience in Volatile Markets. Ofgem. [online]. Available at: <https://www.ofgem.gov.uk/publications/adapting-price-cap-methodology-resilience-volatile-markets>. [Accessed 30/12/21]. Pg10.
- ⁸ Age UK, 2022. It Doesn't Add Up: the hard times facing millions of pensioners. Age UK. [Online]. Available at: <https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/reports-and-briefings/it-doesnt-add-up/it-doesnt-add-up---campaign-report.pdf>. [Accessed 28/05/22]. Pg17.
- ⁹ Age UK analysis of the 2019-20 Living Costs & Food Survey. Older households are defined as households with at least one person aged 60 + residing there.
- ¹⁰ This is based on bringing forward the 54% price cap increase witnessed on April 1st 2022. In practice the actual value of a price cap change on January 1st 2022 may have been higher or lower than this.
- ¹¹ Age UK, 2022. It Doesn't Add Up: the hard times facing millions of pensioners. Age UK. [Online]. Available at: <https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/reports-and-briefings/it-doesnt-add-up/it-doesnt-add-up---campaign-report.pdf>. [Accessed 28/05/22]. Pg6.
- ¹² Age UK, 2022. Consultation on Medium Term Changes to the Price Cap Methodology. Age UK. [Online]. Available at: <https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/consultation-responses-and-submissions/safe-at-home/consultation-response---consultation-on-medium-term-changes-to-the-price-cap-methodology-ofgem.pdf>. [Accessed 28/05/22].