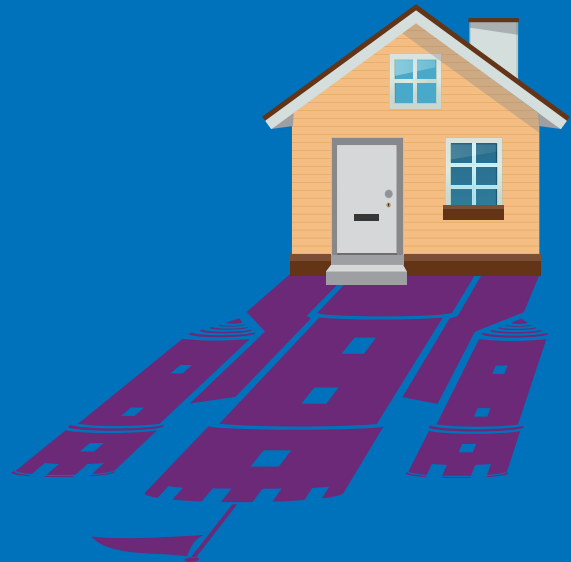




Reimagine welfare

Using our best disruptive thinking to
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Iain Gravestock and Bethan McKay

Government departments pool their spending power to bulk-buy electricity at very low cost. But low income families dependent on prepaid meters must purchase their power at inflated prices. Iain Gravestock and Bethan McKay propose a scheme that could cut the benefits bill whilst tackling fuel poverty – and that's just the start of its potential benefits.

It's a sad fact that those least able to heat and power their homes often pay the highest prices – for four million¹ largely low-income households have prepayment electricity meters, incurring an additional cost that can range from an average £80 to £250 a year.² Even taking the low end of these figures, the poorest families in the country are paying a price premium totalling nearly a third of a billion pounds.

This inequity bites particularly hard in winter, when power use increases; unlike those paying a fixed monthly direct debit, households with prepayment meters cannot even out their electricity costs over the year. Then there's the inconvenience and cost of visiting shops to charge up meter keys, and the harm caused when vulnerable people simply cannot afford to keep the lights on; dependence on a prepayment meter is bad news for many of the poorest in our society.

Yet much of the money coursing through Britain's prepayment meters is provided by an organisation with vast purchasing strength and the country's best credit rating: the UK government. Indeed, the government buys its own electricity at well below retail rates: to minimise the burden on taxpayers, many departments and agencies aggregate their purchases through the Crown Commercial Service (CCS) – which, trading on the wholesale markets, uses its huge spending power and specialist skills to achieve the best prices available. So taxpayer cash which reaches energy markets via the CCS is stretched to the limit; but those government funds which instead pass briefly through the hands of benefit claimants produce far slimmer returns.

Under this system, the poorest in society both pay the highest prices for electricity (and for low-income households, power represents a big chunk of their monthly outgoings) and have the lowest security of supply. Meanwhile, hard-pressed benefits budgets are used inefficiently, so the Department for Work and Pensions (DWP) must spend more to provide the unemployed and vulnerable with life's essentials. And power companies must maintain an unwieldy and expensive physical infrastructure of prepayment meters, in a bid to maintain some level of service for a group they view as high-risk and low-return.

Let's reimagine this whole system...

What if DWP claimants could elect to put some of their benefits entitlement into an innovative new government-run electricity purchasing service, transforming themselves from some of the weakest individuals in the marketplace into members of a huge and powerful electricity-buying syndicate? Pooling their buying power with that of other claimants and the government itself, they would become partners in a huge trading block – and secure much better prices in the market.

“The poorest in society both pay the highest prices for electricity, and have the lowest security of supply”

Not all of those savings would accrue to the consumers – for the government would also share in the savings, enabling it to reduce benefits spending. Given the substantial gap between the below-market prices currently paid by CCS and the premium charged via prepayment meters, there would be plenty of savings to go round.

Participants would also benefit from fixed and predictable monthly outgoings, with their electricity spending smoothed over the year, and eliminate the inconvenience of key charging and the risk of being cut off. In exchange for these advantages, they would see a small reduction in their spending flexibility – for with a proportion of their benefits diverted at source into the scheme, they would draw out less cash – and a still smaller cut in their headline benefits figure; but their spending power would rise.

Electricity suppliers should also benefit. For them, prepayment meters are simply a way to minimise risk when supplying electricity to people who may not have the money to pay bills in arrears. The premiums charged such customers are spent on supporting the infrastructure of meters and charging points; most providers would much prefer to be charging lower rates to a less complex and more reliable set of customers.

If instead these households' bills were paid directly by the government itself, the whole calculation facing energy providers would change: participants would become a very low-risk consumer group, with lower customer acquisition spending and bills handled via an automated central system – producing much reduced administrative and payments costs.

How to deliver the new service

The service would aggregate participants' electricity purchases, perhaps channelling them through the CCS systems already established to take advantage of the best possible wholesale market rates.

The scheme would initially be linked to a single benefit, though it could be expanded later to include others. Participants would be required to 'sacrifice' enough of their monthly benefits to cover their household's average monthly electricity use over the previous year – a figure smaller than previous years' spending, thanks to the discounted rate achieved under the scheme. The lion's share of this 'sacrificed' money would be spent buying electricity on wholesale markets, with a smaller sum returning to the DWP or Treasury.



If participants' electricity use began to rise during the year after they joined the service, threatening to outpace their contributions and leave the government out of pocket, the system – which would track both electricity use and benefits sacrificed – would ask them to raise their monthly payments to cover the difference.

Benefits claimants would access the service via a GOV.UK web page or an app, both of which could verify eligibility with the DWP and keep users informed on market prices and their cumulative savings. Those unable to access or use these technologies could instead call a telephone helpline, but the government would aim to make the digital services so easy to use, quick and convenient that they become by far the most popular channels. These goals would be aided by the use of citizen-centric design, the deployment of emerging cross-government technology platforms, and the application of Government Digital Service expertise and standards.

Alignment with public objectives

As well as the advantages for consumers, suppliers and the government listed above, this system could produce a range of further public benefits. The most obvious of these include:

- By reducing energy costs, smoothing payments over the year and preventing 'blackouts' when participants can't afford to recharge their keys, the service would help the government realise its goals around reducing fuel poverty;
- The system could provide a helpful channel for energy providers to meet their Energy Company Obligation (ECO2t) requirements, further supporting work to tackle fuel poverty and producing more energy savings for the poorest consumers;
- Integrating this approach with the government's winter fuel payments system could reduce the latter's administrative and service delivery costs;
- Collecting data on individuals' spending and their use of services, the government could – with the right consents in place – gather evidence to inform future policymaking, improve its targeting of advice and support services, and identify the most effective ways of reducing energy use.

Going further

This approach has huge potential benefits in electricity, where the existence of prepayment meters creates a twin-track market penalising the most vulnerable consumer groups. But the government could also produce savings within many other markets by aggregating the spending power of benefits claimants and, in many cases, combining it with its own. And if people began using and valuing this service to purchase electricity, they would already have the equipment, experience and confidence to make other essential purchases through the same system.

These purchases might include water and sewerage, basic food, insurance, simple financial products, telecommunications and broadband. And incorporating some of these new services into the system would provide additional social benefits. We might see a rise in the number of insured households, for example – an important goal, given that the poorest families both experience an above-average risk of burglary or home damage, and are poorly prepared to recover from such blows. We might also broaden access to home internet, tackling 'digital exclusion' and – in a virtuous circle – making it easier for people to use the 'benefits sacrifice' portal. We might even improve eating habits, contributing to public health.

Extending the scheme in this way would have obvious benefits for claimants and the government – with both sides seeing their outgoings falling as they share the benefits of bulk discounts – but service providers and retailers would also have strong incentives to participate. Currently, businesses targeting these consumer groups typically find that individuals are highly price sensitive, with low spending power and poor credit ratings. Under this service, they would instead be invited to bid for substantial bulk-sales contracts, with payment underwritten by government and much reduced marketing, service provision and payments costs. In such low-margin markets, these benefits are extremely attractive.

In each of these examples, the purchasing model would be similar to that of electricity. Consumers would voluntarily forego a proportion of their benefits in order to receive the product at a discounted rate – so they'd pay a fixed monthly fee up front, with usage tracked almost in real time.

Addressing challenges and objections

As with any significant policy initiative, there are many potential problems and risks around this idea. Here we address six of the most substantial.

1. The scheme depends on high volumes to drive down prices and attract energy providers. What if it doesn't attract enough claimants?

The project's ability to attract participants would depend on the quantity and quality of marketing; the system's accessibility and ease of use; and the savings available. Given that the government already communicates extensively with benefits recipients, it has a range of existing channels to market. Meanwhile the Government Digital Service has demonstrated its ability to produce accessible, attractive service delivery platforms; and the savings on offer should easily be substantial enough to attract this price-sensitive group of consumers.

2. If service users consume more electricity than they've funded through benefits sacrifice, then stop claiming or disappear, someone's left with an unpaid bill. Who carries that risk?

Energy companies. Because the service tracks energy use monthly, these bills could only be small. And energy suppliers currently find low-income customers an expensive group to supply, with high fixed infrastructure costs and disproportionate expenses for marketing, billing, money transfers, administration, complaints and dispute resolution; the savings that come with moving to a single, highly reliable customer should more than outweigh any additional losses. As an additional safeguard and deterrent, participants could also be required to repay overspends through deductions from any future benefits payments.

3. This looks like a difficult technology project and a brand new form of public service – does government have the skills to deliver it?

In fact, this is only an iterative development of existing successful policies. The Motability service aggregated benefits spending to provide a single service for users. Childcare vouchers involve a salary sacrifice scheme, administered through HMRC. And the DVLA's Vehicle Excise Duty service instantaneously checks vehicles' insurance cover, demonstrating government's ability to manage real-time data exchange with private industry. What's more, in recent years the Major Projects Authority (now the Infrastructure and Projects Authority) has substantially improved government's programme and project management capabilities, whilst the Government Digital Service has boosted digital skills and 'agile' development capabilities. With the right team in place and an intelligent programme of pilots, the service is well within the government's capabilities.

4. Would the wider public, who must pay full price for services, resent the fact that benefits claimants are paying less?

The scheme would have to be restricted to core services and goods, and could not be used for the purchase of luxuries. And whilst benefits claimants would indeed see their total spending power rise a little, taxpayers would also benefit from a share in the savings: the fall in benefits spending should be welcomed by most people, who would see the sense in the government aggregating its buying power – and the waste inherent in the current state of affairs, under which government funds are spent huge inefficiently on basic services provided to claimants.

5. Does the scheme adopt a patriarchal approach, depriving people of choice over their own spending and limiting their independence?

Many consumers' independence is already constrained by their own weakness in the market and their status as high-risk and/or low-value consumers – with outcomes such as their having to use prepayment meters, or paying higher prices for items bought in small quantities. This service would empower people by combining their individual spending powers to form a trading block.

What's more, it would be entirely voluntary: people could choose to opt in or out at any time. And far from decreasing personal responsibility, it would increase it. These consumers have often been deprived of personal responsibility and the task of planning their spending because the market doesn't trust them – preferring instead to refuse them the credit required to smooth payments over the year or to pay bills in arrears. This service would return to people the responsibility for managing spending on a monthly basis, supporting them to 'normalise' their finances.

6. Would businesses currently serving this market oppose the scheme's introduction?

Some might – for these markets include more than one kind of supplier. Some businesses offer cheap food and services to low-income consumers, making a living by 'piling 'em and high and selling 'em cheap': such companies would be well placed to bid for work as suppliers to the new scheme, making good use of their business model whilst reducing their administrative, marketing and billing costs.

Other businesses make their money by taking advantage of poor consumers' weakness in the market – offering sky-high interest rates for unsecured loans, for example, or charging high prices for goods sold in small volumes. These organisations might lose out as the markets were rebalanced to offer more support and security to the poorest in society; but their interests are outweighed by the service's benefits for taxpayers, government's policy aims and wider society.

Summary

Aggregating individuals' buying power in this way would help to reduce the public finances deficit, produce a more efficient energy market and infrastructure, and secure improved services for the most vulnerable in society – many of whom currently get a worse deal than wealthier citizens. The concept sits well with many government policies and agendas, and uses techniques and systems tested in other successful policies.

If at first glance it seems radical, that's simply because we are only just grasping the endless possibilities for the potential of digital technologies and user-centred design. In years gone by, this kind of service could not have been established without vast, bespoke IT systems, layers of regulation, and substantial organisational change. But today the technologies exist to gather, manage and analyse data rapidly, whilst government's ability to deliver digital projects – especially those well-suited to agile development – has much improved.

Whilst we appreciate there are a number of challenges within this piece, it is just a thought; the results of us exercising our imaginations and approaching social goals or challenges from a new perspective.

Contacts

We publish these ideas to stimulate debate so please contact us and share your own at ukfmpsmarket@kpmg.co.uk
Alternatively, please feel free to contact the authors directly.

Bethan McKay

Associate Director

T: +44 20 7694 4580

E: bethan.mckay@kpmg.co.uk

Iain Gravestock

Partner

T: +44 20 7311 6386

E: iain.gravestock@kpmg.co.uk

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