

Lesley Nugent
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Ofgem
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By email: licensing@ofgem.gov.uk

Dear Lesley,

RE: Supplier licensing review - Consultation on New Applications Regulations, Application Forms and Guidance Document

Centrica considers the final proposals of Ofgem's review of supplier licensing to be an important step in implementing a more robust market entry process. While the final proposals may not be as rigorous as those we asked for in our consultation response¹, we consider it a positive outcome compared to the status quo.

We welcome the opportunity to comment on the accompanying Statutory Instruments, application forms and application guidance. Our answers to the specific questions in the consultation are appended to this letter.

We note that Ofgem will be consulting shortly on the ongoing monitoring of suppliers and managing market exit. It is in the monitoring of suppliers and market exit processes where Ofgem should be able to have a more significant impact by reducing the likelihood and impact of mutualisation of costs when suppliers fail.

Recent supplier failures are estimated to have resulted in over £150million being redistributed across the remaining energy suppliers, who will have to pass this cost through to consumers. The current regime is not designed to reduce the likelihood and impact of this harm to competition and consumers.

Centrica remains committed to our proposed licence condition as a potential solution to prevent the mutualisation of costs. Our licence condition would require each licensee to prevent mutualisation of its debts if it fails:

- The onus will be on supply licensees to demonstrate adherence to this condition, for example by:
 - Ringfencing credit balances in an Escrow account;
 - Having sufficient secured finances in place to cover their current and future debts;
 - Having a parent company guarantee in place;
 - Having a 'living will' in place that sets out how the company would be wound down in an orderly fashion, should it fail. The living will should include details of the steps that would be taken to avoid mutualisation of costs; or

¹ https://www.ofgem.gov.uk/system/files/docs/2019/04/centrica_response.pdf

- Appointing an intermediary to cover the credit and mutualisation risk -- and if so, having such funds in place to cover any intermediary fees.
- Suppliers would be required to have secured financing arrangements in place to meet likely scenarios that could place additional costs on a supply business -- including spikes in commodity costs and a colder than average winter.
- Suppliers would be required to lay out clear proposals for the management of aged debtors, both operationally and in terms of accounting. And disclose any factoring arrangements in place – whereby any debt is sold on to a third party to recover.
- Licensees should be required to report to Ofgem on a regular or targeted basis on how they are complying with the above licence condition. The reporting should reveal whether, and the extent to which, customer credit balances and cash required to cover Government policy obligations, are being used to finance risk and operational costs, and whether the licensee could refund customers' credit balances if called upon.
- Ofgem should focus on those licensees which are most likely to risk their debts being mutualised. Therefore, if the reporting to demonstrate compliance with the licence condition is targeted rather than regular, it should be automatically triggered by risk criteria including:
 - low or below-cost tariffs,
 - rapid customer growth,
 - unexpected increases in Direct Debits,
 - requiring customers to pay for energy in advance,
 - customer service problems, particularly those where customers struggle to get their credit balances refunded,
 - balance sheets and / or profit and loss accounts that suggest the supplier would be at risk if e.g. commodity prices were to suddenly increase; or
 - an inability to refund customer credit balances if called upon.

We consider that this licence condition is in the interests of energy consumers. Our proposed licence condition should ensure that:

- There is limited scope for the extent and types of supplier failures in 2018 and 2019 to recur in future;
- End consumers, consequently, do not pick up the substantial mutualised costs associated with supplier failures;
- Suppliers will be less able to accrue large debts and exit the market without consequence;
- There is sustainable competition with the ability for genuinely innovative and well-designed commercial models to emerge.

However, we remain open to other proposals that may be able to reduce or prevent the mutualisation of costs when suppliers fail.

If you have any questions, please contact Tabish Khan in the first instance on 07789 575 665 or Tabish.khan@centrica.com.

Yours sincerely

Tim Dewhurst
Head of Regulatory Affairs
Centrica

Appendix: Consultation questions

Consultation question 1: Do you agree we should extend our enhanced 'fit and proper' assessment questions to all licence application types, not just supply licence applications?

Centrica supports the extension of the fit and proper assessment to all licence application types.

Consultation question 2: Do you agree that the proposed questions in section 12 will enable applicants for a gas or electricity supply licence to demonstrate that they meet the new supply licence application criteria?

We consider that Ofgem's decision to limit the requirement for applicants to provide evidence of their ability to fund their activities to only the first 12 months may be insufficient in identifying suppliers at risk of failure. Almost all recent supplier failures have been for companies that have been in operation for longer than 12 months and therefore extending the proof of funding to at least 24 months would be prudent.

Given the draft application form asks for two years worth of information for financial projections, funding arrangements and risk management strategy it would be consistent to also ask for two year's proof of funding arrangements.

Consultation question 3: Do you have any other comments on the proposed new regulations/application forms, including the updated tiered process or fees? Or, is there anything we have not included that you believe should be?

We have no further comments on the new regulations / application forms.

Consultation question 4: Do you have any comments or would you suggest any changes to the section on 'Suitability to hold a licence' (Chapter 3 of the draft guidance)?

We have no further comments on the 'suitability to hold a licence' section.

Consultation question 5: Do you have any comments or would you suggest any changes to Chapter 4 of the draft licence application guidance, relating to the new criteria and process for supply licence applications?

We have no further comments on chapter 4 of the draft licence application guidance.

Consultation question 6: Do you have any other comments or would you suggest any other changes to any part of the draft guidance?

Ofgem should review existing dormant supply licence holders and seek revocation of such licences where these have not been used for over 12 months. It is important that these are assessed in order to address the risk of parties being able to circumvent the new entry requirements by picking up an existing dormant licence.