

Lesley Nugent
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Ofgem
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E14 4PU

13 May 2019

Dear Lesley,

Consultation on new applications regulations and application guidance document

Thank you for the opportunity to respond to this consultation on proposed new applications regulations and application guidance document.

We are broadly supportive of the proposed amendments to the licence application regulations¹ and application guidance², which were first consulted on as part of the November 2018 Supplier Licensing Review consultation.³ We note that the proposed enhanced disclosure requirements in relation to suitability to hold a licence (“Fit and Proper Persons”) will apply to all licence classes not just supply, which we believe is sensible.

Our answers to the consultation questions are in Annex 1 to this letter. We would also make the following more general points.

The licence application reforms are part of Ofgem’s wider Supply Licensing Review which also covers ongoing monitoring, reporting and financial requirements and should ideally be introduced as a package. That said, we understand that given the nature of some of the reforms being contemplated to the ongoing licensing regime, they could not be developed in time to be implemented alongside the revised application process but will instead be subject to separate consultations later this year.

In our response to Ofgem’s November 2018 consultation, we supported the inclusion of collateral requirements as part of the supply licence application to minimise financial risk to consumers. We understand Ofgem’s decision not to include collateral requirements was made on the basis that Ofgem would instead apply greater scrutiny and monitoring of suppliers’ financial health. In this context we believe it is important that information from the licence application informs Ofgem’s ongoing regime. Specifically we recommend that suppliers who cannot commit to provide a material level of capital or equity nor have their debt covered by a major credit rating agency, should be categorised

¹ https://www.ofgem.gov.uk/system/files/docs/2019/04/appendix_2_-_draft_electricity_si.pdf

² https://www.ofgem.gov.uk/system/files/docs/2019/04/appendix_3_-_draft_application_guidance.pdf

³ https://www.ofgem.gov.uk/system/files/docs/2018/11/supplier_licensing_review_0.pdf

as high risk from the outset and be subject to greater scrutiny by Ofgem and enhanced reporting requirements. We would suggest that an additional section is added to the guidance document explaining the risk rating methodology, how this will be informed by the licence application and how it will impact the ongoing monitoring and reporting regime. Ofgem could make such amendments to the guidance document once it has reached final proposals on the ongoing regime later this year.

We believe it is essential that prospective new entrants are left in no doubt that if they do not provide any material capital or equity or equivalent guarantee, their business will be regarded as high risk and face greater scrutiny from the beginning. In the absence of such amendments we do not see how the last part of Ofgem's principle "Suppliers should adopt effective risk management, be adequately prepared and resourced for growth, and bear an appropriate share of their risk" is being taken into account at the entry stage.

Please do not hesitate to contact me or Haren Thillainathan (tel 0141 614 2007, email: hthillainathan@scottishpower.com) if you have any questions arising from our response.

Yours sincerely,



Richard Sweet
Head of Regulatory Policy

CONSULTATION ON NEW APPLICATIONS REGULATIONS AND APPLICATION GUIDANCE DOCUMENT – SCOTTISHPOWER RESPONSE

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?

Yes, we agree that the enhanced ‘fit and proper’ assessment questions should be extended to all licence application types. The questions are being enhanced to require, in addition to criminal convictions and directorship disqualifications, formal disclosures from licence applicants regarding:

- bankruptcy, insolvency, debt judgements; and
- involvement in compliance and enforcement action by Ofgem and other regulators or competition law infringements.

As we understand it, the above areas are already subject to checks by Ofgem at licence application, and the onus will now be put on licence applicants to disclose this information up front.

As such, we believe these enhanced disclosure requirements will benefit consumers by helping to screen out high risk management and operation of prospective licensees, noting that these disclosures will be extended beyond company directors to anyone with significant management responsibility or influence over the applicant. Whilst we believe the case for these changes is greatest for supply licence applicants given recent insolvencies, we think the proposed changes will also enhance the application process for other licence classes without being unduly onerous.

We support the proposal to extend the scope of persons required to provide fit and proper disclosures at licence application as discussed above. We would however be cautious about placing additional requirements on ‘persons with significant responsibility or influence’ over the applicant, to avoid giving rise to disproportionate “housekeeping” amendments when there is a change of personnel.

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?

Yes. We support the three new application criteria (which Ofgem consulted on as part of the November 2018 Supplier Licensing Review):

- 1) The applicant has the appropriate resources for its proposal to enter the market;
- 2) The applicant understands its regulatory obligations and has appropriate plans in place to meet these;
- 3) The applicant is fit and proper to hold a licence.

The additional questions in section 12 of the draft licence application seek additional information on:

- arrangements for the first two years of operation;

- financial projections, funding arrangements and risk management strategy for the first two years of operations (including proof of funding for the first year);
- statement of intent with regards to customer service licence obligations and approach to compliance.

We agree that these additional questions will enable applicants to better demonstrate their ability to meet the above criteria.

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?

No, at this stage we do not propose any amendments or additions to the licence application regulations or application forms.

With regards to the tiered application process, we think all applications would benefit from being subject to the full tier 2 information requirements including in person interviews with Ofgem. At present, Tier 2 of the process is reserved for applications that Ofgem judges to have important inconsistencies or omissions. We do not believe the combination of Tier 1 and 2 information requirements should prove onerous for licence applicants, and we believe it would help expose any potential risks from all applications. That said, we recognise that subjecting all applications to the combined tiered requirements may prove a constraint on Ofgem's resources. We therefore recommend Ofgem keeps the experience of future applications under review to assess whether it could process all applications on a combined tiered basis.

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 or proposed amendments to this chapter.

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 or proposed amendments to this chapter.

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

We believe the risk-based monitoring and reporting regime should be informed by the information gathered from the application process. Specifically, we recommend suppliers who cannot commit to provide a material level of capital or equity nor have their (or parent company's) debt covered by a major credit rating agency⁴, should be categorised as high risk from the outset and given greater scrutiny by Ofgem and subject to enhanced reporting requirements.

⁴ Eg Standard & Poors, Moodys, Fitch

We would recommend an additional section should be added to the guidance document setting out how Ofgem will assess financial resilience, including amongst other things:

- what constitutes adequate resources for market entry and growth;
- Ofgem's risk rating methodology;
- how Ofgem's assessment will be informed by the licence application;
- how Ofgem's assessment and risk rating will impact the licensee's ongoing monitoring and reporting requirements.

Ofgem could make such amendments to the guidance document once it has reached final proposals on the ongoing regime later this year.

We believe it is essential that prospective new entrants are left in no doubt that if they do not provide any material capital or equity or equivalent guarantee, their business will be regarded as high risk and face greater scrutiny from the beginning. In the absence of such amendments we do not see how Ofgem's principle, "suppliers should adopt effective risk management, be adequately prepared and resourced for growth, and bear an appropriate share of their risk" is being taken into account at the entry stage.

ScottishPower
May 2019