EXPLANATORY MEMORANDUM TO

THE WARM HOME DISCOUNT (RECONCILIATION) REGULATIONS 2011

2011 No. 1414

1. This explanatory memorandum has been prepared by the Department of Energy and Climate Change and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument establishes and provides for the operation of a reconciliation mechanism for the purposes of the Warm Home Discount scheme established by the Warm Home Discount Regulations 2011 ("the Scheme Regulations"). The purpose of the reconciliation mechanism is to achieve an equitable distribution among scheme electricity suppliers of the aggregate amount of rebates which they provide under Part 3 of the Scheme Regulations to customers determined by the Secretary of State. Electricity suppliers are required to make or receive payments so that the amounts of rebates provided by them under Part 3 of the Scheme Regulations, after such adjustments, are proportionate to their market shares.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Legislative Context

4.1 This instrument is made principally under the powers in section 11 of the Energy Act 2010. Obligations placed on electricity suppliers by this instrument are "relevant requirements", as defined in section 25(8) of the Electricity Act 1989 (as amended by the Schedule to the Energy Act 2010), and are enforceable by Ofgem under its powers in that Act.

5. Territorial Extent and Application

5.1 This instrument applies to Great Britain.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

7.1 The Warm Homes and Energy Conservation Act 2000[1] committed Government to implementing a strategy to tackle fuel poverty and led to publication of the UK Fuel Poverty Strategy in 2001. The Government's target is to eradicate fuel poverty in England, as far as is reasonably practicable, by 2016. Similar targets have been set by the devolved administrations in Wales, Scotland and Northern Ireland.

7.2 A household is defined as being in fuel poverty if that household would need to spend at least 10% of its income to heat its home to an adequate level of warmth. The latest figures suggest that in 2008 there were 4.5 million households in fuel poverty in the United Kingdom. There are three main factors that impact on fuel poverty: energy performance of the dwelling, household income and energy prices. Rising energy prices is the key factor behind recent increases in fuel poverty, and measures to reduce household energy bills can provide immediate support to a significant number of fuel poor and vulnerable households.

7.3 Part 2 of the Energy Act 2010 set a framework for the establishment of a statutory scheme for the purpose of reducing fuel poverty. The Warm Home Discount scheme will require, subject to a degree of flexibility permitted by the instrument, spending by suppliers totalling £250 million in 2011/12, increasing annually to £310 million in 2014/15. There are four sections to the scheme: the Core Group, Broader Group, Legacy Spending and Industry Initiatives.

7.4 The Core Group focuses on older pensioners on low incomes. Electricity suppliers will be required to provide rebates to customers determined by the Secretary of State. It is intended that in each year of the scheme suppliers will be directed to provide rebates to a subset of state pension credit recipients or their partners, increasing each year in number, with priority being given to the oldest and to those in receipt of guarantee credit. This group has a high propensity to be in fuel poverty. For the purpose of determining who is to be provided with a rebate, it is intended that Government will compare electricity suppliers' customer databases and DWP's data on pension credit recipients via a secure data-match and sweep-up process.

7.5. It is likely that certain suppliers will have a disproportionate number of customers that are eligible to receive a rebate through the scheme and will, therefore, face a disproportionate share of the costs of the Core group. As such, it is necessary to put in place a reconciliation mechanism in order to balance Core group expenditures across suppliers. The reconciliation mechanism will make cash transfers between suppliers in order to ensure that each supplier pays a share of the total Core group expenditures that is proportionate to their market share. This will ensure that a supplier that has a disproportionate number of eligible customers is not put at a competitive disadvantage.

7.6 This instrument establishes the methodology and processes through which Core group expenditures will be reconciled between energy suppliers. It also places a

[1] The Warm Homes and Energy Conservation Act 2000 extends to England and Wales. The Housing (Scotland) Act 2001 contains similar provisions in relation to Scotland.

requirement, in each Scheme year in which the Core group operates, on the Secretary of State to appoint an operator of the reconciliation mechanism.

8. Consultation outcome

8.1 The Department carried out a public consultation on the Warm Home Discount scheme from 2 December 2010 to 14 January 2011. Formal public consultation could not be commenced earlier as development of the policy was dependent on the level of funding available for the scheme being confirmed in the Spending Review. The consultation period was reduced to approximately 6 weeks to enable the scheme to be implemented in or as soon as possible after April 2011, in order to ensure continuity in the provision of support following the end of the voluntary agreement[2]. The draft reconciliation regulations were published alongside the Warm Home Discount consultation document on 16 December 2010 and energy suppliers were given an additional three weeks (beyond the end of the formal consultation period) in which to provide comments on the draft regulations.

8.2 The consultation proposals were welcomed by the majority of respondents, who agreed that it was vital to have a reconciliation mechanism alongside the Warm Home Discount scheme in order to ensure that the cost of providing rebates to customers in the Core group were shared between energy suppliers in an equitable way. A small number of respondents were concerned by the length of time between making payments to customers in the Core group and the point when the reconciliation mechanism would balance expenditures across suppliers. To deal with this issue, the consultation response set out the intention to have multiple reconciliation runs in each scheme year and stated that the issue would be kept under review throughout the course of the policy.

9. Guidance

9.1 The operator of the reconciliation mechanism, which will be appointed by the Secretary of State following a competition, will provide energy suppliers with guidance on compliance with the requirements of the mechanism. This guidance will focus on the process and timings for making and receiving reconciliation payments.

10. Impact

10.1 This instrument will impact on business through balancing the costs of Core group rebates across participating energy suppliers in order to ensure that no supplier (or suppliers) is put at a competitive disadvantage due to having a disproportionate number of customers that are eligible for a Core group rebate. It is anticipated that suppliers will incur some administration costs associated with reconciliation (e.g., the costs of making and receiving payments through the mechanism) but these costs are expected to be small.

[2] Under the voluntary agreement, the ‘big six’ energy supply companies agreed to spend £100mn in 2008/09, £125mn in 2009/10 and £150mn in 2010/11 on support for vulnerable customers.

10.2 The impact on the public sector is limited to the cost borne by Government in relation to the activities of the operator of the reconciliation mechanism. These costs are estimated to be small relative to the size of the scheme.

10.3 An Impact Assessment is attached to this memorandum and will be published alongside the Explanatory Memorandum on www.legislation.gov.uk.

11. Regulating small business

11.1 The legislation does not impose obligations on small businesses. The Warm Home Discount Scheme includes a threshold for mandatory participation. If licensed electricity suppliers who are below the threshold for mandatory participation wish to take part in the Core Group of the scheme (and, therefore, the reconciliation process) they may do so on a voluntary basis.

11.2 To minimise the impact of the requirements on firms employing up to 20 people, the approach taken is that a threshold based on the number of customer accounts that a licensed energy supplier serves has been introduced for mandatory participation in the scheme. This threshold has been set at 250,000 customer accounts for this scheme.

11.3 The basis for the final decision on what action to take to assist small business was informed by a consultation carried out by DECC on the appropriate threshold for participation in the range of schemes through which DECC places social and environmental obligations on energy suppliers.

12. Monitoring & review

12.1 The Secretary of State intends to place a contractual requirement on the operator of the reconciliation mechanism, which will be appointed following a competition, to report on an annual basis on the operation of the reconciliation mechanism.

12.2 The Secretary of State may, under regulation 31 of the Scheme Regulations, review any aspect of the operation of the Warm Home Discount scheme if he considers that it is not, or may not be, operating effectively or if its effectiveness could be improved.

13. Contact

Jamie Torrens at the Department of Energy and Climate Change Tel: 0300 068 5664 or email: jamie.torrens@decc.gsi.gov.uk can answer any queries regarding the instrument.