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5 May 2023

Dear David,

Thank you for providing us with an opportunity to comment on Ofgem's further statutory consultation on strengthening the financial resilience of the energy supply sector. This submission is non-confidential and may be published on your website.

We remain extremely supportive of efforts to improve the financial resilience of the sector, noting the serious financial and customer service issues that have previously been caused by underprepared suppliers operating, and failing, in the market.

In our response to the previous consultation round, we expressed concerns about the discretionary nature of the powers that Ofgem was proposing in some areas, and its ability to rapidly identify and act on problems. We retain those concerns, although we take some comfort from the more detailed explanation of market monitoring in this consultation, and the clarification that the default assumption when a Consumer Credit Balance (CCB) trigger is hit is to direct ringfencing.

Capital Floor

On face value, there is a risk that the introduction of a Capital Floor at zero could be a placebo; causing no harm but providing relatively limited consumer protection. This is because any supplier in that situation should already have triggered the Transition Controls tied to the Minimum Capital Requirement, and be the subject of remedial attention to get a credible Capitalisation Plan in place. Some business as usual enforcement measures may have limited application for a licence breach in these circumstances. For example, fining a firm that is trading while technically insolvent may simply bring about its collapse.

However we recognise that there is a risk that a supplier may continue to trade while technically insolvent in a manner that sees its financial situation further deteriorate, bringing risks that an eventual collapse may result in unnecessarily high socialised costs. While 'pulling the plug' may be an unattractive prospect for a regulator, having that power may be prudent as a backstop.

Minimum Capital Requirement

We are supportive of the introduction of a Minimum Capital Requirement. We have no comment on the proposed level of £130 per domestic dual fuel consumer.

It is vitally important that the capital requirement relates to liquid, accessible capital that is not secured against other debts or subject to conditions that could prevent its access if a supplier enters trading difficulties. Inevitably this will involve some judgement on the part of the regulator. Chapter 2 of the consultation provides a thoughtful overview of the types of assets that may be appropriate; this list should be kept under periodic review.

Capitalisation Plans

We agree with the principle of the introduction, and enforcement of, Capitalisation Plans to demonstrate how suppliers will meet their Minimum Capital Requirements, however the flexibility that Ofgem allows itself on the form of those plans brings some risks of competitive distortion.

Suppliers will be in very different starting positions in reaching the Minimum Capital Requirements, and may propose very different routes to get there. There is some risk that these divergences may favour some suppliers over others, and in particular that those who can meet the Minimum Capital Requirements early - or who already do - may effectively suffer disadvantage as they compete against others with more leeway.

Transition Period / Controls

The Transition Period is slower than we would like, and exposes consumers to a material risk of significant failure costs for a further two years. We recognise that there are reasons for this - that suppliers cannot capitalise overnight - and that there is a risk of adverse unintended consequences in going sooner. For example, that a rush to accrue capital could result in overly aggressive debt recovery, which would not be in consumers' interests during a cost of living crisis. However, we are also acutely mindful that the socialised costs of past SoLRs runs into £bns and that a combination of volatility in wholesale markets and financial fragility in the supply sector brings risks of further collapses. As previously highlighted, there is also some risk of market distortion arising from allowing under-capitalised suppliers to compete with adequately capitalised ones.

We would therefore encourage you to view April 2025 as a backstop not a target when setting Capitalisation Plans for suppliers - those that can realistically reach the Minimum Capital Requirement earlier should be required to get there sooner.

The Transition Controls that you propose appear to have teeth and should therefore have a meaningful incentive effect on suppliers to provide suitable Capitalisation Plans.

Credit Cover Balance ('CCB') ringfencing

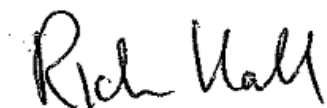
We expressed concern in our previous response about the discretionary approach to ringfencing CCBs, and the risk that this step may not be triggered until it is too late. You acknowledge these concerns, highlighting that your revised monitoring framework should be ordinarily sufficient. We retain concerns that Ofgem's track record on identifying and then stepping in to prevent consumer detriment is mixed. We will look to Ofgem to provide ongoing confidence that it is adequately resourcing its market monitoring and enforcement functions.

Although what you are proposing still gives Ofgem some discretion on whether to direct the ringfencing of CCBs when a trigger is met, we take some comfort from paragraph 4.42 that the default obligation, implicitly the default assumption, is that it will be directed. This gives slightly more certainty than previous proposals which implied that the hitting of a trigger would simply prompt an Ofgem decision, with less of a clear sense of what that decision was likely to be.

Other issues

Outwith the scope of this consultation, but similarly relating to the reduction in consumer exposure to SoLR costs, you consulted in 2022 on proposals to retain the value of hedges in the event that customers are transferred to a SoLR. Given the majority of past mutualised SoLR costs have related to wholesale costs, that workstream could offer significant protections to future consumers if a solution can be found. We would welcome an update on how your thinking on that matter is evolving.

Yours sincerely



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Chief Energy Economist