



ALL PARTY PARLIAMENTARY
GROUP ON POVERTY

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Report of the APPG on Poverty inquiry into the poverty premium

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Introduction

The All-Party Parliamentary Group on Poverty aims to increase understanding of poverty among parliamentarians and to seek all-party solutions. It held an inquiry over the course of 2018 to investigate the concern that low-income households continue to face higher costs for essential goods and services – the poverty premium.

Life is getting increasingly tough for the 14 million people in the UK living in poverty¹ – social security payments have been frozen for three years, the roll out of universal credit has caused great hardship, the benefit cap has broken the link between a family's needs and the support they get and the two-child limit has been introduced, resulting in a particularly harsh impact on large families.

Although we have record employment, work is not always the route out of poverty it should be and many people are in low-paid and insecure jobs that keep them in poverty. We are also seeing increasing numbers of people in crisis situations where they have had to suffer the indignity of relying on emergency food aid to avoid destitution. Against this backdrop, the fact that being poor also means having to pay more for essential goods and services is a glaring injustice.

The injustice of the poverty premium is compounded by the fact that many instances involving a premium are impossible to avoid – we all need to heat our homes, buy groceries, fridges and cookers to feed our families and many of us living in rural areas cannot avoid the cost of running a car. We all experience periods of unexpected expense – for example, because the washing machine has broken down and there is laundry to be done. We may all be consumers, but the market fails those of us who are living on a very low income as this means fewer choices about which services to use, how to spread additional costs and how to manage credit in such a way as to avoid it becoming unmanageable debt.

The aim of this inquiry was to shine a light on the poverty premium, hear from those affected and also to highlight some of the emerging solutions coming from businesses, social enterprises, charities and others. The inquiry was not intended to be an exhaustive study of all areas affected by some sort of poverty premium but to look closely at some of these areas, examine work underway to tackle the poverty premium and to learn from experts in the field about what more could be done to make life better for those affected.

We are grateful to those who were willing to share their personal experiences of encountering the poverty premium, either in person at one of our meetings, or through submissions to the inquiry. Their experiences added a very valuable dimension, keeping us focused on the very real human impact of what might otherwise be seen as a challenge of business processes and market regulation.

Throughout the inquiry we were also grateful for the assistance of many academics, charities, social enterprises and businesses that have studied the area in depth and are proposing solutions. A notable example was the Fair by Design² campaign and its fund³ investing in innovative enterprises to tackle the poverty premium. We are grateful for their support for our inquiry and while we do not wish to duplicate their efforts nor the other very valuable work in this area, we have drawn on it where appropriate. The full list of contributors can be found at the end of this report.

¹ Relative low income after housing costs, House of Commons Library research briefing: "Poverty in the UK", 2019

² www.barrowcadbury.org.uk/what-we-do/fair-design-campaign/

³ www.fairbydesignfund.com

We were greatly encouraged by the extent of work already underway in this field by businesses, charities, social enterprises and housing providers, taking action against the poverty premium and adjusting their business models or developing solutions that could really make a difference. Some of these are highlighted in our report but there are many more that we haven't had space to include. A full list of written submissions can be found on the APPG's website.⁴

While they may not solve all aspects of a really complex problem, these activities are a good start and illustrate that with good intentions, commitment and the investment of time and resources, the poverty premium can be tackled. It may not always be the easy thing to do, but it is the right thing to do.

Why does being poor cost more?

The term 'poverty premium' describes the extra costs that low-income households face for goods and services, including energy, insurance and groceries, in comparison to households on higher incomes. In other words, life costs more if you are poor.

While this concept is not new, the effects of the poverty premium continue to entrench poverty for low-income households and lead to greater levels of debt, which in turn reduces the household income available to spend on essentials.

Over the last ten years, academics and civil society have attempted to quantify exactly how much this premium costs poor households each year. The University of Bristol's calculation⁵ amounts to £490 a year on average, with some households paying up to £2,250 a year extra. Analysis by the End Child Poverty⁶ coalition found that a typical family on a low income could be paying around £1,700 a year more for the same essential goods and services than a similar higher-income family. Research by Scope⁷ found that disabled people pay a financial penalty on everyday living costs that is on average £583 more a month through a combination of the additional costs of disability and the poverty premium.

Poverty premiums arise from an inability to access better deals for a variety of reasons, including geographical barriers, digital exclusion and a need for tight budgeting control. It is also worth noting that the estimated cost of the premium does not include the extent to which low-income households 'go without', a cost-saving behaviour identified by multiple participants throughout this inquiry.

For those with the ability to buy food and other household essentials in bulk and store them, there are numerous options to pay a lower price. These discounts are not limited to food and household goods. For many items, consumers on low incomes are penalised because they can't afford high upfront costs in order to save money overall. This includes, for example, the cost of travel season tickets, insurance and mobile phone contracts. The savings made by paying for train travel using a monthly or annual season ticket, in comparison to buying a ticket on a daily or weekly basis, can be from hundreds to thousands of pounds a year. One impact of the poverty premium is the fact that lower-income workers will often pay more on their commuting costs than their better-paid colleagues if they lack access to credit.

⁴ www.appgpoverty.org.uk

⁵ Davies S. & Finney A. (2017) 'Making the Poverty Premium History – A practical guide for business and policy makers', University of Bristol Personal Finance Research Centre

⁶ End Child Poverty (2017) 'Feeling the Pinch'

⁷ John E., Thomas G. and Touchet A., (2019) 'The Disability Price Tag'

Increasingly the market for goods and services favours digitally-literate consumers. Service providers have developed automated models that rely on customers to manage their transactions online. These models that reduce the need for person-to-person interaction are cheaper to supply, so services can be provided at a lower cost.

While the use of technology may open up more choices to some consumers on low incomes, others may be further excluded as a result of a lack of digital skills, poor access to the internet or a preference for in-person interactions. The 'digital by default' design of universal credit is a notable example of how those who are already vulnerable are further disadvantaged by online services.

In 2018, 89% of UK households had internet access.⁸ However, 20% of those without reported this to be due to a lack of skills.⁹ Elderly and disabled people are disproportionately represented within this group. It is encouraging that housing associations and others are providing free 'digital inclusion' training to individuals on low-incomes in order to lessen the impact of the poverty premium on those lacking digital skills. However, local government cuts have had an impact on library services – often the only source of free internet access in non-urban areas – so that access to online services cannot be assumed even for those with digital skills.

People with disabilities face particular barriers. For example, digital exclusion from online discounts may be worsened by websites that are inaccessible to blind and partially-sighted people, while the onerous processes involved in finding good deals and switching providers in energy or telecoms act as a barrier to those with mental health problems.

Expanding digital inclusion, while important, will not work for everyone and cannot be seen as the only solution to the poverty premium.

Some businesses, regulatory bodies and others are already working to reduce the poverty premium. For instance, within the charitable sector, the Fair By Design Fund¹⁰ has been established to eliminate the poverty premium by disrupting the energy, finance and insurance markets and investing in alternatives. A number of alternative providers of rent-to-own products and essential services have emerged, and are addressing the needs of vulnerable consumers on low incomes by offering their products at a fair cost to all consumers, and using innovative ways of challenging markets that produce and perpetuate such premiums.

Regulators such as Ofwat, Ofgem and the Financial Conduct Authority (FCA) have all taken some action to tighten regulation on essential services providers and payday lenders respectively. However, these initial steps could be seen as sticking plasters in that they have not gone far enough to ensure that markets are consciously and universally redesigned to work for, rather than against, consumers on low incomes.

⁸ ONS (2018), 'Internet access – households and individuals'

⁹ ONS (2019), 'Exploring the UK's Digital Divide'

¹⁰ www.fairbydesignfund.com

Living in poverty

Living in poverty means not having an adequate income to meet an individual or family's needs and allow them to participate in society.¹¹ This might be as a result of low pay or insecure work, a sudden fall in income, additional costs relating to disability, poor physical or mental health or inadequate social security support – or a combination of such factors. When managing on a very tight budget, even small fluctuations in income or increases in outgoings can have a devastating impact.

During the inquiry, we heard from individuals about how the poverty premium causes additional hardship. Examples include:

- Struggling to keep up-to-date with housing costs, pay bills and buy groceries and other essentials.
- The necessity to do small regular shops, often using convenience stores, to manage on a low income and avoid the cost of travel. Research by *Which?* in 2017¹² found that there is a 7% premium on products purchased in convenience shops.
- Not being able to buy in bulk or shop online because of the upfront costs and minimum spend, although this can be cheaper in the long run.
- Cheaper foods and basic goods can turn out to be a 'false economy' as they may be less healthy or run out more quickly.
- Home and motor insurance cost more in areas deemed 'high risk' and it costs more to spread payments if up-front costs are not affordable.
- Free to use ATMs may not be available locally, leading to the use of ATMs that charge a fee for every withdrawal.
- Sometimes the best deals for goods and services are only available online – this means that people who do not have access to the internet, basic website skills or a bank card miss out.
- Not being on the best energy, water and telecoms tariffs (including using prepayment energy meters or being on a standard variable tariff), and not switching providers regularly – it is difficult to 'shop around' to get the best deals if bills are in arrears and a payment plan has been agreed with a particular supplier.
- 'Emergency' purchases of essential household goods can mean being forced to use 'rent to buy' or other high-cost credit schemes with payments spread over a long period. However, this means that they end up costing much more in the long run and could be lost in the event of non-payment.
- Transport costs are often cheaper with a 'season ticket' but these usually require an expensive up-front payment to obtain savings.

¹¹ Townsend P. (1979), 'Poverty in the United Kingdom'

¹² Which? (2017), 'Supermarket convenience stores charge up to 7% more'

- For disabled people living in poverty, there may be additional premiums resulting from lack of choice in relation to, for example, suitable transport, food and insurance, as well as higher use of essential goods and services such as energy.¹³
- Insecure accommodation often results in the additional costs associated with moving home frequently.

The impact of these additional costs are severe. The savings low-income households could make if the poverty premium were eradicated would help families to accrue a savings buffer, to live more healthily and with less stress, and would help prevent people from 'going without' essentials such as a warm and secure home, a healthy, nutritious diet and being able to fully participate in society.

The following section of the report explores a number of aspects of the poverty premium highlighted by the inquiry's contributors across a number of sectors, considering in particular what the problems are, what is already being done and what more needs to be done.

Financial services

Affordable credit

At some point, almost everyone will need to access credit to be able to respond to sudden unexpected expenses or to spread the cost of a large purchase. Better off households are more likely to have some savings to cover substantial, unexpected costs (such as unexpectedly large bills, a job loss or a broken kitchen appliance), and if they do require credit for these they will be able to use lower-cost options through arranged overdraft facilities and credit cards, which may even be interest-free for an introductory period. Recent research by Aviva found that families on low incomes typically have just £95 in savings and investments compared to £3,134 on average across all UK families and £62,885 among high-income families.¹⁴

Although access to an agreed bank overdraft is one of the most cost-efficient forms of lending, those on a lower income who slip into deficit unexpectedly can find themselves subject to high charges for unauthorised overdrafts and mounting charges for declined direct debits and standing orders.

The 'high-cost, short-term' credit (HCSTC) market caters to a group of borrowers who have few alternative options when they need a loan upfront to cover unexpected costs. A number of contributors to the inquiry cited HCSTC as a significant cause of problem debt. As well as the high personal cost to individuals, problem debt has a high social cost too as it frequently leads to mental health problems, such as anxiety or depression. Payday and doorstep lenders are notorious for their high Annual Percentage Rates (APR), which can place customers in great financial difficulty as interest payments become unaffordable. Research by the University of Bristol found that although a majority of low-income households opt not to use these forms of credit, the significant number who do spend an additional £120 a year repaying payday loans and £540 a year on home-collected credit.¹⁵

¹³ John E., Thomas G. and Touchet A. (2019) 'The Disability Price Tag'

¹⁴ Aviva (2017), 'Family Finances Report'

¹⁵ Davies S. & Finney A. (2017) 'Making the Poverty Premium History – A practical guide for business and policy makers', University of Bristol Personal Finance Research Centre

Contributors often cited these companies as a ‘necessary evil’ within the current climate, where budgets are stretched further and access to affordable credit for this group is not sufficiently substantial to meet the growing demand. Contributors to this inquiry highlighted that the much-celebrated decline of the payday lender ‘Wonga’, resulting from the Financial Conduct Authority’s cap on borrowing costs, would in fact leave some of the most vulnerable families in need of cash with far worse options, including illegal loan sharks. A number of contributors suggested that the demand for HCSTC had increased in England as a result of the severe cutbacks in local welfare assistance provision by local government. Local welfare assistance schemes (the Scottish Welfare Fund in Scotland) replaced the national Social Fund that previously provided crisis loans and budgeting loans. This may have inadvertently created a new market for lending to a particularly vulnerable group of people.

With the use of credit now an established part of the way people manage their finances, the need for affordable, alternative sources of credit for low-income households is clear. Traditionally credit unions and other social finance models have filled this role, but they are perhaps less appealing to borrowers looking for easy to access lending with a rapid response time. A number of businesses have emerged to fill this gap, for example, Incuto.¹⁶ Incuto provides an online banking platform for credit unions and community banks, allowing them to ‘mimic’ a customer’s experience of receiving a payday loan, but without the extortionate costs. The company’s founders identified the appeal of payday loans as a combination of fast turnaround and online access and have, therefore, produced an online service for credit unions that guarantees the payment of loans even faster than payday lenders pay.

Another social business that re-invests its profits to benefit its customers is Fair Finance.¹⁷ It aims to revolutionise financial services for people who are financially excluded, providing personal loans, business loans and money advice.

Moneyline¹⁸ offers low-value (up to £1,500), short-term loans (from 3 to 8 months) to those on benefits and with limited borrowing options, subject to affordability assessment. Lending decisions are not based on credit scores, but credit checking is used to check information and to ensure the applicant is up-to-date on other payments.

Wagestream¹⁹ helps tackle high-cost payday lending by enabling employees to access their earnings before payday, removing the need for loans, credit or interest charges. It also encourages direct-from-salary saving through Savestream. It works with employers in a way that doesn’t require them to make any changes to their payroll systems.

However, these alternatives are simply unable to match the advertising and marketing campaigns of the biggest payday lenders. As was noted in the inquiry, responsible lenders do exist, but are simply ‘swamped in a market of well-funded privately-owned scale operators’. Supporting alternative lenders to reach those who require affordable credit is therefore central to disrupting the market advantage of the HCSTC sector.

Credit-scoring mechanisms

Reliance on high-cost credit often stems directly from low-income consumers’ poor credit history, or a lack of credit history. Credit scoring is used routinely to decide whether people can access mainstream forms of lending that offer affordable interest rates, for example, bank overdrafts, loans and credit cards.

¹⁶ www.incuto.com

¹⁷ www.fairfinance.org.uk

¹⁸ www.moneyline-uk.com

¹⁹ www.wagestream.co.uk

For many individuals, the data generally used for credit scoring and creditworthiness assessments are likely to disadvantage those who may have defaulted on payments or have County Court Judgments against them. Others may lack a substantial track record as a result of limited use of financial services in the past.

Rental payments, energy and telecoms bills, council tax payments, wages and benefits are not routinely considered in credit scoring, and payments on catalogue debt, for instance, are not considered as favourably as mainstream credit cards. However, some tenants are now able to have their rental track record taken into account when making a mortgage application through a new collaboration between CreditLadder²⁰ and Nationwide through the Government-backed Rent Recognition Challenge²¹ that aims to increase the number of home owners.

Among the inquiry's range of contributors, there was a lack of consensus over whether the inclusion of further data would benefit or further disadvantage individuals on low incomes. The Creditworthiness Assessment Bill,²² a private member's bill sponsored by Lord Bird and Justine Greening MP, is currently progressing through Parliament (at the time of writing) and was endorsed by the Treasury Select Committee in its recent report, "Consumers' access to financial services".²³ It proposes that credit service providers be required to take rental and council tax payment data (where it is shared) into account when assessing a borrower's creditworthiness.

Some contributors believe that this Bill, if passed, would assist many people – currently without or with a limited credit history – with opportunities to access a wider range of credit products and services. Although the use of data-sharing to authenticate individuals' digital identities can help to increase access to financial services, including transactional payment services, current accounts and more affordable credit services, others have suggested that the most vulnerable may be further disadvantaged through inappropriate sharing of rental default and council tax payment data with lenders or credit reference agencies. These arrears may have arisen as a result of errors or delays in benefit payments with the result that individuals may suffer the consequences of delayed payments through no fault of their own.

As the wider implications of the inclusion of these datasets are currently unclear, a review of how publicly-held datasets could be shared, to improve financial outcomes for low-income and financially vulnerable households, is now needed. A Government-led, cross-sector Financial Inclusion Data-Sharing Group could lead a strategic approach to assessing which public datasets would be most effective in tackling financial exclusion. It could safely and systematically identify, test and evaluate the impact of data sharing with a focus on the impact on those most exposed to the poverty premium.

Rent-to-own retailers

The rent-to-own (RTO) market offers high-interest contracts to customers on low incomes for essential items such as white goods, technology and furniture. Renting-to-own can be seen as the only option – and as a 'lifeline' – for consumers on low incomes who lack savings or access to affordable credit. Buying goods in this way may mean the difference between having a working fridge or cooker to prepare family meals and needing to spend more on poorer-quality take-away food. However, buying goods in this way means paying extremely high interest with a typical APR of between 60% and 1,500%. Overall, people may end up paying more than double what the product was originally worth.

²⁰ www.creditladder.co.uk

²¹ www.gov.uk/government/publications/rent-recognition-challenge-using-fintech-to-help-renters

²² www.services.parliament.uk/Bills/2017-19/creditworthinessassessment/documents.html

²³ www.publications.parliament.uk/pa/cm201719/cmselect/cmtreasy/1642/164202.htm

For example, a fridge that could be bought for £494.50 outright would cost £1,092 over a period of 156 weeks (not including transport costs, installation fees and insurance) if purchased through a rent-to-own supplier. For low income consumers, especially those whose income fluctuates even slightly, these monthly payback rates can create significant problems and contribute to problem debt. Research by Citizens Advice Scotland found that 60% of their clients seek a further loan to fund their rent-to-own commitments.²⁴

A leading provider of rent-to-own household goods, BrightHouse, submitted evidence to the inquiry to explain its model.²⁵ Its view is that this model is popular because it enables the customer to use, and ultimately own, goods that they have no other way of affording. Before entering into an agreement, customers undergo a detailed affordability assessment and a key requirement is that their income exceeds their outgoings by at least £100 a month. Its contracts are hire purchase, not credit contracts, so customers can exit the contract at any time by returning the goods without the risk of a bad credit record. BrightHouse argues that if it did not exist, there would be no equivalent business to which its customers could turn. Ultimately, BrightHouse justifies its high costs as being related to the inherent risks and costs of lending to its customer base – a fifth are unable to make electronic payments, so it maintains a high street presence to allow in-store payments.

The FCA's proposed cap on this form of finance,²⁶ and restrictions on the sale of extended warranties, are welcome to protect customers from very high costs in a market with little choice for those who depend on it.

A new not-for-profit enterprise, Fair for You,²⁷ aims to disrupt the rent-to-own market by offering flexible and affordable loans to buy household goods. Loans are paid back in flexible instalments with the benefit that customers can pay off the loan quicker to reduce their interest payments. One key issue for consumers is that it lacks the BrightHouse network of high street shops, so its reliance on its customers being digitally active may be a disadvantage for some. Its mission is not to be the biggest provider, but to be the best provider and, through this, set a standard for others to follow.

Utilities and essential services

As with goods, the poverty premium in relation to utilities and essential services has a major impact on families on low incomes. University of Bristol research on the poverty premium²⁸ found that households living in poverty are unlikely to be on the best utility rate, with these costs identified as the 'single biggest premium' affecting around three-quarters of low-income households. This research also found that one-third of low-income households have more costly prepayment energy meters installed.

Regulation in favour of increasing competition in the utility market is intended to protect consumers by enabling them to 'switch' to achieve the best deal. This assumes that consumers are fully-informed on the rates available and are able to make comparisons and choices. However, competition provides little protection for those on the lowest-incomes who are struggling to make payments.

²⁴ Wilde M., (2018) Citizen's Advice Scotland evidence to this inquiry: www.appgpoverty.org.uk/home-page/poverty-premium-inquiry-written-submissions/

²⁵ www.appgpoverty.org.uk/wp-content/uploads/2019/02/BrightHouse-submission-to-APPG-on-Poverty.pdf

²⁶ www.fca.org.uk/news/press-releases/fca-confirms-introduction-rent-own-price-cap

²⁷ www.fairforyou.co.uk

²⁸ Davies S. & Finney A. (2017) 'Making the Poverty Premium History – A practical guide for business and policy makers', University of Bristol Personal Finance Research Centre

“A low-income household may end up paying more for their energy needs for a number of different reasons: because they need to budget closely (which a pre-payment meter affords them); they are financially excluded, including as a result of prior arrears (which makes other payment options unavailable to them); they are digitally excluded or have low financial capability which, in the context of complex tariffs and evolving markets, makes comparing more difficult; and they are risk-averse, and may not wish to switch, aside from the fact that the alternatives open to them personally may not be any more attractive”

Sara Davies, Personal Finance Research Centre, University of Bristol

Switching and the loyalty penalty

The utilities market fails consumers on low incomes by assuming consumers are continually switching providers to access the best deals, and inflicts a ‘loyalty penalty’ on anyone who is not proactive in shopping around. The myth of the rational ‘super consumer’, who actively engages with the market to achieve the best deals, continues to persist despite overwhelming evidence that markets structured in this way consistently disadvantage the most vulnerable.²⁹

Poorer consumers are disproportionately less likely to be on the best deals. Consumers on low incomes are 30% more likely to be paying a loyalty penalty for energy, 20% more likely for insurance and 100% for broadband, amounting to a cost of £1,000 a year across six essential markets. Analysis by the Department for Business, Energy and Industrial Strategy (BEIS)³⁰ found that in the energy market, the consumers least likely to have switched had household incomes under £18,000 a year, were living in rented social housing, were without qualifications, were aged 65 and over and were disabled.

People who are income-poor are also often time-poor, which makes finding the time to browse price comparison websites or making phone calls to negotiate a better deal even harder for poorer families. Moreover, the number of markets that operate on the super-consumer model and which are considered ‘essential services’ continues to grow. Therefore consumers on low incomes are expected to find more and more time to negotiate cheaper deals for not only gas and electricity, but also home insurance, broadband, television and mobile phone contracts. Joseph Rowntree Foundation’s submission to the inquiry³¹ highlighted the impact of poverty in ‘depleting cognitive bandwidth’ – meaning that dealing with the mental load of living in poverty is exhausting, leaving people with even less mental capacity to think about switching utilities.

Moreover, the experience of switching itself is not made easy for anyone, let alone elderly and disabled consumers on low incomes. The Money and Mental Health Institute’s submission to the inquiry³² focused on how people with mental health problems are financially disadvantaged by the ‘super-consumer’ model underpinning the essential services market. The most common symptoms of mental ill health – lack of motivation, loss in confidence, lethargy, impulsivity and short attention span – are the

²⁹ Fair by Design (2018), evidence to this inquiry - www.appgpoverty.org.uk/wp-content/uploads/2018/11/Minutes-162F102F18-evidence-session-on-consumer-protection.pdf

³⁰ Department for Business, Energy and Industrial Strategy (2018), ‘Modernising Consumer Markets’ Green Paper

³¹ www.appgpoverty.org.uk/wp-content/uploads/2019/02/JRF-response-to-APPG-Poverty-inquiry-into-the-poverty-premium-30-April-2018.pdf

³² www.appgpoverty.org.uk/wp-content/uploads/2019/02/Money-and-Mental-Health-response-to-the-APPG-on-Poverty-poverty-premium-inquiry.pdf

very opposite of the characteristics needed to successfully navigate these markets and actively pursue good deals. Switching also often requires using the phone, which can deter people with anxiety disorders.

One solution for people with mental health problems lies in the importance of communicating with them in a range of different ways, to enable them to engage with providers in a way that suits them, in addition to simplifying processes. Overall, it was suggested that the market should be redesigned as its current reliance on active engagement causes direct financial disadvantage to those who are least able to engage.

Prepayment meters, standard variable tariffs and billing methods

Each of the individuals giving evidence to the inquiry on their experiences of the poverty premium referred to living in a home with an expensive prepayment meter. Often landlords had offered no indication of whether or not tenants were able to switch to a metered, billed tariff, while other landlords had specifically forbidden tenants from changing these within their contracts. Many people stated that they were not aware that prepayment meters were significantly more expensive than paying monthly or quarterly. If they were aware, they were not sure how to switch.

A wide array of barriers to accessing a cheaper utilities deal were highlighted by contributors, with many households experiencing more than one of these at the same time:

- They were not aware that they could have shopped around for a cheaper deal.
- They did not have the time or energy to shop around for a cheaper deal.
- They were reluctant to sign up to direct debit billing, despite this offering a discount, as they needed more control over when they paid bills throughout the month.
- They were concerned about paying the penalty of a refused direct debit if there was not enough money in their account when it went through.
- They did not have a transactional bank account, and so were required to pay by cheque.
- They did not have digital skills to find an online discount or to manage their accounts online (e.g. paying and receiving bills online).
- They did not have access to the internet to access online deals.
- Their disability prevented them from either using the internet to access cheaper deals, or from being able to phone up to cancel a contract or renegotiate a deal.

The additional costs relating to paper billing, paying by cheque, and the inability to access online and direct debit discounts all contribute to the poverty premium that better off households tend to avoid.

With price caps introduced on prepayment tariffs and default tariffs, introduced over the past few years, it remains to be seen whether or not these significantly reduce the poverty premium and alter the market. For instance, Energy UK's submission to the inquiry suggested that the impact of the prepayment price cap has simply been to spread the costs of servicing prepayment customers across

the entire customer base, which in effect increases the cost of energy for anyone living in poverty and on a default or fixed tariff.

Energy efficiency measures

Energy suppliers noted in their contributions the importance of energy efficiency measures in reducing the cost of bills. Contributors highlighted that it is often the poorest households, living in poor-quality rented housing, who deal with the costs of 'inefficient' homes. Improving a property from a 'Q' rating to an 'A' rating will save a household 85% on energy bills, but even to improve a 'G' rated property up to a 'D' rating would save a household up to £2,000 a year on their energy bills.

In its submission E.ON Energy³³ said that improving the UK's housing stock is the most effective and sustainable way to end fuel poverty. The energy companies who contributed to the inquiry viewed energy efficiency measures and improving the country's poor housing stock as central to eliminating the poverty premium. They suggested that action is needed on the part of both suppliers and the government.

The UK government has announced through its Clean Growth Strategy that it will invest £3.6 billion to upgrade a million homes through the Energy Company Obligation (ECO) by 2020 and will extend this support to 2028. Its aim is that fuel poor homes are upgraded to Energy Performance Certificate (EPC) Band C by 2030 and it is requiring landlords of the worst performing privately rented homes to improve them to at least Band E. Scotland and Wales have their own state-funded schemes.

Energy UK³⁴ argued that the Energy Company Obligation (ECO) did not go far enough considering the scale of the challenge. It has also been noted that there is a significant funding gap in energy efficiency measures to ensure the country meets fuel poverty reduction targets by 2030.

From the business perspective, suppliers such as E.ON Energy have offered to fit energy efficiency measures free of charge in the homes of those identified as living in poverty. This investment benefits both the customer and the supplier, as reduced energy bills for the household is also likely to reduce defaults on payments.

However, it was also noted in evidence from people living in poverty that there is a degree of mistrust in energy providers and a suspicion that they are driven more by their profits than the needs of consumers on low incomes. As such, there is some work to be done by both the government and energy suppliers to rebuild trust in energy efficiency measures and their benefits.

Smart Meters

In its evidence, E.ON spoke about the company's preference for encouraging the use of Smart Meters – compared to prepayment meters they are cheaper to maintain and also provide a way of better identifying customers struggling to meet costs. Smart Meters help suppliers to identify struggling customers and provide appropriate support if necessary. They can also help with budgeting by showing energy usage, and its cost, in near real time, removing the need for meter readings. However, switching supplier can be the best way of saving energy costs and many Smart Meters will lose some of their functionality after switching to a new supplier, although they will still function as a basic meter.

³³ www.eonenergy.com

³⁴ www.energy-uk.org.uk

Warm Home Discount, Winter Fuel Payments (Winter Heating Assistance in Scotland) and the ‘automatic’ application of benefits

The Warm Home Discount scheme offers a discount of £140 off electricity bills to qualifying customers who have difficulty paying energy bills during the winter months. It emerged during the inquiry that not all energy suppliers are required to offer the Warm Home Discount,³⁵ meaning some eligible customers may inadvertently miss out. Moreover, while all pensioners signed up to a relevant supplier receive the discount, the broader discounts available for low-income households are limited and apply on a first-come-first-served basis. Contributors also highlighted the fact that some who receive this support are not inclined to switch providers because they are worried that by switching to get a better deal they may end up losing access to the discount. Conversely, the Winter Fuel Payment (or Winter Heating Assistance in Scotland³⁶) is paid automatically to anyone over a certain age, without means-testing. One possible solution would be for suppliers to identify customers on low incomes proactively and apply such discounts automatically. Mandating all providers to apply these discounts could resolve a number of issues relating to the poverty premium. For example, the recent introduction of price caps in this market, applied automatically for customers and across all providers, has successfully reached all eligible consumers on low incomes without the need for them to be proactive.

Other solutions to the poverty premium may come in the form of collective switching or wholesale purchasing in which communities come together and create greater purchasing power. An example of this is Robin Hood Energy³⁷, a not-for-profit energy provider owned by Nottingham City Council with the aim of improving affordability of energy for local residents.

Housing

The submission to the inquiry from Shelter³⁸ highlighted a number of issues relating to the high costs of renting in the private rented sector, particularly for the poorest families and the most vulnerable.

These include:

- Tenants receiving social security benefits are often discriminated against by landlords and lettings agents, restricting their choice. Those who do manage to rent in the private rented sector are faced with high upfront costs as a result of deposits and agency fees. However, the UK Government has recently legislated to ban tenant fees from June 2019.
- Households experiencing multiple moves, as a result of insecure tenancies for example, face these costs repeatedly.
- 80% of privately-rented homes are unfurnished (although some may include white goods), which can cause households to take on high-risk, expensive loans or sign up to high-interest rent-to-own contracts for furniture – the effects of which are outlined in previous sections.

³⁵ www.gov.uk/the-warm-home-discount-scheme

³⁶ www.gov.scot/publications/winter-benefits-policy-position-paper/

³⁷ robinhoodenergy.co.uk

³⁸ www.england.shelter.org.uk/professional_resources/policy_and_research/policy_library/policy_library_folder/consultation_response_appg_poverty_inquiry_into_the_poverty_premium

- Poor energy efficiency and poor quality of homes means that families have to pay high energy costs to stay warm.
- The overarching effects of the poverty premium in stretching the money available to a household can cause rent arrears to build up, which may lead to homelessness.

Social housing providers are leading the way in helping their tenants to avoid the poverty premium in a number of ways. Orbit Group³⁹ recognises the costs incurred by tenants equipping their new home at the start of their tenancy and has adopted a policy of only removing fixtures and fittings left in the property by previous tenants if they are in a poor condition. The Reuse network⁴⁰ and its member organisations also help new tenants avoid having to resort to rent-to-own providers by re-using millions of items destined for landfill and diverting them to people in need of household goods. Hastoe Group⁴¹ has invested in building ultra-energy efficient homes to reduce energy costs to tenants, which will enable them to avoid a major aspect of the poverty premium.

Another innovative solution proposed to the inquiry was a rent flexibility scheme being piloted by the Centre for Responsible Credit.⁴² The scheme allows flexibility over rent payments to prevent the need to access credit. Tenants on the scheme are able to plan an annual budget, identifying months where they will choose to 'overpay' or 'underpay' thus allowing planned 'rent holidays' at times of particular financial pressure, for example school holidays or Christmas. Initial findings had been positive and the scheme also proved beneficial to landlords as it lowered the likelihood of defaulted payments and, therefore, reduced spending on debt collection.

³⁹ www.appgpoverty.org.uk/wp-content/uploads/2019/02/Orbit-APPG-on-Poverty---Poverty-Premium-Inquiry-Response.pdf

⁴⁰ www.reuse-network.org.uk

⁴¹ www.hastoe.com

⁴² www.responsible-credit.org.uk/how-rent-flex-works-case-study-one-paying-off-debt-and-stabilising-finances/

Recommendations

1. The UK Government should show leadership to tackle the poverty premium

- Develop a cross-government strategy to tackle the poverty premium under its strategic aim to “make the economy work for everyone”.
- Engage with the Competition and Markets Authority and other relevant stakeholders, academics and others to explore the potential for an official measure of the poverty premium and its impact on low-income households, to enable progress on ending the poverty premium to be tracked.
- Identify areas across all government departments and their arms’ length bodies that have an impact on the poverty premium and develop delivery plans to address them.
- Use its influence, policy levers and regulatory powers, where necessary, to promote action by business to carry out a poverty-premium risk assessment on goods and services and remove poverty premium costs.
- Establish and lead a Financial Inclusion Data-Sharing Group to safely identify, evaluate and increase appropriate access to datasets aimed at reducing the poverty premium and improving outcomes for financially-vulnerable households.

2. The UK Competition and Markets Authority (CMA) and other regulators should show leadership to tackle the poverty premium

- The CMA and regulators of essential services such as the FCA and Ofgem should adopt inclusive design strategies to:
 - guide their approach to understanding the needs of all consumers – through evidence, research and market analysis – to help set their priorities, develop and implement interventions, and assess their effectiveness.
 - guide their expectations of businesses to embed consideration of low-income consumers when they design and deliver products and services.

3. The UK Government should reduce the risks of debt for people receiving social security support

- Review the cumulative impact of the wide-ranging cuts to social security and the benefit freeze that are driving increases in poverty. These leave the most vulnerable struggling to pay for essentials such as rent, utilities and household goods.
- End the structural and design issues in universal credit that drive up poverty and debt, particularly the 5-week delay before a first payment is made which causes hardship to people without savings to fall back on.
- Allow more flexibility in payments of universal credit – provide the option of choosing payments every two weeks, to help people on low incomes to budget more effectively and avoid getting into debt with payday lenders. The splitting of payments between the adults in

couple households – by default or on request – should be considered for all claimants, not just those in situations where there is or has been domestic abuse.

- Reinstatement of the Social Fund in England as a rights-based national assistance scheme for people on low incomes, based on clear criteria and promoted to those in need. While working towards this there should be a duty on local authorities to operate local welfare assistance schemes, supported by ring-fenced funding.

4. Businesses should provide support to employees affected by the poverty premium

- Move progressively towards paying all employees at least the Real Living Wage (as advocated by the Living Wage Foundation) and provide stable, secure and predictable hours of employment through permanent, salaried contracts as far as possible.
- Make low interest or interest-free loans available to staff to cover the costs of travel, to enable employees to take advantage of reduced tariffs, with repayment through monthly salary. Similar schemes should also be considered to fund tenancy deposit loans, repaid through salary deductions.
- Investigate the possibility of more flexible payroll systems that allow employees to access their wages as and when they need them, reducing the need to access credit between monthly salary payments.
- Establish a hardship fund that can provide loans to employees who are struggling to pay for unexpected costs, preventing the need to access high-cost credit.
- Sensitively offer financial advice and/or digital literacy skills – including advice on eligibility for additional support – to employees.
- Business groups including the CBI, IoD, FSB, BCC and BiTC to work together with the APPG on poverty and other stakeholders to aggregate and disseminate best practice on tackling poverty amongst their members' workforces and customers.

5. Financial services providers should improve their services to consumers on low incomes

- Have a duty of care to customers on low incomes – this might, for instance, mean that they refer borrowers with a low income to appropriate lenders such as credit unions.
- Review credit-scoring methods to explore additional and alternative ways of assessing creditworthiness, with a focus on supporting the financial inclusion of consumers on low incomes. One approach might be to use a customer's current financial circumstances, rather than credit history, as a means of making a fairer assessment of their current circumstances.
- Develop insurance products to meet the needs of customers on low incomes, carrying out customer research to address barriers to take-up and considering ways to minimise location-based premiums.

6. Housing providers should better meet the needs of tenants on low incomes

- Explore flexible options to make rental deposits more affordable for tenants on low incomes, while balancing risk e.g. rather than requiring the full deposit to be paid upfront, it could be paid in instalments in addition to rent over the first months of a tenancy.
- Provide properties to social housing tenants with floor and window coverings and white goods (cooker, fridge and washing machine) in place wherever possible – such items should not be removed when a tenancy ends unless they are in an unusable condition. This will help prevent families on low incomes going without essential goods or being forced into debt through high-cost credit or rent-to-own purchases.
- Ensure that social housing properties let to tenants on low incomes are energy efficient and that tenants are placed on the most beneficial utility tariffs for their needs at the start of a tenancy.
- Consider the benefit of offering rent flexibility schemes that enable tenants to pay more at certain times of the year to provide for ‘rent holidays’ at times of particular financial pressure (summer holidays or Christmas).

7. Utility and essential service providers should better support low-income and vulnerable customers

- Review their customer services standards to ensure that staff are aware of the impact of utility debt on customers on low incomes and that their vulnerability is considered in all interactions.
- Enter vulnerable customers onto a priority register with training to support staff to look out for signs of financial difficulty and mental health problems. This would allow companies to offer specific support and guidance tailored to those who need it.
- Make so-called ‘social tariffs’ available to customers in vulnerable circumstances. All energy suppliers to pay the Warm Home Discount, to prevent fear of switching among elderly and low-income households.
- Proactively approach the process of reviewing contracts, with assistance offered and options clearly explained. Suppliers should carry out research with customers to explore how this could be improved.
- Spread the additional costs of support for customers on low incomes across all customers to eradicate the poverty premium.
- Make flexible payment schedules available at no extra cost, such as weekly or fortnightly payments, where this will help budgeting for those not paid monthly.

8. Local government and community action to tackle the poverty premium

Where community hubs already exist they could have a valuable role in sharing information to empower people on low incomes to defeat the poverty premium. In other areas, these could possibly be developed from food bank hubs.

- Providing advice and support on income maximisation.
- Signposting to responsible credit alternatives, such as credit unions and affordable rent-to-own retailers.
- Identifying cheaper alternatives for purchasing food, household goods and other services.
- Organising collective switching and wholesale community energy buying schemes.
- Helping those less able to switch providers or access a good deal communicate with essential services providers.
- Local government to improve their debt collection practices, particularly with regard to council tax arrears.

By acting together in this way, communities can provide direct support to tackle poverty premiums and, through this, disrupt the superior marketing power of high-cost lenders and other business that charge poverty premiums or do not adequately meet the needs of consumers on low incomes.

List of contributors

The inquiry heard the views of the following individuals across six evidence sessions in 2018.

Sharing personal experience of the poverty premium:

Rob Murthwaite

Aimee White

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Alicia Vernalls – Commissioner, Birmingham Poverty Truth Commission
and 24 members of the public who provided evidence anonymously.

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Social Market Foundation

StepChange

Thomas Pocklington Trust

Turn2us

Young Foundation

Scope

Shelter

The All-Party Parliamentary Group on Poverty

The APPG's aim is to increase understanding of poverty among parliamentarians and to seek all-party solutions, while drawing on a range of outside people and knowledge.

Officers:

- Kevin Hollinrake MP – Co-Chair
- Neil Gray MP – Co-Chair
- Baroness Ruth Lister – Vice-Chair
- Heidi Allen MP – Vice-Chair
- Lord Bird – Vice-Chair
- Patricia Gibson MP – Vice-Chair
- Lyn Brown MP – Officer
- Baroness Anna Healy of Primrose Hill – Officer
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- Janet Daby MP
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- Rachael Maskell MP
- Kate Green MP
- Lord Jeff Rooker
- Dr Philippa Whitford MP
- Tony Lloyd MP

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