



PAYMENT SYSTEMS AND THE POVERTY PREMIUM

May 2023

Key issues and recommendations



FAIR BY DESIGN

Ending the extra costs of being poor

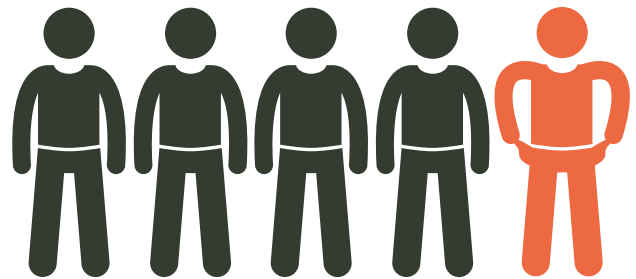
THE POVERTY PREMIUM

By their very nature, essential services such as payments, energy, credit and insurance are needed by everyone. However, these services have been designed in a way that treat some people unfairly. Poorer people pay more for products and services than those who are better off. This is known as the poverty premium. It can also mean that products and services do not meet people's needs, or even that they are excluded altogether.

Why does the poverty premium exist?

- Policymakers and regulators being disconnected from people with lived experience of poverty and exclusion.
- Essential products and services are designed around mythical 'super consumers'. These are people who never become ill, always have a steady income, are able to understand complex terms and conditions and always have the time and technology to easily find the best deal for them. The reality is very different for many of us.
- A dependence on competition to meet all consumers' needs and provide choice for everybody. In practice, competition favours the most easily profitable and engaged consumers.
- A lack of ownership and responsibility amongst regulators and government about addressing the impact of poverty and exclusion on access to essential goods and services, with no clear, transparent way to address these issues.
- A lack of a joined-up approach between the various different regulators and relevant government departments.

IN 2021/22 THERE WERE
£14.4 MILLION
PEOPLE IN THE UK LIVING IN POVERTY



THAT EQUATES TO **1 IN 5**

IN 2021/22
**THE HOUSEHOLD
POVERTY LINE**

**WAS
£15,600**



(after tax and housing costs)

Department for Work and Pensions (2023)

PAYMENTS AND THE POVERTY PREMIUM

We all need to pay for things, but payment systems for essential goods and services have not been designed with the needs of people in poverty in mind. This report highlights the challenges faced by people on low incomes when they pay for products and services that we all need.

Payment systems describe the way in which we pay for things: from online transactions to cash in shops. Some people may be able to pay up front for a purchase, for example, an annual insurance premium, while others will make payments over a period of time. Some people will set up a payment process with their bank to pay some suppliers, like a direct debit for utility bills, while others will make top-up payments for their purchases, like on a pay-as-you-go phone.

Different types of poverty premium in payment methods

Some methods of payment create a poverty premium, meaning people are charged more for the way they spend their own money. Not everyone can access all forms of payments: some people do not have bank accounts and, therefore, have no access to direct debits to make payments.

Some people pay for essentials, like energy, once the bill is received, known as 'payment on receipt of bill' or quarterly cash or cheque. People can opt for their supplier to send a quarterly bill showing exactly how much energy has been used over three months – but they are charged extra for this. People have also paid more for energy when using a prepayment meter, although this is set to change from July 2023.

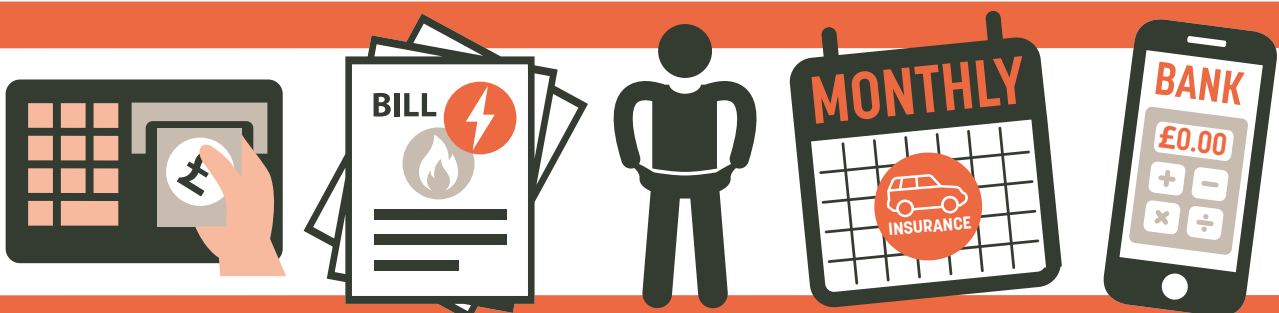
Some people who need insurance are not able to pay the full cost for a year in one go, so they end up paying extra for the ability to pay in instalments.

“Flexibility of payment dates was an issue... I had to plead with them to change that date to when I felt most comfortable, I could pay.”

Expert by experience of poverty, Poverty Alliance workshop, Scotland, 2022

“By the time I have paid for food and energy costs, I am almost running out of money. I tried to change it [insurance payments] to the start of the month, but I couldn't do it. I was up all night stressing. I tried to call, but it took forever. Waiting until the middle of the month means I am having very little or nothing in my account. I had to call the insurance company and wait for a long time.”

Expert by experience of poverty, Poverty Alliance workshop, Scotland, May 2022



SOME METHODS OF PAYMENT CREATE A POVERTY PREMIUM

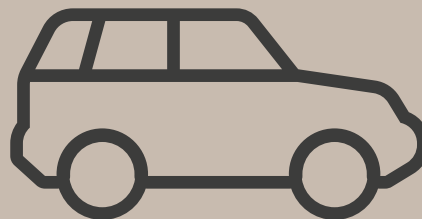
ENERGY

IT COSTS PEOPLE AN EXTRA £202 TO PAY FOR THEIR ENERGY ON RECEIPT OF BILL HISTORICALLY, PEOPLE HAVE ALSO PAID A POVERTY PREMIUM OF AROUND £45 FOR PAYING BY A PREPAYMENT METER



INSURANCE

PAYING FOR CAR INSURANCE BY MONTHLY PAYMENTS, RATHER THAN AN UP-FRONT ANNUAL LUMP SUM,



COSTS AN EXTRA £103 PER YEAR

CASH

PEOPLE ARE INCREASINGLY RELIANT ON FEE-CHARGING CASH MACHINES WHERE A FLAT FEE IS CHARGED FOR TAKING OUT ANY AMOUNT OF CASH



We're calling for the removal of these extra costs for low-income consumers, who have no choice but to pay for their essentials the way they do.



THE PAYMENT POVERTY PREMIUM AND ENERGY

There are a number of ways of paying for household energy. Many people in the UK pay for their energy using direct debit, which lets suppliers authorise payments from their account when they are due.

Paying for energy on receipt of bill

Some energy customers pay on receipt of their bill or through quarterly cash or cheque. They often choose these options so they can keep a closer eye on their bill payments or because their income fluctuates too much to allow them to use direct debits. For households who pay for both their electricity and gas in this way, they are charged an extra £202 a year¹. This way of paying affects 8% (electricity) and 7% (gas) of low-income households².



FOR HOUSEHOLDS WHO PAY FOR BOTH THEIR ELECTRICITY AND GAS IN THIS WAY, THEY ARE CHARGED AN EXTRA £202 A YEAR



Ofgem is currently looking at whether the “receipt of bill premium” should be abolished in addition to looking at how to make the end of the prepayment meter premium permanent.

Paying for energy via prepayment meters

Not everyone has access to direct debits. For those who do, many cannot use them because their income fluctuates too much, for example, people on zero-hour contracts. Over four million people pay for their energy using a prepayment meter³. This is either a key, which can be topped up at participating shops with cash, or a card payment. In some cases, they pay via an in-home display which can be topped up online.

Historically, people have paid a poverty premium of around £45 for paying by a prepayment meter⁴. Fair by Design was very pleased that in the March 2023 Budget, the Chancellor announced that the prepayment meter premium would be abolished. The government will do this via the Energy Price Guarantee up until April 2024. Ofgem is looking at how to equalise payment methods after that.

“I think if you’re on direct debit you’ve got to be really savvy and like check how much you are using each month... I have had that before where the payment has not come out for the right amount [...] and then you end up with a huge bill... my husband thinks I am obsessed but I’m just like, I don’t want a huge bill, I can’t pay a huge bill.”

Expert by experience of poverty, Toynbee Hall online workshop, Plymouth, 2019

¹ Davies, S., Evans, J., 2023. [The Poverty Premium in 2022. Progress & Problems. A Report from the Personal Finance Research Centre](#)

² Ibid.

³ Ofgem (2023a). [Ofgem launches national evidence-call on prepayment meters](#)


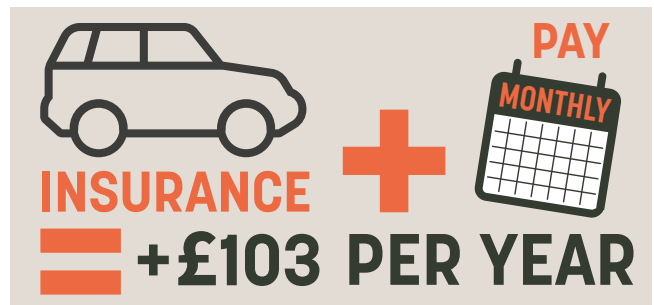
⁴ Ofgem (2023b). [Default tariff cap level: 1 April 2023 to 30 June 2023. Reports, plans and updates](#)

PREMIUMS ON INSURANCE PAYMENTS

Access to insurance provides protection from financial loss and is compulsory if someone needs to drive a car. How people pay for insurance also affects the price charged. Many of those who take out insurance policies cannot afford to pay for them in one lump sum, so they spread the cost over the year. This costs them extra.

Paying for car insurance by monthly payments, rather than an up-front annual lump-sum, costs an extra £103 per year. This affects nearly one third of households on low incomes. Insurers say they need to charge extra for payments by instalment, and this amount is charged despite them facing little risk, as insurers are able to stop the insurance part way through the year due to non-payment. Almost 1 in 3 of low-income households incur a poverty premium due to monthly payments for home contents insurance too. This is much less, at an average of £5 per year – a small sum, but still significant for someone on a very low income⁵.

Consumers pay a premium for monthly insurance payments because they are regarded as a loan: the product being purchased is annual insurance, so the customer is “borrowing” money from the insurer to cover the cost of future months’ cover. These “premium finance credit facilities” are, according to the Financial Conduct Authority (FCA), most frequently used by consumers to access household and motor insurance⁶. The nature of the transaction is not immediately obvious to all consumers, because the transaction doesn’t feel like a loan that will be paid back over the course of a year. It feels more like a one-off purchase.



Use of premium finance credit adds an additional cost for insurance and contributes to the poverty premium. We’re calling for this method of financing insurance premiums to be removed. Instead, we need an interest-free, affordable option to increase the uptake and meet the needs of low-income consumers accessing insurance.

⁵ Davies, S., Evans, J., 2023. *The Poverty Premium in 2022. Progress & Problems. A Report from the Personal Finance Research Centre*


⁶ Financial Conduct Authority (2015). *Provision of premium finance to retail general insurance customers. Thematic Review TR15/5. London: Financial Conduct Authority*

USING CASH


Many people prefer to buy things using cash. This can be because it helps them budget better and track in real time how much money they have left. Others may not have access to a bank account and the payment options this offers. The FCA has previously found that 45% of people who rely on cash do so because it helps them to budget or to avoid getting into debt. One in 3 rely on cash because they trust it more than other payment methods.⁷

Some people access their cash through automated teller machines (ATMs), or cash machines. Cash machines are often associated with banks, and people can access their cash for free using a bank cash machine. However, bank closures threaten the ability to do this easily for everybody.

In many areas, people are increasingly reliant on fee-charging cash machines where a flat fee is charged for taking out any amount of cash. Whether you take out £5 or £500, the same fee is charged. The average fee in 2022 was £1.68, and fee-charging cash machines are more frequently the only option in low-income areas. Close to 1 in 3 (29%) of low-income households pay, over the course of a year, a cash withdrawal premium of at least £20. Meanwhile, the premium for using a prepaid card, which mainly consists of card application fees and cash withdrawal fees, is £36 over a year.⁸

**CLOSE TO
1 IN 3** 
**OF LOW-INCOME HOUSEHOLDS
PAY, OVER THE COURSE OF A YEAR,
A CASH WITHDRAWAL PREMIUM OF
AT LEAST £20**

**THE PREMIUM
FOR USING
A PREPAID
CARD IS
£36 OVER
A YEAR** 

We are calling on the government, the FCA and the Payment Systems Regulator (PSR) to ensure people have free and local access to cash, wherever they live. 

⁷ Financial Conduct Authority (2021). [Financial Lives 2020 survey: the impact of coronavirus. Key findings from the FCA's Financial Lives 2020 survey and October 2020 Covid-19 panel survey](#). London: Financial Conduct Authority. Which? has found that, of those who regularly use cash, half (52%) say that cash helps them keep track of their spending – equivalent to 15 million people. See: [Which? \(2022\). Cash a lifeline for keeping track of spending for 15 million people amid cost of living crisis, Which? research reveals.](#)

⁸ Davies, S., Evans, J., 2023. [The Poverty Premium in 2022. Progress & Problems. A Report from the Personal Finance Research Centre.](#)



RECOMMENDATIONS:

HOW DO WE TACKLE

THE POVERTY PREMIUM

IN PAYMENT SERVICES?

We welcome Ofgem's current review of premiums for non-standard payment methods. We believe that:

Ofgem should require energy providers to remove the extra charges low-income customers pay for paying on receipt of bill



Ofgem should modify the energy price cap to fulfil the government's commitment to remove the prepayment meter penalty permanently



The FCA should require insurers to remove the premium charged to customers who pay monthly for their insurance



This can be done through removing premium finance from the insurance offer and replacing with a no-interest finance option. Alternatively, this could be achieved by removing the cost and requiring insurers to find other ways to absorb any costs, i.e., cross-subsidising between customers.

The government, the FCA, and the PSR need to ensure people have free access to cash



The FCA and the PSR should work with industry to create a common approach for keeping cash in circulation, in a way that is free to access. Supporting the delivery of access to cash should remain a part of the PSR and the Bank of England's role⁹. The government must also provide clarity about the content of its access to cash policy statement, which is required of Treasury, as soon as possible. The Treasury should ensure that the policy statement is explicit about what regulators need to consider to create a common approach for keeping access to cash free and tackle the poverty premium.

⁹ HM Treasury (2022). [New powers to protect access to cash](#)

RECOMMENDATIONS: HOW DO WE TACKLE THE POVERTY PREMIUM IN PAYMENT SERVICES?

The PSR should ensure wide availability and viability of inclusive and flexible payment methods, which can be adopted by utility providers



Payment systems which have in-built flexibility give customers greater control over how they pay their bills, managing other financial commitments in the process. Systems, such as Request to Pay¹⁰ and other customer-controlled payment flexibility innovations¹¹, allow people to underpay and overpay bills at particular periods in a way that doesn't penalise them.

Utility providers, with direction and guidance from their regulator, need to adopt flexible payment systems to allow customers more control over their payments



This can help customers avoid building up arrears. It could, in the example of energy, also provide payment control for people currently paying on receipt of bill, who don't wish to pay a premium for doing so, as is currently the case, but also worry about moving over to monthly direct debits.

¹⁰ Request to Pay (n.d.). [About Us](#)

¹¹ Variable Recurring Payments can facilitate flexibility. See: Open Banking (2021). [Variable Recurring Payments. What are they and how can they help SMEs?](#)



FAIR BY DESIGN IS CALLING FOR:



- 1** Ofgem to remove the extra charges low-income customers pay for paying on receipt of bill 
- 2** Ofgem to fulfil the government's commitment to remove the prepayment meter penalty permanently 
- 3** The FCA to require insurers to remove the premium charged of pay monthly customers 
- 4** The FCA and PSR to ensure people have free access to cash 
- 5** The PSR to ensure wide availability and viability of inclusive and flexible payment methods 
- 6** Utility providers, under guidance from regulators, to adopt flexible payment systems 



Fair By Design is dedicated to reshaping essential services such as energy, credit, insurance and payments so that they don't cost more if you're poor – also known as the poverty premium. Fair By Design collaborates with regulators, government and industry to design out the poverty premium. Our Venture Fund provides capital/funding to grow new scalable ventures to innovate the market and design out the poverty premium. Ascension manages the Fair By Design Fund.



Fair By Design is managed by the Barrow Cadbury Trust on behalf of a group of foundations.

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