Debt strategy

A ‘reset’ and ‘reform’ for customers in debt

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As a result of the energy crisis, we are seeing energy debt at levels we’ve never seen before. Despite prices dropping from their peak and now stabilising, the overall debt burden remains stubbornly high. Energy is one of many critical bills a consumer must pay and faced with multiple financial pressures, many households are getting into deeper debt with their energy suppliers.

Energy debt is now one of the most common reasons for seeking debt advice. Energy debt and arrears have risen by 91% in the last two years, and 75% sits with customers who are not on repayment plans. While energy prices have gone up to account for this, it does not translate to individual consumers’ debt being ‘cancelled’.

How we handle debt in our household energy system is based on several underlying principles. Energy is an essential service, and going without energy, even for a short time, can have serious consequences for people. And in a competitive energy market, suppliers must be able to cover the efficient costs of providing the service, including the cost of debt. These costs are recovered through consumer bills.

This obviously creates intense pressures on those households that are in debt. Any debt can be stressful, but consumers in energy debt, or at risk of going into debt, are more likely to cut back or go without energy. This can cause harm, leading to cold, damp homes and ill health. For people in a vulnerable situation, it can create a risk to life. And while the industry is much better at protecting vulnerable consumers, with disconnections due to debt now very rare, we are seeing high rates of self-disconnections and consumers who are rationing their energy use.

This situation is also harmful for those consumers who aren’t in debt, because everyone’s energy bills increase due to the rising costs creating by those unpaid bills. Those who are just managing to stay on top of their bills are seeing an increase because others are in debt.

Earlier this year, we set out our intention to take a step back and look at issues of affordability and debt. In doing that we were able to gain a better picture of the current state of debt in the market, what has driven it, and what we need to do about it now.

Through that process, we've identified areas that need urgent attention if we are to achieve a sector with consumer-centric debt management practices that are sustainable for both individuals and for the sector, at the lowest possible cost.

First, that the level of debt we are seeing in the energy system now is caused by the largest global energy shock in a generation – and it will need a bespoke solution.

Second, that the handling of debt by energy suppliers isn't as consistently good as it should be.

Today, we're setting out our plans to reset the debt, and reform the system.

We think there is a case to **reset the debt** situation that has built up. An option we could explore is to create a £0.5 to 1bn fund to directly reduce the debt of customers who are in both vulnerable situations and financial difficulty as a result of the energy crisis. A debt relief scheme could be available to customers of any supplier, and could be delivered automatically or claimed through consumer organisations and charities.

The scheme could provide a one-off reset of the debt built up over the energy crisis to give customers in extreme difficulties a chance to recover. We are consulting on whether such a scheme is desirable and feasible and, if so, how it might work.

We also want to **raise debt standards**. We think there is more suppliers can do to prevent customers getting into debt and support them through it to get them into debt recovery in a compassionate, sustainable way. To do this, we are proposing a 'debt guarantee' so it's clear what consumers in payment difficulty can expect from their supplier, standardise the approach suppliers take to assessing a customer's ability to pay and, critically, require suppliers to work with any chosen charity or consumer organisation working on behalf of customers. Reaching out to ask for help is the most difficult step – we should help consumers take that step with more confidence and make the whole process easier for them.

It's clear we also need to **prevent debt** from being built up in the first place – which will lower the cost of debt for all consumers. We know that features of the market make it more likely to build up debt than in other sectors, so we want to look at whether our regulations and incentives are in the right place to help stop debt from occurring.

Ofgem alone cannot make energy affordable for all consumers. The impacts of the energy crisis are long lasting, and while bills are far below their peak, they are still unaffordable for many people. We will continue to work with the Government on long-term solutions on affordability and debt advice, which are critical to sustainable debt management in the future.

It will take time for consumers and the market to recover from the extreme strain experienced during the energy crisis – but on debt, that recovery will take too long. The plans we have set out today would address the problem, and put guard rails in place to prevent it happening again.

Tim Jarvis
Director General, Markets

We want sustainable debt management in energy, but we are not there yet

We want all customers, no matter what supplier they are with, to receive compassionate and empathetic support which they don't always need to explicitly ask for. It can be challenging for consumers in debt, or at risk of debt, to reach out for help. For these customers, it's crucial that the service they receive is at its best. A poor experience could prevent them from getting the support they need to help them afford their energy bills and lead to unnecessary worry.

We understand that many consumers are reluctant to contact their energy supplier or don't see why their supplier would be able to help them if they are unable to pay. This can make it even more challenging for a supplier to get the help to these customers when they are in need. This is why the relationships with trusted third parties, like consumer organisations and charities are so critical.

We expect suppliers to take all steps to prevent consumers from getting into energy debt wherever possible but if they do, they are supported to address their debt problems. This means consumers who are struggling to pay their bills can:

- Receive timely, and accurate bills from their supplier.
- Have appropriate, tailored and proactive advice on the best way to manage payments if they are in financial difficulty without ever feeling they have to go off supply.
- Easily access and understand empathetic and sustainable options to manage their debt with their supplier. Receive forbearance, for example like payment holidays, when they need it.
- Have a choice of any consumer group or charity to help them and receive the same level of support, in a timely manner.
- Have peace of mind that if they are in a vulnerable situation they will never be forcibly without energy supply, and they shouldn't feel the need to go off supply to manage their energy needs.
- Have confidence that all suppliers are keeping the cost of debt to a minimum.

We have seen some great practice from some supplies providing tailored, compassionate and specialist advice for those struggling to pay. But this is not consistent across all suppliers.

Case study: Maggie

"If I'd been aware of it [hardship grant] during the period when it [debt] was under £1,500, I would have actually applied for help to get it cleared"

Situation: Last year Maggie received a bill for £2,000. After waiting 1hr 45mins to speak with her supplier, she was offered a repayment plan, which she agreed to. No confirmation about this came and she then received a new bill for £3,000.

Experience: She got in contact again and was told the repayment plan hadn't gone through (the system rejected it as the repayment amount was too low). This made her very "stressed" and "anxious". She was offered another plan with a slightly higher amount. Again, she received no confirmation, then was contacted by a debt collection agency demanding payment. Initially she was scared to call them but found them "kind" and "sympathetic". They thought she could get a hardship grant, however her supplier said she was not eligible. This exacerbated the debt further and had a detrimental impact on her mental health.

Case study: Amina

Situation: Amina is 54 and is unable to work due to her disability. She realised she was £300 in debt to her energy supplier when the money was taken from her bank account.

Experience: After this, she rang them up and got through quickly, in 15 minutes. Her supplier returned the money to her bank account and gave her a one month's payment holiday. She arranged to be put on a repayment plan. She was also put on the PSR which she said "made a difference" and was "reassuring" as she gets notice of advanced work and would be contacted in case of an outage.

From: Consumers' experiences of debt and affordability support from suppliers

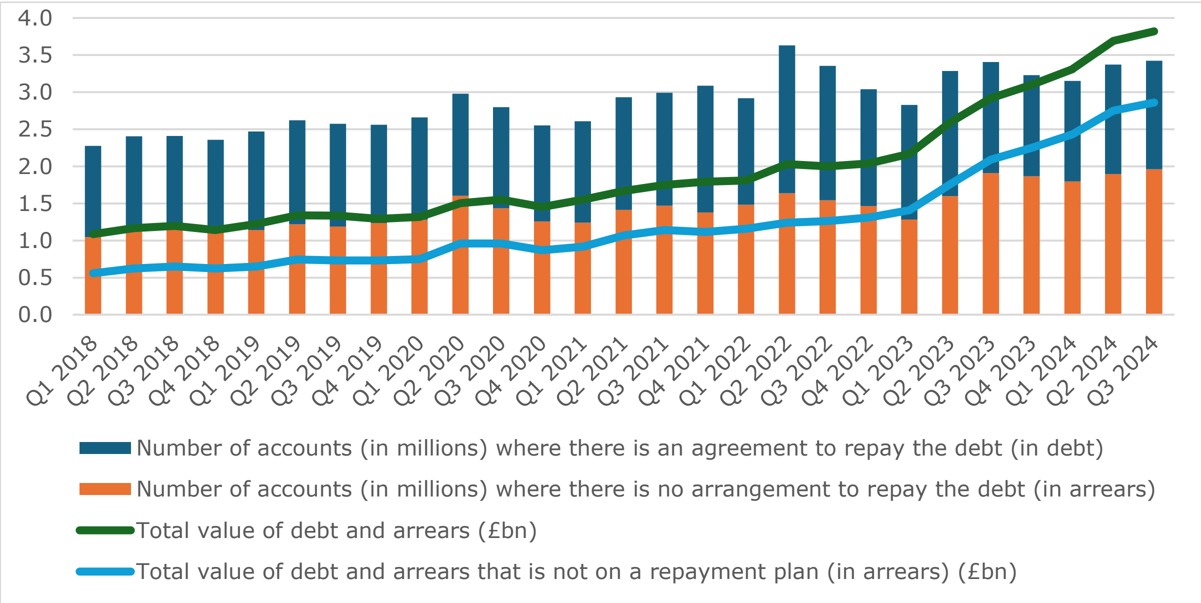
Debt and arrears levels are growing significantly

Over the last two years alone there has been a 91% increase in energy debt/arrears and the most recent data shows a record high of £3.82bn. As shown in Figure 1 below, nearly three quarters of this is accounted for by customers not on a repayment plan (arrears).

Although the number of those in debt/arrears is increasing (see Figure 1), it is not increasing as fast as the value. This means that those in debt are owing much more. The average debt (of those in debt) has risen by over 50% in the past two years.

For those on a repayment plan, some are unlikely to ever repay the debt due to the scale of energy debt, in combination with the length of repayment plans. For example, we have also seen repayment plans as long as 10 years as suppliers seek to provide affordable repayment plans for very high levels of debt.

Figure 1 – total number of domestic accounts in arrears/debt, the total value of arrears and the total value of debt and arrears between Q1 2018 and Q3 2024, debt/arrears is defined as existing over 91 days (Source: Debt and Arrears Indicators | Ofgem)



Rising debt affects all consumers, particularly those in vulnerable situations

Energy debt causes direct harm to consumers. To stay on top of energy bills, consumers may self-ration or self-disconnect their energy leading to harms associated with living in a cold, damp home. Falling behind on bills and being in debt can negatively impact credit ratings which affects household finances, including the ability to access credit. Consumers can also be at risk of harm if inappropriate or aggressive debt recovery methods are used. These cumulative impacts of debt build-up can have consequences on consumers' mental and physical health including experiences of stress, anxiety, and suicidal ideation (The State We're In - Money and Mental Health, Suicide prevention in England: 5-year cross-sector strategy - GOV.UK).

Higher debt and arrears leads to higher prices for *all* consumers as suppliers look to recover the cost of debt. The price cap includes an additional allowance to facilitate this. Where the rise in debt and arrears are, in part, a consequence of factors outside of suppliers' control, the allowance in the cap needs to reflect the resulting costs.

Finally, unsustainable levels of debt and arrears risk destabilising the market and making it more difficult for suppliers to focus on what we as the regulator want to see from suppliers: excellent customer service, innovation in goods and services for the benefit of consumers, and competition to provide the best deals for all.

There are features of the market which make it more likely to build up debt

In most industries, customers that do not pay for something would stop receiving it - energy is different. It is an essential good, and going without it, even for small periods can have serious, even catastrophic consequences. As a result, disconnection is rare and the use of involuntary prepayment to manage debt is strictly controlled. The consequence is we effectively mandate suppliers offer credit towards energy bills for most customers. Suppliers are also not required to undertake credit checks for new customers (and the Universal Service Obligation would require them to offer a supply contract even if a customer fails). So, while the impact of debt and arrears may be harmful, our view is that the lack of access to energy would be worse.

Competition for indebted customers is also low - suppliers can block credit customers with debt as low as £100 from switching. PPM customers can switch with up to £500 of debt per fuel but are much less likely to switch. This means the market is not providing 'better deals' for these customers.

While it is relatively easy to get into debt, the tools for collecting debt remain an issue. The practice of forced disconnections is now, rightly, very rare and we do not see significant use of 'blunt' tools such as bailiffs or County Court Judgements (CCJs) to manage energy debt and we have actively limited the use of involuntary PPM. The use of these 'blunt' tools is not appropriate for all situations and over reliance on them can lead to long term inefficiencies in debt management. However, without these tools at all, debt levels are likely to be higher than they might otherwise be. We have worked hard with the sector to reform how energy suppliers use PPM installations to manage debt in an appropriate and proportionate way.

We have taken steps to help consumers

We have worked hard with the suppliers, consumer representatives, charities to put in place essential support for customers struggling to pay. This includes:

- During the energy crisis suppliers, at our request, stopped installing PPMs to prevent debt without the customers consent. We are allowing 'involuntary' installations now but under very strict rules (which were strengthened in November 2023).

- We introduced 'additional support credit' (ASC) rules which require suppliers to offer credit to vulnerable prepayment customers at risk of self-disconnecting. This provides crisis support in instances of self-disconnection, but, due in large part to affordability challenges, the use of ASC has become one of the main mechanisms to keep PPM customers in vulnerable situations on supply. This has led to us introducing ASC bad debt allowances in the price cap.

- New rules – which came into effect in December 2023 – to drive better customer service standards; making it easier to get help if they are struggling to pay, and encouraging the use of 'debt repayment holidays' to give customers breathing space when they need it.

- Removing the 'pre-pay premium' by making pre-payment the lowest cost payment method to use.

- Launch of our 'Consumer Confidence' programme which is about driving up customer service standards by creating a consumer centric culture.

- Taken enforcement and compliance action against suppliers that have failed to comply with our debt obligations. This and wider action to drive up standards has resulted in the largest ever funding in our Energy Redress Scheme of £35 million for 2024. These funds are available as grants to charities and community energy groups.

But there is more to do. We are proposing a 'reset and reform' of debt management practices.

Resetting the debt

There are a range of financial support available to customers through voluntary supplier hardship funds, Warm Home Discount Industry Initiatives and debt advice; but in our assessment this support is much smaller than the scale required. We are working closely with Government to help consumers to afford their energy bills, but this is not something the regulator can tackle alone. However, the rising debt and arrears is causing higher costs for all consumers, including those already unable to pay and we need to break the cycle. While suppliers are 'writing off' a proportion of debt they do not expect to recover this does not translate to reducing the burden of debt for individual customers.

We are seeking views on whether a 'debt relief scheme' should be introduced which could create a £0.5 to 1bn debt write-off to directly help those customers in severe payment difficulty. We are considering some options for how a scheme could be financed. Our analysis shows it would be cost neutral, in that it would lead to lower overall bills against the counterfactual of not intervening, and contribute to lowering the overall cost of debt and therefore bills over time.

The funds in a debt relief scheme could be used to directly help individual customers in payment difficulties, unlike price cap allowances. This could help build trust and confidence in the sector but also better incentivise behaviour change. For instance, the scheme could encourage input of consumer money via debt matching contributions from indebted customers in receipt of support.

A debt relief scheme would be a one-off intervention, targeted solely at debt accumulated during the extraordinary circumstances which arose during the energy crisis. This would be to help customers who are struggling to pay back historical debt.

We are keen that the design of a debt relief scheme follows some key principles which: (1) avoids perverse incentives for consumers and suppliers; (2) is fair and consistently applied to consumers regardless of their supplier; (3) targets those with demonstrable affordability issues as far as possible; (4) delivers in a timely manner.

We expect those that access the scheme are the most in need and that it creates the right incentives beyond the life of the scheme. This is why we would be considering eligibility criteria that would require suppliers to demonstrate 'best practice' in debt management, but also that consumers accessing a debt relief scheme are willing to contribute to repaying their energy debt.

Raising debt standards

Financial support needs to be coupled with improved standards across the debt pathway

Whilst our Standards of Conduct require suppliers to treat customers fairly (the 'customer objective'), we want to explore a new approach to raise standards for consumers along the debt pathway. Regardless of a customer circumstance or supplier, suppliers should be taking decisions that place customer experience at the heart of their business model. This is a critical part of our new 'Consumer Confidence' programme. We know the existing rules for debt can be complex and it's not always easy for a customer to know what to expect from their supplier when they are in financial difficulty.

To simplify this for both suppliers and customers, we are proposing to develop a 'debt outcome' so suppliers understand what 'good' outcomes look like, and customers know what to expect when they are in debt – a 'debt guarantee'.

Our proposed debt outcome is: *Domestic customers in, or at risk of debt or arrears receive proactive, tailored, and consistent customer service that meets their needs and helps them sustainability manage their debt or arrears.*

We will work with consumer groups, charities, and industry to set out what a customer can expect in practice under this outcome and fully develop a debt guarantee.

We would expect suppliers to be able to demonstrate and evidence how they have met the proposed new debt outcome. By focussing on the end outcome rather than the means, we hope it will encourage suppliers to develop innovative methods and solutions to support customers struggling with their bills.

It is important that repayment plans are affordable

There is evidence that households are not only struggling to afford their energy but also with repayment plans. When a household gets into debt with their energy supplier, it is critical that debt repayment arrangements are based on robust ability to pay assessments.

Whilst we welcome the positive steps that suppliers have made in ensuring repayment plans are sustainable and affordable we think more needs to be done to standardise this for consumers.

With this in mind, we are proposing options to standardised ability to pay assessments and require suppliers to accept offers of repayment from FCA-authorised debt advice agencies unless there is an exceptional reason otherwise. This means that when setting a repayment plan consumers will be clearer on what information is expected of them, no matter what supplier or consumer group or charity may be helping them. This should result in a smoother and quicker process for the consumer.

More positive collaboration can better support those in debt

We know consumer trust in energy suppliers is low, and those customers in payment difficulty sometimes find it hard to reach out for help. More positively, when customers do reach out for support from their supplier, most report positive experiences. 69% of those that had received support from their supplier for help with running out of credit/falling behind saying that they were satisfied with the support that they received. (Energy Consumer Satisfaction Survey: July 2024 | Ofgem)

However, we also know that suppliers are not always best placed to adequately support all the needs of consumers with complex cases. For these people, consumer groups and charities can act as a lifeline to help them navigate their affairs when they feel unable to do so themselves. Despite this, consumer groups and charities have raised concerns around their ability to advocate on behalf of their clients.

We are concerned there are inconsistent approaches to enabling consumer representatives to act on behalf of customers. Similarly, we also understand that for suppliers it can be challenging to accept authorisation from different consumer groups and charities who may not use standardised or centralised communication or processes. We believe there is scope for improvement to reduce friction and improve trust on both sides. We are proposing to expand and make clearer our rules and expectations around third party authorisation which can drive consistency and higher standards.

To help customers struggling with their bills, suppliers refer customers to consumer groups and charities to provide additional support. While this can work well, consumer groups and charities have also told us that referrals could be improved. Equally, it can be challenging for suppliers to know how best to support customers and how to navigate issues around data protection and consent. We are proposing options to work with stakeholders to improve the effectiveness of referral pathways and consider whether suppliers could be required to conduct warm referrals (where a supplier refers the customer to another organisation directly without the customer having to make a second call) to help provide consumers in vulnerable situations with more hands-on support.

Preventing debt and enabling appropriate recovery of debt

Debt and arrears in the energy sector raises costs for everyone and it’s critical we minimise this cost, both by the rules we have today but also thinking about the impact the broader market design may have on it. Our proposals today are incentivising putting the customer at the centre of the decision-making process for debt and getting the support to those that need it, rather than relying on debt recovery tools only.

We are conscious that these proposals could be a step in the right direction to a system that is centred around the needs of a customer in debt, but we also have a duty to protect the interests of all consumers. We ultimately want a consumer centric system for managing debt that long term is lowest possible costs for all consumers.

The design features of the energy market means that consumers can build up debt more quickly than in other sectors. This is primarily driven by energy being an essential good that a lack of access to can be very harmful for customers. Although debt and arrears have risen mainly because of the energy crisis, it is important to reflect on what we can learn from other sectors in Great Britain and from the energy sector in other countries.

We see other sectors and countries have a different approach to 'access to credit' to limit the ability for consumers to build up debt. For instance, using credit checks before supply is established, or the use of security deposits. Some countries do not have prepayment meters, but instead use disconnections for customers that are not in a vulnerable situation. However, what was also common was the use of financial support for customers on low incomes or in financial hardship, for instance like social tariffs, state benefits or a 'funding pool'. We need to ensure the right balance between protecting vulnerable consumers, and treating those in debt with sensitivity, with protecting the interests of all consumers. We need to give all consumers confidence that the costs of debt are as low as possible which includes helping people to avoid unnecessary or problem debt and providing safe mechanisms for suppliers to recover debt appropriately.

We want to limit the harm debt may have on the system as a whole and therefore we will be exploring whether there is more we can do to prevent debt from building in the first place. We also need to ensure we have a shared approach between Government, regulator and the industry on how debt should be recovered and what reasonable costs of bad debt should be socialised.

For example, this could include whether more can be done to prevent 'shock bills', whether we can/should refine the approach to change of tenancy, whether the use of credit checks should be more common and what we can do to advance the upgrade of metering technology, like smart metering, to support more accurate billing. And as we apply our new rules on the involuntary installation of prepayment meters, we should explore what the role these and other forms of debt control and collection should be alongside working with Government on how data sharing can help identify vulnerable households.

What is clear to us is that accurate billing is fundamental to allow a customer to effectively budget. As part of our Consumer Confidence work, we will be reviewing the rules around billing accuracy and practices. This includes considering new rules to improve and incentivise better billing accuracy and debt support, including default monthly bills for households and reviewing the back billing rules to reduce how far back a supplier can bill a customer where the error was the supplier's fault.

Get involved and have your say

The proposals outlined are the focus of two consultations, 'Resetting the energy debt landscape: the case for a debt relief scheme' and 'Improving debt standards in the domestic retail market'.

Both will close for written responses on Thursday 6th February 2025 and we are happy to receive joint responses to both consultations. We will be running stakeholder engagement sessions during the consultation period to give a chance for discussion.

On 'resetting debt' we are keen to hear your views on:

- How to identify customers who are eligible for the debt relief and views on our alternative eligibility criteria.
- To what extent customers should engage with their supplier, or debt advice charity, to receive support.
- The options for how to fund and socialise the costs of the scheme.
- Our proposal for suppliers to deliver and Ofgem to administer the scheme.

On 'raising debt standards', we are keen to hear your views on:

- Our proposals for a 'debt outcome' and 'debt guarantee'.
- Standardising and improving the consistency of ability to pay assessments.

- How to achieve better working between suppliers, and consumer groups and charities.

- What our longer-term priorities should be in protecting consumers across the debt pathway in prevention, support and recovery.

Following the closure of these consultations, we will carefully consider and review the responses. We will aim to publish an update on these by Spring 2025.