

22nd January 2019

Response to Ofgem consultation: Supplier Licensing Review

Summary:

We agree that a supplier failure is disruptive for the market and imposes costs on other parties in the market, including independent network operators. These costs include additional administration in managing the Supplier of Last Resort (SoLR) process and seeking to recover bad debt.

Energy markets differ from others in that participants are interconnected, and consumers continue to receive a service even when their energy supplier fails. This presents a risk to the market that is not seen elsewhere and justifies additional safeguards being in place.

We therefore support this initiative from Ofgem to ensure that the licensing regime for suppliers is more robust and failures are reduced as much possible.

We agree with the view that in a competitive market there will always be supplier failures and therefore it is important to look at ensuring the exit arrangements work to minimise costs and disruption.

It is not right that future energy consumers pay higher costs than they should to fund a small sub-set of customers who have benefitted from having lower prices charged to them by a risky supplier in the past. This cross-subsidy is not in the interests of consumers nor the market.

In our view the best form of protection for consumers and the market will be to look to reintroduce some form of security cover requirement for suppliers or an insurance scheme to be called upon in the event of a default.

It isn't clear to us as to why this was removed in 2001 and the recent failure of multiple suppliers calls the logic of this into question. There will be a cost to suppliers of introducing a requirement for security cover, but we believe that these costs can be justified if it protects the wider customer base paying more than they should.

We believe Ofgem's review of exit arrangements should include a wider review of the credit cover and collateral requirements that suppliers currently need to put in place. It would be better to have a more consolidated approach to security cover; replacing the existing obligations within industry codes (that support network, smart metering and settlement) and last resort supplier payments. Such a scheme could also help protect Government environmental and renewables schemes.

This approach would be straight forward for new entrant suppliers to understand; could be tailored to look at the risk that specific companies present to the market, as well as being less costly to administer. Ultimately a lower cost, more resilient set of arrangements will lead to reduced charges for the market and for consumers when suppliers fail.

Response to consultation questions:

Do you agree with our proposal to introduce new tougher entry requirements and increase scrutiny of supply licence applicants? Do you agree this can be achieved with increased information requirements and qualitative assessment criteria?

Yes, this will help although this ultimately will not remove the potential risk of supplier failures impacting upon the market and customers of other suppliers.

Do you agree that our proposed assessment criteria for supply licences applications are appropriate?

Yes, the criteria seem reasonable although there are additional costs that this approach will present to the market.

Firstly, the proposed level of reporting and oversight will incur costs on suppliers. Therefore, it is right to conclude that this might act as a barrier to innovation by deterring very small new entrant companies.

Secondly, there will also be a significant cost to Ofgem to resource the oversight of the supplier market which should be included in the assessment. Ofgem will need to have the resource available to be able to interpret and understand the different approaches to risk being proposed by licensees. This may not be an easy task to achieve and require significant effort by Ofgem.

We believe that these additional administrative costs are justified by the protection to the market that the proposals should deliver.

Do you agree that applicants should provide evidence of their ability to fund their activities for the first 12 months, and provide a declaration of adequacy?

Yes, this seems a reasonable approach.

Do you agree with the specific information we would generally expect applicants to provide (in Appendix 1)? If not, why/what would you add or change?

No comment

Do you agree that applicants should provide a narrative in respect of their key customer-related obligations under the licence?

No comment

Do you agree with the areas we would generally expect applicants to cover (in Appendix 1)? If not, why/what would you add?

Do you agree that we should ask additional 'fit and proper' questions as part of the application process (as set out in Appendix 1)?

No comment

Do you agree that Ofgem's licensing process should be undertaken closer to proposed market entry? Do you identify any barriers to this approach or any adverse impacts of this change?

Yes, it is a good idea to address the issues that the emergence of the 'supplier in a box' process has created for the market. Providing for the licence award to be between entry

assessment and controlled market entry should remove some of the existing issues and create a more robust process.

Do you consider that suppliers should report on their financial and operational resilience on an ongoing basis? If so, do you have any initial views on the content of these reports/statements?

Yes, this proposal would be an additional minor administrative burden on suppliers but is something that a prudent financial organisation should be able to provide without significant effort.

Do you have any initial views on the potential introduction of targeted or strategic monitoring/requirements on active suppliers?

Regardless of their relative size, disruption and costs to the market is created by a supplier failing. The same processes must be undertaken to enact the SoLR and to redistribute the affected customers.

It isn't therefore clear that there is a justification for applying different criteria to suppliers based upon the number of customers they have. It should also be recognised that different safety measures apply to large suppliers which now make the risk that they present to the market lower.

A more comprehensive risk-based approach to security cover for suppliers might address the issues of company size and is something that we would suggest Ofgem consider further in their review of supplier exit arrangements.

Do you have any initial views on the potential introduction of prudential/financial requirements on active suppliers?

It is sensible to set out clearly the criteria by which suppliers will be measured to aid in their preparation and to set expectations for new entrants.

It isn't clear what sanctions Ofgem would be able to apply should a supplier fail the requirements. An option may be to stop new registrations by the supplier as this has been shown to be effective in the past at addressing poor performance and behaviour.

In practice it may only provide an early warning of a supplier failure. It may allow for a degree of mitigation as the market prepares for a failure but ultimately it will not eradicate the issue of supplier failure and the consequences for consumers.

Do you consider that Ofgem should introduce a new ongoing requirement on suppliers to be 'fit and proper' to hold a licence?

Yes, this seems a sensible approach.