

Adhir Ramdarshan
Ofgem
9 Millbank
London
SW1P 3GE

Sent via e-mail: futureretailregulation@ofgem.gov.uk

11 March 2016

Future of Retail Market Regulation

Dear Adhir,

I am pleased to attach the Energy UK response to the above consultation. It is not confidential.

The way customers interact with the market is evolving, and suppliers are responding to the demand for more flexible and innovative services and products. At the same time new and different suppliers are entering the market, and transformative technology and industry system changes are being introduced. Energy UK welcomes Ofgem's ambition to develop a regulatory framework which supports these changes, and the opportunity to respond to Ofgem's initial proposals - both through this consultation response and wider opportunities for engagement.

Energy UK's response is structured to address themes and priorities of immediate relevance. Some questions raised in the consultation ask for views on issues and areas which are contingent on decisions yet to be made by Ofgem (for example possible narrow principles) and the final recommendations of the Competition and Markets Authority (CMA) market investigation. Energy UK will comment on these proposals as they develop. Answers to individual questions are provided in Annex 1 of this response.

This response focuses on Ofgem's proposals as part of a move to more principles within the domestic retail electricity and gas licence conditions. Should Ofgem review the non-domestic licence conditions with the same intent, members urge it to do so with a fresh perspective which takes into account differences between the two markets, as default application of the approach taken in the domestic licence conditions to the non-domestic licence conditions would not be appropriate.

If you have any questions please do not hesitate to contact me on 020 7747 2963 or daisy.cross@energy-uk.org.uk

Yours sincerely

Daisy Cross
Policy Manager

Energy UK
Charles House
5-11 Regent Street
London SW1Y 4LR

T 020 7930 9390
www.energy-uk.org.uk
t @EnergyUKcomms

The future of retail market regulation

Energy UK response

11 March 2016

1. Introduction

1. 1. Energy UK is the main trade association for the energy industry, with over 80 members; representing energy generators and suppliers of all sizes. Our members supply gas and electricity and provide network services to both the domestic and non-domestic market. Energy UK members own over 90% of energy generation capacity in the UK market and supply 26 million homes and 5 million businesses, contributing over £25 billion to the UK economy each year. The industry employs 619,000 people across the length and breadth of the UK, not just in the South East, contributing £83bn to the economy and paying over £6bn annually in tax.
1. 2. Energy UK's retail members are: British Gas, Co-Operative Energy, DONG Energy, Ecotricity, EDF Energy, Engie, E.ON, Flow Energy, First Utility, GB Energy Supply, Good Energy, Haven Power, npower, Opus Energy, ScottishPower, Smartest Energy, Spark Energy, SSE, Utilita and Utility Warehouse.
1. 3. Energy UK strongly believes in promoting competitive energy markets that produce good outcomes for consumers. In this context, we are committed to working with Government, regulators, consumer groups and our members to develop reforms which enhance consumer trust and effective engagement. At the same time, Energy UK believes in a stable and predictable regulatory regime that fosters innovation, market entry and growth, bringing benefits to consumers and helping provide the certainty that is needed to encourage investment and enhance the competitiveness of the UK economy.
1. 4. These high-level principles underpin Energy UK's response to Ofgem's consultation on the future of retail market regulation (FRR). This is a high-level industry view; Energy UK's members may hold different views on particular issues. We would be happy to discuss any of the points made in further detail with Ofgem or any other interested party if this is considered to be beneficial.

2. Executive summary

Principles and prescriptive rules

2. 1. Energy UK is supportive of Ofgem using Standards of Conduct (SoC) as a keystone principle as it develops its proposals. However, Energy UK is not supportive of the broad principles proposed by Ofgem on the basis that:
 - There is not a clear justification for introducing the proposed principles.
 - The case has not been made for the need to regulate supplier inputs, as three of the broad principles seek to do. Suppliers already have incentives to engage constructively with the regulator, maintain good records and ensure board level assurances for the embedding of principles.
 - The proposed broad principles are potentially better suited to inclusion in compliance/enforcement guidelines.
2. 2. Members believe Ofgem should instead develop more specific, customer-oriented narrow principles.

2. 3. Members agree that some prescriptive rules will need to be retained, for example where the rules are constitutive to allow interoperability between suppliers, or where certain safeguards are needed for particular customer groups.

Compliance and Monitoring

2. 4. Ofgem's approach to compliance and monitoring must evolve to be compatible with more principle-based rules within the licence, and Energy UK welcomes Ofgem's intent to develop a safe environment for suppliers to trial new products and services. Ofgem should be prepared to lower its reliance on quantitative data, and monitoring should be risk based, be able to isolate and acknowledge the impact of external factors and influences on customer outcomes and opinions, and differentiate between one-off issues and systematic failures. Care must be taken to ensure implementation of any monitoring approach does not result in minimum standards, and compliance with principles should not be measured through benchmarking or comparisons.

Guidance

2. 5. Ofgem should ensure that any guidance produced as a result of its move towards principles-based regulation (PBR) does not undermine its goals regarding simplification and removing barriers to entry and innovation. The development of guidance should take account of Ofgem's commitments in its Simplification Plan¹ and Corporate Strategy². The full spectrum of rules and guidance to which suppliers must have regard should be accessible and navigable through Ofgem's website, ideally consolidated in one area of the website.

Merits-based appeals

2. 6. Given the more subjective nature of principles compared with prescriptive rules, licensees must have an effective route through which they can appeal Ofgem's enforcement decisions on the merits of cases brought.

3. Overview

3. 1. Energy UK welcomes the collaborative approach Ofgem has taken to its FRR programme, and members have appreciated the various opportunities to feed in views to Ofgem's wider consultation process, including through Ofgem's visits to the Energy UK Principles Based Regulation (PBR) Working Group. Members look forward to further engagement with Ofgem as it progresses with its plans, and Energy UK extends an open invitation for Ofgem to attend future meetings.
3. 2. Depending on the scale of changes to the licence, and the approach Ofgem takes to compliance and monitoring, the implementation of Ofgem's ultimate proposals could constitute the most fundamental change to the regulatory framework for the retail energy market since liberalisation. In view of this, and mindful of BIS' Principles for Economic Regulation³, Energy UK urges Ofgem to provide a suitable evidence base for and impact assess its proposals.
3. 3. In line with better regulation principles Ofgem should provide a compelling case for any proposals which would constitute extra regulation.
3. 4. Energy UK and its members believe Ofgem should seek to follow five guiding principles in order to ensure a successful transition to PBR:

¹ <https://www.ofgem.gov.uk/publications-and-updates/simplification-plan-2015-16-0>

² <https://www.ofgem.gov.uk/publications-and-updates/ofgem-our-strategy>

³ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31623/11-795-principles-for-economic-regulation.pdf

Energy UK's Guiding Principles for implementation of PBR

A. Communication

An open and trusting relationship between Ofgem and those it regulates is required for PBR to be successful.

B. Trust

Trust is based on open, honest and frank dialogue. To encourage the dialogue required to build this trust, the following could be explored:

- Regular engagement between Ofgem and suppliers
- Engagement through a range of bilateral meetings, workshops and an adequate and accessible policy interpretation and advice function within Ofgem; and
- A fair and appropriate compliance process with opportunities for dialogue with the regulator and an enforcement regime which allows for the option of independent review.

To encourage the dialogue required to build this trust, the following should be in place:

- An adequate and accessible policy interpretation and advice function within Ofgem; and
- A fair and appropriate enforcement process with opportunities for dialogue with the regulator and the option of independent review.

In addition, suppliers should be open and transparent and should cooperate with Ofgem.

The compliance, monitoring and enforcement regime needed to enable PBR to work needs to be developed in parallel with the regulatory framework. The reasonable person test used under Standards of Conduct is a useful starting point.

C. Flexibility

A desired outcome of a transition to PBR should be to facilitate greater innovation and competition. To promote this outcome compliance and enforcement must be flexible and allow for different suppliers to comply with Ofgem rules in different ways. If a matter comes to compliance/enforcement, it is reasonable for Ofgem to expect a supplier to be able to evidence that a reasonable and appropriate process was followed when it made the business decision to take an action, that action should be customer-focused and be able to demonstrate to Ofgem why the decision adheres to the relevant principle.

D. Clarity and consistency

Ofgem should work with suppliers to ensure all suppliers understand their responsibilities under a principle-based approach to regulation.

There should not be retrospective changes to Ofgem's interpretation of principles. Any policy changes should follow due process (i.e. consultation and impact assessment).

Ofgem should be consistent in its approach to compliance and enforcement, and be able to evidence this consistency.

E. Collaboration

We agree that Ofgem should consider the role and approach other stakeholders (including the Ombudsman Services: Energy and Citizens Advice) as it develops its proposals and introduces new rules.

Where possible consumer groups should be encouraged to approach suppliers directly to resolve/answer issues, concerns or questions, rather than going straight to Ofgem.

4. Broad principles

- 4.1. Members agree that the existing principles of SoC could provide a useful precedent as Ofgem considers how further principles could be used, both in terms of how they are used in the licence

(i.e. drafting) and how Ofgem implements, monitors and enforces principles as opposed to prescriptive rules.

4. 2. However, Energy UK does not support the supplemental broad principles proposed by Ofgem in its consultation. In particular, members note that three of the broad principles are not customer-focused, and do not promote or test consumer outcomes.
4. 3. Considering that in both the current regime and in a PBR world the licence is - and will likely continue to be - a combination of principles and prescriptive rules, Energy UK members ask Ofgem to explain its rationale for suggesting supplemental broad principles. Energy UK believes that suppliers have an incentive to demonstrate good corporate governance and compliance with Ofgem's rules. Members want to understand why Ofgem believes that the current legal and regulatory framework around corporate responsibility is not sufficient to ensure good practice in these areas.

Energy UK views on the specific principles proposed by Ofgem

Constructive engagement with the regulator

Depending on how it is drafted, the inclusion of such a principle could imply that suppliers should give Ofgem regular and detailed updates of their plans, or risk facing compliance assessment and possibly enforcement action. The spirit of such a principle would conflict with Ofgem's intent to promote flexibility and reduce the regulatory burden of its rules.

If Ofgem would like to receive specific quantitative information from suppliers, members feel that it would be preferable for Ofgem to make these requirements clear (rather than rely on principles).

Good record-keeping

Members are keen to understand whether Ofgem has evidence to suggest that suppliers do not currently keep adequate records which demonstrate compliance with obligations. Suppliers have an incentive to keep good records of their decision-making processes. Members note that the licence conditions, including the SOC, encourage suppliers to retain contemporaneous documentation. Members suggest that any expectations on suppliers with regards to record-keeping should be set via Ofgem's compliance approach, rather than through broad principles in the licence conditions.

Board-level assurance around embedding of principles

Members question whether it is appropriate or necessary for Ofgem to be able to make a judgement-based decision on the suitability of a supplier's board engagement strategy. Members believe that existing company law should provide an adequate framework and incentive for suppliers to follow good practice with regards to Board-level assurance. If this is not the case, Ofgem should provide evidence that suppliers are not taking appropriate steps in this regard, and define what type of relationship they want with the Boards.

Not putting consumer outcomes at risk

Innovation involves trialling and testing new products to determine whether customers are interested in those products. Suppliers do not know whether these trials will be successful and so the very act of a trial may put customer outcomes at risk. A broad principle requiring suppliers to not put customer outcomes at risk may make suppliers risk averse, reduce innovation and undermine the achievement of customer outcomes.

5. Narrow principles

5. 1. Members agree with Ofgem's suggested development of narrow principles with defined specific customer-focused outcomes. Such outcomes might apply to a specific customer group. However, until the CMA Market Investigation concludes, Energy UK will not comment further on possible suitable narrow principles.

5. 2. Members note the potential for conflict between narrow principles if they are derived individually, and urge Ofgem to consider narrow principles holistically to ensure individual principles fit into a cohesive whole. For example, Ofgem could revise groups of similar or related licence conditions.
5. 3. Ofgem should commit to not making retrospective changes to its interpretation of principles, including the existing SoC. Any policy changes should follow due process (i.e. consultation and impact assessment), and new principles should not be applied retrospectively to existing licence conditions.

6. Prescriptive rules

6. 1. Energy UK members agree that some prescriptive rules may need to be maintained, particularly where they are constitutive or provided specific customer protections. We believe that Ofgem should develop criteria to determine when to retain prescription, when to remove prescription and when to replace prescription with principles. Energy UK will provide views on possible rules that should remain prescriptive as Ofgem's programme develops, and after the CMA's final report is published.

7. Compliance framework

7. 1. A compliance process, which allows Ofgem to work with those it regulates to resolve problems that it has identified, could be the most important element in a successful transition to more principles-based regulation. Energy UK welcomes the focus Ofgem gives this theme in its consultation.
7. 2. Ofgem notes, and Energy UK agrees, that there will be times where Ofgem should only escalate an issue to enforcement after having given a supplier the opportunity to put things right. Members support Ofgem's review of its current process, and look forward to seeing further detail on Ofgem's plans.
7. 3. Energy UK acknowledges that any compliance or monitoring regime needs to allow Ofgem to maintain its ability to take enforcement action where a licensee acts contrary to its obligations in a way that causes detriment to consumers. It is in the interests of our members, their customers and of the industry as a whole that it continues to do so. Suppliers should be expected to be able to evidence that a reasonable and appropriate process was followed in making decisions which affect customers, and be able to demonstrate to Ofgem why these decisions meet relevant principles. At the same time, balance must be kept to ensure suppliers are able to innovate.
7. 4. Ofgem must also consider the role, views and approach of other stakeholders (including the Ombudsman Services: Energy and Citizens Advice). Where issues, concerns or questions around suppliers' interpretation of principles arise consumer groups should be encouraged to approach suppliers directly in the first instance rather than going straight to Ofgem.

Engagement

7. 5. Energy UK believes that Ofgem has an important role in providing assistance to companies on areas of regulation that are not straightforward to interpret, and this is particularly important as Ofgem moves to a more principles-based approach to regulation. Large companies need to provide clear internal policies for their many thousands of employees to follow, and new entrants may need time and assistance building experience and equipping themselves with the skills to deal with considerable, and often complex, regulatory requirements - including the ability to correctly interpret principles.
7. 6. Members agree that supplier-Ofgem interactions will need to change if Ofgem is to increasingly regulate through principles. An ongoing concern is suppliers' ability to accurately interpret Ofgem's rules.
7. 7. Resource within Ofgem which provides policy interpretation and advice for any new broad, narrow or prescriptive rules that are introduced to the licence would benefit consumers by:
 - helping to ensure that company behaviour reflects Ofgem's policy intent;

- helping new and potential new entrants understand what is or might be required of them when entering the supply market; and
 - lowering barriers to entry and growth, thus promoting competition.
7. 8. Examples of good practice in the industry can be found at Gemserv and at Elexon who provide support for suppliers who are going through industry accreditation of the Master Registration Agreement (MRA) and Balancing and Settlement Code (BSC).
7. 9. Energy UK looks forward to hearing further details of Ofgem’s ‘innovation space’.
7. 10. The full spectrum of rules and guidance to which suppliers must have regard to should be easily accessible through Ofgem’s website. Energy UK welcomes Ofgem’s proposals for a ‘guidance hub’, and suggests that guidance is clearly linked to relevant regulatory instruments, primary and secondary legislation.
7. 11. Energy UK welcomes the Ofgem/DECC Independent Suppliers’ Forum and Ofgem’s enforcement conferences as useful opportunities for government and industry to build relationships and share concerns.

Monitoring

7. 12. Energy UK believes that an effective monitoring regime which provides honest and reliable findings consists of two elements: 1) Ofgem getting to know and understand how different energy suppliers’ work; and 2) Ofgem gathering and analysing appropriate data in order to make evidence-based judgments on suppliers’ compliance with achievement of outcomes.
7. 13. We welcome Ofgem acknowledging the importance of monitoring being proportionate, risk-based, targeted and not unduly burdensome. Ofgem must not assume that increased monitoring is needed to ensure suppliers are compliant with its rules, but rather that monitoring should fit with a new way of viewing compliance.
7. 14. Energy UK notes that as Ofgem moves to a more principle-based rule book there will be fewer common data points across suppliers to measure compliance via quantitative analysis, and that monitoring will need to become more qualitative and bespoke. Each supplier’s compliance should be monitored and measured independently, and it would not be appropriate for Ofgem to measure suppliers’ compliance with principles through comparisons with or by benchmarking against other suppliers. For instance, if one supplier chooses to fulfil its obligations under a customer communication principles by providing its customers with an online live chat service, other suppliers should still be able to demonstrate compliance without providing this service. If Ofgem believes that prescriptive rules are required to achieve customer-focused outcomes, this should be specified and provided for in the licence.
7. 15. As is currently the case, responsibility for deciding whether a supplier practice is appropriate should lie with the supplier, and Ofgem’s compliance and monitoring regime should not involve Ofgem suggesting or signing-off suppliers’ practices.
7. 16. Any monitoring system needs to be able to isolate and acknowledge the impact of external factors and influences (e.g. price changes, industry system changes) on customer outcomes, and be able to differentiate between one-off issues and systematic failures. Ofgem should look to include positive metrics and not just seek to rely on negative metrics to measure market performance as can be seen in the current regime.
7. 17. Ofgem should only seek to publish data on supplier performance where it can be assured that the data is both (a) objective and (b) provided by licensees using common defined rules of interpretation. An example where this does not happen today is the publication by Ofgem of supplier complaints metrics which are (a) self-reported and (b) based on a highly subjective definition whereby suppliers determine their own interpretation of the requirements accordingly.
7. 18. Energy UK comments on various monitoring models and options in Annex 3. When evaluating these options, the following points should be considered:

- The options could be used on either an ad hoc or routine basis.
- A combination of different options could be used for different licence or customer service themes. Ofgem might determine that certain aspects of market activity are ‘high risk’ (for instance through a market-wide analysis), and allocate the appropriate monitoring method accordingly. Determining high risk areas may be contingent on the size of the problem (e.g. how many customers affected) and the intensity of the problem (e.g. how badly they are affected), or a combination of the two.
- Ofgem could choose a different key risk theme each year, and concentrate its high-intensity approaches (e.g. challenge panels) on these areas, while using lower-intensity approaches (e.g. informal bilateral meetings) for areas it identifies as low-risk. Some options may be able to address both high and low risk issues in tandem, for example bilateral meetings.

7. 19. Energy UK has not commented on quantitative data in this response or in the Annex. Neither will we comment here on the suitability of the quantitative data Ofgem currently gathers for monitoring current or future markets. As before, the CMA outcomes and Ofgem’s decisions on narrow principles could influence Energy UK’s position on appropriate data to be gathered by Ofgem.

7. 20. An example of an industry monitoring system is set out in Annex 2, which provides a high level summary of the Performance Assurance Framework in the BSC.

8. Guidance

8. 1. Energy UK welcomes Ofgem’s acknowledgment that guidance can amount to “prescription by the back door”.

8. 2. Ofgem should ensure that any guidance produced as a result of its move towards PBR does not undermine its goal of simplification and removing barriers to innovation. The development of guidance should take account of Ofgem’s commitments in its Simplification Plan 2016-17 and Corporate Strategy.

8. 3. It is unclear from the consultation whether and how Ofgem differentiates between binding and non-binding guidance, and members welcome clarity on this point.

8. 4. As noted in paragraph 7.10, guidance should be clear and easy to find on Ofgem’s website. Ofgem should review the layout of its website to ensure guidance is clearly signposted and linked to licence conditions.

9. Enforcement

9. 1. Since 2012 there have been a number of developments which have strengthened the case for an appeals process that is clearly merits-based. One of these is Ofgem’s intent to regulate more through principles which, being more subjective than prescriptive rules, are more susceptible to mistakes in enforcement decisions. Ofgem has also stated that it intends to impose higher fines as a matter of policy. It is, therefore, important that licensees have an effective route to appeal all Ofgem enforcement decisions on the merits of the case.

9. 2. Members believe that Ofgem should allow a due diligence defence as further principles are added to the licence, as this would solve many of the known problems of PBR identified by Black *et al* (2007)⁴ such as regulatory uncertainty, guidance proliferation, and hindsight-driven enforcement. The supplier should be able to show that it ‘took all reasonable precautions and exercised all due diligence’ to prevent a negative outcome. The standard is high and requires the supplier to have taken all reasonable precautions to prevent a negative outcome. The due diligence defence is well established in the UK law, regulated sectors such as food standards and in regulation in other jurisdictions, such as Canada.

⁴ Black, J, Hopper M and Band, C (2007), ‘Making a Success of Principles Based Regulation’ *Law and Financial Markets Review* 1(3): 191-206

10. Next steps

10. 1. Energy UK looks forward to engaging with Ofgem in detail on certain areas Ofgem has identified, such as monitoring and compliance, and continues to extend an open invitation for Ofgem to attend the regular sessions of our standing PBR Working Group.
10. 2. Members would welcome a schedule or plan which details which prescriptive rules will be reviewed - and timelines for this review.

11. Timelines

11. 1. As it progresses with its plans, Ofgem must also consider the impact of the CMA's final findings and remedies, the impact of potentially prescriptive European regulation in retail energy markets (i.e. the Commission's New Deal), and continued Ofgem and DECC-led policy development taking place before and during the transition (e.g. Ofgem's Priority Services Register review, objections review and Switching Significant Code Review).

ANNEX 1: Answers to specific questions

Chapter 2: Reforming the rulebook

Question 1: In what circumstances do you think that prescriptive rules are likely to be most appropriate? Which specific SLCs/policy areas should remain prescriptive in nature?

- Energy UK will reserve judgement on the suitability of existing or possible future prescriptive rules until more detail is known about Ofgem's approach to broad and narrow principles, and what the rule book as a whole may look like.

Question 2: Should we supplement the principle of "treating customers fairly" with any other broad principles? If yes, please outline what these should be and why.

- Energy UK does not understand the justification for introducing new broad principles, and does not agree with Ofgem's proposed broad principles set out in the consultation.
- See section 4 for our views on broad principles.

Question 3: Where might narrow principles be more appropriate than broad principles or prescription?

- See response to Question 1. See sections 4, 5 and 6 for more information on Energy UK's views on broad, narrow and prescriptive rules.

Question 4: What are your views on the potential merits or drawbacks of incorporating consumer protection law into licences?

- Energy UK members do not support this incorporation. If Parliament had felt it suitable that Ofgem held these powers, these would have been granted already. The recent introduction of the Consumer Rights Act 2015 has already consolidated consumer protection in one place.
- Suppliers should not face dual regulation.

Question 5: How should we use principles and prescription to most effectively protect consumers in vulnerable situations?

- See response to Question 1.

Question 6: Do you agree with our proposed approach to guidance?

- See section 8.

Chapter 3: Operating the rulebook: engagement and monitoring activities

Question 7: How can we best engage with suppliers in the context of principles?

- Energy UK members are supportive of Ofgem's proposal to expand its engagement to help broaden its understanding of the market and the suppliers that operate within it. See section 7 for Energy UK's views on a suitable monitoring regime for a more principles-based regulatory framework.

Question 8: What specific support may be needed for new and prospective entrants?

- See section 7 for Energy UK's views on engagement.

Question 9: Do you have any views on how best to approach monitoring in the context of principles? Specifically, which indicators and approaches should we use to catch potential problems early?

- See section 7 for Energy UK's views on a suitable monitoring regime for a more principles-based regulatory framework.

Question 10: Do you have any views or comments on the following proposals?

- We will expand our engagement with suppliers to enhance our understanding of their businesses and help them better understand our rules so they can get things right first time.
- We will collaborate closely with the Citizens Advice Service and the Ombudsman Services: Energy to ensure we maximise the effectiveness and impact of the monitoring activities across our organisations.
- Energy UK is supportive of the proposals expressed in Question 10. See section 7 for Energy UK's views on a suitable monitoring regime to fit with a more principles-based regulatory framework.

Chapter 4: Operating the rulebook: compliance and enforcement

Question 11: Do you have any views on how best to approach compliance in the context of principles?

- See section 7 for Energy UK's views on compliance.

Question 12: Do you have any views or comments on the following proposals?

- We will retain our current flexible and discretionary approach to escalating issues to enforcement. We will prioritise compliance activities where possible and appropriate.
- We will increase the links to the level and impact of harm when deciding whether to open a case.
- Engaging early with Ofgem may reduce the likelihood of later enforcement. Information from engagement and monitoring activities may be shared with enforcement where appropriate.
- We will continue to apply our full range of enforcement tools to principles-based rules.
- We will make it easier for all suppliers to learn lessons from enforcement outcomes.
- Enforcement action will continue as usual throughout the transition to principles.
- See section 9 for Energy UK's views on Ofgem's approach to enforcement to fit with a more principles-based regulatory framework.

Chapter 5: Managing the transition effectively

Question 13: How would you like to engage with us on our proposals and the broader work programme?

- See sections 10 and 11 for Energy UK's views.

Question 14: Do you agree with our proposal to take a phased, priority-driven approach to reforming the supply licences.

- Energy UK approves of Ofgem's approach here.
- As stated in section 5.2, there might be increased potential for conflict in the licence if narrow principles are approached and determined individually.

Question 15: Which areas of the licence should we prioritise? In particular, please provide examples where existing prescriptive rules may be causing problems or where market developments are leading to new risks to consumers.

- As well as SLC25 Energy UK recommends Ofgem prioritises the following:
 - Billing provisions (SLC31.A)
 - Tariff cap rules (SLC22B)

Question 16: Can you provide any initial views on potential costs and benefits (eg avoided costs) of regulation via principles versus prescription to your organisation? Please explain which parts of our proposals (eg rulebook, operations) these costs relate to.

- Members will respond individually.

Chapter 6: Exploring priority areas for reform

Question 17: Are the existing provisions of SLCs 25.1 and 25.2 the right ones for regulating sales and marketing activities (or are any additional principles needed)?

- Energy UK agrees that this condition should be reviewed. Members note that face-to-face sales is an important channel for key non-switching groups to access deals in the market, and it shouldn't be eliminated.

Question 18: What, if any, prescriptive rules are needed in addition to the principles in SLC 25 to deliver good consumer outcomes?

- Members note that suppliers should ensure that customers have access to fair comparisons over the phone/face-to-face, for example at what point is the personal projection used, and that this could be an element which needs to be consistent across the market. For instance a supplier could be thorough, but in doing so provide a bad customer experience.

Question 19: What engagement and monitoring process might be required to best operate SLC 25? Members note the potential for a media backlash on the removal of this rule – customers have been failed in the past.

- See monitoring options table in Annex 3.

ANNEX 2: A high level summary of the Performance Assurance Framework in the Balancing & Settlement Code (BSC).

Elexon, the BSC code administrator, monitors industry performance against a number of different measures, which are measured against lagging indicators.

If a supplier falls behind the minimum standard required for a measure for three consecutive months, it will likely be placed into the Error & Failure Resolution (EFR) process at which point the issue is brought to the attention of the Performance Assurance Board (PAB). When a party is placed in the EFR process it is required to submit a plan to improve its performance to Elexon. If Elexon has any concerns with that party, for example they consistently fail to meet the plan milestones, the issue will be escalated to the PAB. The PAB may ask for that party to come in to one of its meetings to explain its performance and how it will get back to the required standard. The PAB will then decide the course of action required.

The PAB is a BSC Panel subcommittee made up of individuals who work in the industry. These individuals must sign a confidentiality agreement and, if employed by a company, a waiver is signed by their manager to say that the individual will be impartial industry representatives i.e. not representing that company.

In effect, the PAB polices industry performance. It meets monthly to look at performance trends based on information provided by Elexon, discusses any settlement related and BSC audit issues, as well as acting as an escalation point on failing parties as previously mentioned. If necessary it can escalate issues to the Panel who, in turn, can escalate the issue to Ofgem - although in practice this would rarely happen.

Installing a function similar to the PAB subcommittee within Ofgem is worth consideration, although members suggest a similar function would need to differ in some aspects, for example Ofgem representatives rather than industry representatives should staff the committee.

Elexon also has Operational Support Managers (OSMs) who manage the relationships with industry parties. They manage several different parties each and meet on a monthly basis with those parties to discuss performance and issues, but are also available for ad hoc discussions between those meetings. If a supplier is in the EFR process it might meet more regularly with OSMs.

ANNEX 3: Monitoring options for principles-based/outcomes-led regulation in the electricity and gas retail energy market

- The options discussed here do not include quantitative data e.g. complaints data, which will be considered as Ofgem progresses with its proposals. Neither will we comment here on the suitability of the quantitative data Ofgem currently gathers for monitoring current or future markets.
- Throughout this annex the term 'Process' is used to describe the protocol suppliers use to come up with a product, internal process or system (for example customer feedback mechanism, product testing, double checking customer details, information flows etc.). This could also capture whether the supplier's leadership or management is appropriate. 'Practice' is used here to describe these supplier actions.
- Any of the options set out here could be used on either an ad hoc or routine basis.
- A mix of different options could be used for different areas. Ofgem might determine that certain areas are 'high risk' (for instance through a market-wide analysis). Determining high risk areas may be contingent on the size of the problem (e.g. how many customers affected) and the intensity of the problem (e.g. how badly they are affected), or a combination of the two.
- Ofgem could choose a different key risk theme or area every year, and concentrate its high-intensity approaches (e.g. challenge panels) on these areas, while using lower-intensity approaches (e.g. informal bilateral meetings) for areas it identifies as low-risk. Some options may be able to address both high and low risk issues in tandem, for example during bilateral meetings.
- The table considers each option against the following criteria:
 - Does each option lend itself to specific areas, or to general supplier behaviour?
 - How responsive is the option i.e. is there a time lag?
 - Is it scalable?
 - Is it futureproof?
 - How resource-intensive is it for suppliers?

| Option | Is it used elsewhere? | How will it work? | Good for a specific area, or more general? | Is it responsive? | Is it scalable? | Is it practical on a long term basis? | Is it resource intensive for suppliers? | Is it time intensive for suppliers? |
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| Challenge Panel | <p>In 2014 Ofgem used a challenge panel to explore supplier progress in implementing its SOC⁵.</p> <p>Ofgem asked suppliers to tell it what they had changed to make things fair for consumers and what impact this was having.</p> <p>Ofgem reviewed their submissions and invited some suppliers to be interviewed by the Panel.</p> | <p>This unit or panel would engage regularly (for example on an annual basis) or on an ad hoc basis with suppliers, as well as Ofgem policy and enforcement teams.</p> <p>Ofgem will need to make it clear that any reports produced do not constitute best practice.</p> <p>Panellists must have an appropriate level of expertise and experience of the retail energy market.</p> <p>Panel members should be rotated regularly.</p> <p>It would not be appropriate for suppliers to share ideas on innovation or other business-sensitive information.</p> | <p>This could work either as a number of distinct panels looking at specific issues or as one wider group of experts looking at more general issues.</p> | <p>Limited ability to respond quickly. Using a panel is unlikely to work in an environment where other suppliers are present. It really only works on a retrospective basis. Better suited to addressing priority areas determined in advance.</p> | <p>Limited ability to scale this option, as an effective panel would need to have a minimum number of participants.</p> | <p>This option is flexible, and therefore able to adapt to future regulatory changes.</p> | <p>This option could be resource-intensive, depending on how it is used.</p> <p>If used periodically this would not necessarily be too resource-intensive for suppliers.</p> | <p>This option could be time-intensive, depending on how it is used.</p> <p>If used periodically this would not necessarily be too time-intensive for suppliers.</p> |

⁵ <https://www.ofgem.gov.uk/ofgem-publications/93839/standards-of-conduct-findings-from-the-2014-challenge-panel-pdf>

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| Internal supplier challenge panel | Some suppliers have held 'mock' internal panels and invited external stakeholders (for example consumer groups). | Individual suppliers would host a panel or roundtable session where they would set out Practice or Process in front of external stakeholders. An open dialogue on these Practices and Processes could lead to a submission from the supplier to Ofgem, in the form of an annotated internal audit. | This could work either as a number of distinct panels looking at specific issues or as one wider group of experts looking at more general issues. | Limited ability to respond quickly. Better suited to addressing priority areas determined in advance. | Limited ability to scale this option, as an effective panel would need to have a minimum number of participants. | This option is flexible, and therefore able to adapt to future regulatory changes. | This option could be resource-intensive, depending on how it is used. If used periodically this would not necessarily be too resource-intensive for suppliers. | This option could be time-intensive, depending on how it is used. If used periodically this would not necessarily be too time-intensive for suppliers. |
| Account management/ relationship-led monitoring | FCA model | Firms are allocated a dedicated account manager. Ofgem can undertake high-intensity oversight of firms. Firms may need to participate in business model and strategy analysis, regular meetings between Ofgem officials and senior management, annual strategy meetings and annual firm evaluation, 'deep dive' assessments, and baseline monitoring of regulatory returns. | Depending on how it is used, this model seems better suited to evaluating a company more generally given the level of seniority involved in the monitoring activity. | Yes | Yes | This option is flexible, and therefore able to adapt to future regulatory changes. | This option could be resource-intensive, depending on how it is used. | This option would be very time intensive given the pressures on senior staff but it could be kept to a fairly tight timeline to mitigate this. |

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| Site visits | Ofgem already does this on an ad hoc basis | Ofgem would visit suppliers premises on an individual basis | This could be tailored to a general inspection or a visit to investigate a particular activity. | Yes | Yes | This option is flexible, and therefore able to adapt to future regulatory changes. | This option could be resource-intensive, depending on how it is used. If used periodically this would not necessarily be too resource - intensive for suppliers. | This option could be time-intensive, depending on how it is used. If used periodically this would not necessarily be too time-intensive for suppliers. |
| Case studies | | Suppliers would give Ofgem an example of its Process to ensure a supplier succeeds in meeting a certain customer outcome. This could be supplemented by a follow-up visit if required. Feedback would be provided bilaterally. | This would be more suited to investigate specific issues. | Limited ability to respond quickly. Better suited to addressing priority areas determined in advance. | Limited ability to scale this effectively. | This option is flexible, and therefore able to adapt to future regulatory changes. | This option could be resource-intensive, depending on how it is used. If used periodically this would not necessarily be too resource - intensive for suppliers. | This option could be time-intensive, depending on how it is used. If used periodically this would not necessarily be too time-intensive for suppliers. |

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| Mystery shopping | Suppliers, consumer bodies and Ofgem already use this. | Primary research would be commissioned to test different areas of customer service. | This would be more suited to investigate specific issues. | Limited ability to respond quickly. Better suited to addressing priority areas determined in advance. | Limited ability to scale this option, as an effective panel would need to have a minimum number of participants. | This option is flexible, and therefore able to adapt to future regulatory changes. | No | No |
| Customer forums/surveys (Ofgem-led) | Network operators use a similar system. | Suppliers could provide details of a subset of customers to Ofgem, who would contact customers and get feedback on key customer service themes. | This could be tailored to a general inspection or a visit to investigate a particular activity. | No | No | A long term tracker survey could be created for monitoring particular areas of concern. | No | No |
| Customer forums/surveys (supplier-led) | N/A | Suppliers would contact customers and get feedback on key customer service themes. | This could be tailored to a general inspection or a visit to investigate a particular activity. | No | No | A long term tracker survey could be created for monitoring particular areas of concern. | No. | No. |
| Bilateral 'risk' meetings | N/A | Ofgem could meet with suppliers on an individual basis to allow Ofgem/suppliers to share views on what risks exist, and determine what is being done by suppliers to mitigate/manage these risks. | This would be more suited to investigate specific issues. | Fairly responsive as it would be easy to call a meeting at short notice. | Limited ability to scale this option as it eventually it becomes Account management/relationship-led monitoring. | This option is flexible, and therefore able to adapt to future regulatory changes. | If used periodically this would not necessarily be too resource - intensive for suppliers. | If used periodically this would not necessarily be too time-intensive for suppliers. |

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| Independent audit | Energy UK Safety Net, and Billing Code | An external auditor would assess suppliers' business practices to establish whether suppliers are operating in line with their Processes and Practices, highlighting areas of further investigation. | This would be more suited to investigate specific issues. | No | No | This option would require regular monitoring of and rewriting of codes to keep relevant/respond to changes. | This option has the potential to become fairly resource-intensive for supplier. | This option has the potential to become fairly time-intensive for suppliers. |
| Increased bilateral engagement | Ofgem meets suppliers on a regular basis | A more regular, longer, more detailed and/or routinely scheduled programme of meetings between suppliers and Ofgem which could capture detail on supplier Practice and/or Process. | This could be tailored to a general inspection or a visit to investigate a particular activity. | No | Limited ability to scale this option as it eventually it becomes Account management/ Relationship-led monitoring. | This option is flexible, and therefore able to adapt to future regulatory changes. | This option has the potential to become very resource-intensive for supplier. | This option has the potential to become very time-intensive for suppliers. |

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| <p>Earned recognition</p> | <p>Defra⁶ uses this method for farm inspections.</p> | <p>Ofgem concentrates its monitoring resource on suppliers with a history of non-compliance - previous non-compliance triggers more in-depth focus.</p> | <p>This could be tailored to a general inspection or a visit to investigate a particular activity.</p> | <p>By definition it is responsive as non-compliance triggers more in-depth monitoring.</p> | <p>Yes</p> | <p>This option may become unsuitable under future regulatory conditions.</p> | <p>The appeal of this approach is that high performing companies reduce their regulatory burden.</p> <p>Will have resource implications for lower performing suppliers when they try and improve performance.</p> <p>Also allows higher performing suppliers to allow their resource to work on continuous improvement rather than and potentially unnecessarily regulatory burdens.</p> | <p>The appeal of this approach is that high performing companies reduce their regulatory burden.</p> |
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⁶ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/236270/pb14026-earned-recognition-plan-130830.pdf

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| <p>Unannounced visits/inspections</p> | <p>Ofsted</p> | <p>Following an initial monitoring inspection, the inspector would recommend whether or not further monitoring and other activity should occur to encourage the company's improvement to give it the incentive to improve and be judged good or outstanding at its next inspection.</p> <p>During the monitoring inspection, the inspector could decide where to focus inspection activities and vary the way they work to reflect the circumstances of the company.</p> | <p>This model seems better suited to evaluating a company more generally while having the potential to identify particular issues for companies to improve on.</p> | <p>No. The nature of the monitoring activity is the fairly random and arbitrary nature of the visits.</p> | <p>Yes.</p> | <p>This option is flexible, and therefore able to adapt to future regulatory changes.</p> <p>However, business' future working practices may change as suppliers become increasingly agile in their working practices, and unannounced visits are likely to be unproductive if the relevant people are not on site.</p> | <p>This option has the potential to become very resource-intensive for supplier but only for a limited time i.e. during the visit itself. This is dependent on how many visits occur.</p> | <p>This option has the potential to become very time-intensive for suppliers but only for a limited time i.e. during the visit itself. This is dependent on how many visits occur.</p> |
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| In-depth issue-specific review | Debt and disconnection best practice review ⁷ | <p>Closed best practice review meetings, consisting of ad hoc meetings on specific high-risk issues, between consumer groups, Ofgem and supplier.</p> <p>This could be used as a baseline best practice exercise, undertaken as PBR is implemented, and then subsequently for each new supplier as it enters the market.</p> | Issue specific. | Yes. | Yes. | This option is flexible, and therefore able to adapt to future regulatory changes. | This option has the potential to become very resource-intensive for suppliers but only for a limited time (the review period). This is dependent on how often reviews occur. | This option has the potential to become very time-intensive for suppliers but only for a limited time (the review period). This is dependent on how often reviews occur. |
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⁷ <https://www.ofgem.gov.uk/ofgem-publications/57449/debt-and-disconnection-best-practice-review.pdf>