

31 March 2023

## **ICoSS response to Call for input on the Non-Domestic gas and electricity market**

The Industrial and Commercial Shippers and Suppliers (ICoSS) group is the trade body representing non-domestic industrial and commercial (I&C) suppliers in the GB energy market<sup>i</sup>.

This response is not confidential.

### **Q1. Do you have evidence of suppliers not being proportionate or reasonable regarding charges necessary to secure a contract, including security deposits? If so, please provide us with details.**

We do not have any evidence of such activities. We would note that despite the concerns raised regarding security deposits, the number of security deposits in the market is still relatively low; the Ofgem CEO letter indicates that 400 deposits a month in electricity, 150 a month in gas are usually requested, rising to a peak of around 800 a month in electricity and less than 200 a month in gas this winter. This represented at peak around 3% of all offers. Even if this reported rate is low, this figure needs to be set against the 2,500,000 meter points in the electricity non-domestic sector and 800,000 in gas; security deposits are still a small proportion of market coverage therefore, which need to be borne in mind when assessing the need for any systemic market reform in this area.

When looking at the amount a supplier may request to cover the likely risk of a supplying a customer, it is extremely difficult to assess the quantifiable cost in terms of risk when supplying a customer in such a large and diverse market. The nature and characteristics of the customer, in particular its financial viability will be amongst such factors, but the retail energy market has a number of specific characteristics that increase the risk compared to other markets:

- Suppliers cannot prevent a customer from taking an energy supply until they are disconnected, which takes considerable time and cost to achieve. By contrast wholesale suppliers to businesses in other market can simply stop providing goods or services when payment is not forthcoming.
- A customer can fail to pay for an energy supply for a considerable period without a supplier being aware that a customer will not be seeking or be able to pay for the energy it has used.
- Energy supply is a high turnover, low margin activity. As was stated in the recent letter to the Chancellor from the Ofgem Chief Executive<sup>1</sup> supplier profits are at most 3.6%. This is unsurprising as members have indicated that their cost to serve (including margin) only

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<sup>1</sup> <https://www.ofgem.gov.uk/publications/update-non-domestic-market-review>

represents 15-20% of the total bill. A single customer failing to pay therefore represents a large negative cost to the supplier in proportion to any potential margin.

- The market is currently going through the after-effects of the gas crisis where wholesale prices have increased significantly, as set out in the call for input. This will increase costs for customers which suppliers have no control over. As the materiality of the risk will also increase as prices rise, then suppliers will need to increase credit protections. This is recognised in the CEO letter. We would note that during times of market stress, for example during the COVID pandemic, other markets increased the duration of any credit protection required to cover their positions. A recent example given by a hospitality trade body during a roundtable was deposits for food deliveries increasing from 3 months to 6 months.
- Liquidity issues in the power market that are limiting non-domestic suppliers' ability to buy energy efficiently and so reduce costs as fast as markets are falling.

When taking the risk profile of the non-domestic retail market, it is our belief, backed up by the data provided by Ofgem so far in recent publications, that the strain the market is currently experiencing is due to high market prices not widespread unreasonable behaviour by suppliers. We do not believe therefore there is a case for significant market change to address a systemic or long-lasting market problem.

## **Q2. Do you have suggested solutions to the concerns around high costs requested to secure a contract and manage risk?**

We believe there are a number of ways in which the costs and risk can be managed to aid customers:

- Renew the underwriting of the Trade Credit Reinsurance Scheme<sup>2</sup> which allowed suppliers to continue to obtain credit insurance on non-domestic customers during the COVID pandemic. This will reduce the need for cash security deposits.
- A supplier of last resort scheme for sites that have entered administration. Suppliers would be able to transfer customers who have entered administration or liquidation to a central body. This is a common feature in a number of European energy markets and helps preserve the existence of the site until a new customer enters the premises.
- Move government levies and taxes off the energy balance sheet, either to central taxation or via payments to customers via their supplier until the market improves. This was a feature of the support provided during the winter of 2022/23 as the EBSR included costs of energy levies.
- Defer network cost increases through a "blend and extend" of costs to network customers. We note that the move to fix BSUoS costs has effectively done this.
- It is currently difficult for a supplier benchmark against its peers owing to a dearth of public information on security deposits, etc. We would again encourage Ofgem to publish the data they have received via RFIs in this area in an anonymised form that will allow

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<sup>2</sup> <https://www.gov.uk/government/publications/trade-credit-reinsurance-scheme>

suppliers to understand whether their activities are reasonable. We believe this will help reduce the occurrence of perceived unreasonable behaviour.

- As set out in Question 3 in more detail a number of members have indicated that prices in the market are starting to reduce as wholesale prices reduce, which is evidence of competitive pressures benefiting customers. Maintaining the competitive environment will further reduce prices faster than any market interventions.
- Improve market liquidity issues to allow falling market costs to be passed through to market prices as fast as possible.

We would have serious concerns over the negative impacts on the long-term viability of the market if suppliers were prohibited from managing their cost exposure, either through artificial price caps on prices or explicit limits on security deposits. Placing such limits will mean that customers who would have been supplied on the basis of a security being lodged, will instead not be offered contracts and remain on out of contract or Deemed rates. Longer-term, suppliers would seek to exit the market if suppliers cannot maintain their financial viability, as has occurred in the domestic market.

**Q3. Do you believe there has been an improvement in terms to contract as market conditions start to show signs of improvement? Please explain your answer.**

Yes. Members have reported that they are now seeking to reduce their prices and have already done so, which is evidence of the competitive market working as intended. It is vital that this price reduction is not jeopardised.

**Q4. Do you have evidence to support the allegation that suppliers have been inflating prices in response to the introduction of the Energy Bill Relief Scheme? If so, please provide us with details.**

We have no evidence of such practices. If such practices are being undertaken, then they would be contrary to the provisions of The Energy Bill Relief Scheme Regulations 2022. If Ofgem does have evidence of such a breach, we would anticipate it will look to undertake action in line with its powers under Part 6 of the regulations.

**Q5. What issues are you aware of businesses having in relation to deemed contracts?**

We request clarity on the use of the phrase “deemed contract”. As is set out in the Call for Input most customers when their fixed term supply contract ends do not move onto Deemed Contracts as covered under the Electricity Act 1989 and the Gas Act 1986; they move onto Out-of-Contract Contract (as recognised by the Supply Licence Condition 7A). With regard to Deemed Contracts we would note that Supply Licence Condition 7 sets out clear obligations on suppliers. We would welcome Ofgem undertaking enforcement action, if they are aware of any potential breaches of the licence in this area.

**Q6. Are there any other matters not discussed above related to pricing and contractual**

**behaviour that you would like us to explore? Please provide details and your reasons.**

The non-domestic market is, unlike the domestic market, subject to competitive pressure which will reduce prices as wholesale markets allow. There is evidence from members of contract prices dropping in response to these pressures. Significant changes to the market will not increase the rate of price reduction and instead is likely to harm the positive aspects of the market. Focus should be on helping customers through the current spell of high prices through the measures set out in Question 2.

**Q7. Do you believe there has been an increase in offers to contract in the past year as wholesale market conditions improved, or are there are segments of the market that are still struggling to secure contracts?**

We have left individual members to provide this information to Ofgem as is it commercially confidential.

We are aware of the concerns raised by certain customer representatives regarding the difficulty in obtaining contract quotes. ICoSS would like to repeat its offer to support any action by these trade bodies to help improve the understanding of their market sector.

**Q8. Are suppliers following the best practice steps around debt management and disconnection that we highlighted in our December 2022 letter or do you think that licence conditions need amending? Please provide evidence for your views and details of any specific examples.**

Considering the size of the non-domestic market we believe it will be very difficult to provide a comprehensive picture of supplier behaviour through specific case studies and individual examples will need to be assessed against the overall market. We note that Ofgem in its letter of 3 February 2023<sup>3</sup> that it required suppliers to provide a response on this subject. We believe it would be beneficial if Ofgem could consider publishing their overall findings (in an anonymised form) as a result of this request before any policy decisions are made in this area.

**Q9. Are suppliers' complaints process easy to find on their websites, or elsewhere? Do you believe we need to strengthen the rules around complaints processes? Please explain the reasons for your response.**

The Gas and Electricity (Consumer Complaints Handling Standards) Regulations 2008 states in regulation 11, that "*Each regulated provider must ensure that its complaints handling procedure appears at a clear and prominent location on its website.*" There is a clear and unambiguous obligation on suppliers to ensure their complaints process is easy to find and Ofgem should therefore seek to enforce the existing regulations.

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<sup>3</sup> <https://www.ofgem.gov.uk/publications/letter-suppliers-treatment-non-domestic-customers-during-debt-management-and-disconnection>

As demonstrated above, the current complaints process is highly prescriptive and places strict timescales on suppliers to acknowledge and address complaints. We are not aware of any systemic issues with the current complaint's framework. If Ofgem is aware of any suppliers who are not managing complaints in accordance with the current regulations, Ofgem should seek to undertake enforcement action.

**Q10. To what extent do you believe the communication you receive from your nondomestic supplier is clear and transparent? Please provide examples where possible.**

Considering the size of the non-domestic market we believe it will be very difficult to provide a comprehensive picture of supplier behaviour through specific case studies and individual examples will need to be assessed against the overall market.

**Q11. Do you think the issues around Change of Tenancy/Occupier are significant? What potential solutions would you suggest to address the perceived shortfalls in the existing Change of Tenancy and Change of Occupancy processes, that do not exacerbate the potential for fraud?**

Members do experience issues with false Change of Tenancy and Occupancy notifications in an attempt by customer to commit fraud. We would also expect in isolated incidences where communications between customers and suppliers will occur resulting in misunderstanding regarding the energy supply at a particular premises.

We believe that the most effective measures to address these issues is to provide clarity on what customers can expect from suppliers regarding contract renewals and what the customer can do to manage the issue. We would be supportive of Ofgem building on the work already done by EUK and ICoSS in this area and provide a trusted source of information that can be relied upon by customers.

**Q12. Are there any other issues you would like to highlight related to competition in the non-domestic supply market? Please provide detailed explanations.**

We agree with Ofgem; there is currently competition in the non-domestic sector. This provides significant benefits to customers in terms of customer service and lower prices than otherwise they would pay. The issues and concerns raised in the call for input and in other recent Ofgem publications are caused by high wholesale prices and increases in other costs that are outside of a supplier's control, not by excessive profit taking by suppliers.

Restricting competition through limits on supplier costs or how they manage risk will not reduce these outside cost pressures, or the risk they represent to the market. Any market changes must be focussed on allowing customers to manage these costs until market prices reduce, not damage competition as has occurred in the domestic market.

**Q13. Do you believe that there are segments of the non-domestic supply market, other than microbusiness customers, where there is not sufficient market pressure to correct any potential inappropriate supplier behaviours? Please provide detailed descriptions of these customers and evidence to explain your view, including what aspects of harm the regulations would need to help protect against.**

No. The current upper limits for microbusiness, with 100,00 kWh of electricity and 293,000 kWh resulting in an electricity currently spend around £500,000 a year in either fuel, implies large, well-established business. Customers with that level of energy consumption are likely to be seen as attractive customers and will have a more robust credit record. They are likely therefore to have more leverage with any supplier regarding contractual issues. If such customers are experiencing issues accessing the market at present, the focus should be in managing the unprecedented challenges in the non-domestic caused by very high energy prices as set out in Q2.

**Q14. If you responded yes to question 13, please suggest how these customers could be defined in the supply licence and identified by suppliers and customers.**

Please see our answer to Q13, though we would note there is currently considerable difficulty in identifying microbusiness customers currently on any definition that does not rely on information the supplier holds which is limited to the annual consumption of the energy being supplied by that supplier.

**Q15. If we expanded the definition of microbusiness customers or created a new class of customers, what are the possible implications and costs of doing this?**

Expanding the definition of microbusiness will have negative impacts in terms of higher costs and reduce competition for those customers captured by any wider definition, or a new class with additional obligations.

A number of regulatory processes apply only to microbusiness customers, which adds significant operational costs onto serving them. We would note that a number of non-domestic suppliers avoid supplying microbusiness customers owing to these higher costs. This applies to the broker market as well. For instance, members have noted that a significant number of brokers will no longer seek to engage with Microbusiness Customers owing to the additional costs the new ADR obligations represents. Expanding these obligations will mean fewer potential supply options for those customers.

In addition to these negative operational commercial impacts, we would also have concerns if the existing complaints process were extended to larger and more complex contracts. The level of expertise to appropriately judge appropriate costs in any complaint would be much greater, if customers with large and complex portfolios are classified as “microbusinesses”, which will drive up costs for all customers in a supplier’s portfolio.

**Q16. What additional protections do you think might need to be put in place to protect domestic customers who are supplied via a non-domestic contract? Please provide an explanation or evidence of the areas of harm any new regulation would protect against.**

This is a wide-ranging question and it would be useful to understand what specific detriment domestic consumers have occurred when being supplied under a non-domestic contract. We do not believe that such a customer would suffer detriment with regard to contract management or bill calculations as the non-domestic contract holder would be responsible for this; in the rare occurrence where a site has changed use or ownership from a non-domestic to a domestic premises then the customer can and should switch to a domestic supplier to ensure appropriate treatment.

With regard to safety, a considerable body of legislation exists regarding the protection of domestic consumers that are supplied via non-domestic contracts. In particular the Health and Safety at Work Act 1974 applies to any action by a supplier that exposes any third party (such as a domestic consumer) to risks to their health or safety. In addition, there is likely to be civil claims due to negligence, with the supplier potentially liable for any costs incurred. It would therefore be wrong to imply that non-domestic suppliers can disregard the welfare of domestic consumers in non-domestic premises given that our members are equally exposed to the same significant legal consequences.

Placing new obligations on suppliers to identify any potential domestic consumers will have a number of negative impacts. The cost of identifying, recording and managing this information will be high, as we anticipate that central system solution will be needed to capture and track this information, and will raise costs for all non-domestic customers at a time of high prices.

We also do not believe that suppliers will be able to easily discharge any such obligation as there will be no way to determine whether a domestic consumer is present in the non-domestic premises. Suppliers would be reliant on the non-domestic customer in informing the suppliers; experience of members in other areas of the market would suggest that not all customers will do so in a timely manner.

The additional cost of identifying and managing domestic consumers, the difficulty in doing so and the resultant higher regulatory risk created by any new obligations is likely to result in non-domestic customers with domestic consumers becoming less attractive to suppliers. This will reduce the likelihood of such customers being offered a contract and increase the probability of security deposits being requested. In particular we believe requiring non-domestic suppliers to manage domestic consumers will make small scale hospitality venues (such as pubs) less attractive to suppliers, so exacerbating the perceived issues regarding contract offers in this sector.

**Q17. Do you agree with the definition of, and clarifications around, what is a domestic customer as described in Appendix A? Are there other areas where further clarification is required?**

Yes. We believe that the licence condition is clear in how it sets out when a customer is domestic or non-domestic and so is the basis for identifying a domestic or non-domestic customer; we do note that in many cases industry parties erroneously use other definitions that are not based on the legal definition, such as Profile Classes in electricity settlement. We welcome this additional clarity from Ofgem and believe it will help improve understanding in the market.

Please note we believe the reference in this question is to Appendix 1 and have answered accordingly.

**Q18. Do you have any further comments about how the non-domestic market is currently segmented?**

We do not have any additional comments at this time as we believe the current definitions are appropriate.

Yours sincerely



Gareth Evans ICoSS

