

Licensing Frameworks,  
Industry Codes and Licensing,  
Ofgem,  
10 South Colonnade,  
Canary Wharf,  
London,  
E14 4PU

06 July 2020

Dear Sir/Madam

**RE: Supplier Licensing Review: Ongoing requirements and exit arrangements**

Thank you for the detail of the consultation dated the 25 June 2020. We have responded to the specific sections below, however I thought it appropriate to lay out our general position in advance.

A fundamental change has occurred in the GB utility market in the last 6 years. The number of energy suppliers has more than doubled from 27 in 2014 to its current levels. The impacts of this on competition cannot and should not be underestimated. A consumer has never had more choice in terms of the supplier they purchase from, and the decision-making process behind this can be based on a multitude of factors.

This explosion in competition must be viewed as a positive from the consumers perspective, but industry systems and processes have not kept pace. Multiple elements are funded by the industry on a user pays basis, which means in the event of supplier failure, the relevant costs must be covered. The current mutualisation process is demonstrably unfair to prudent suppliers who have run their businesses with sufficient resources to remain operational.

Furthermore, the introduction of the Safety Net was well intentioned to protect customer balances that had built up as a result of the effects of seasonality on Fixed Direct Debit collection. In practice it has given rise to the practice of up-front consumer payments and reckless business models. In the event of a supplier failure the majority of consumers end up subsidising those consumers whose suppliers have exited the market and have obtained a saving. Perversely this means that those customers who are least able to engage with the market, end up paying for customers who have switched to the cheapest (loss-leading) deals.

A decade ago, suppliers billed customers in arrears, meaning that large customer credit balances were rare. Now suppliers billing in arrears are very much in the minority, meaning that most are collecting one- or two-months payments prior to providing any service and as such building up large credit balances which are used as working capital. Effectively suppliers have made their customers unsecured investors in their business.

While Ofgem makes it clear in each SOLR event that they aim to negotiate with the incoming supplier to cover the costs of credit balances, precedent shows that this is rarely successful. Usually

the industry has to make up a proportion of the bill. Not only is this a completely unforecastable cost it also has to be recovered from a suppliers existing customers.

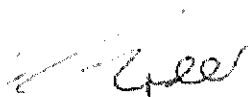
The issue is further exacerbated by the fact that suppliers are currently allowed to continue trading for too long after it is clear they are in trouble. Suppliers can make a financial loss for decades, but only fail when they run out of cash. The nature of billing in advance allows struggling suppliers to enter ever cheaper deals into switching sites, and use the cash gained (without providing a service) to continue to operate. We have often seen these offers becoming ever more desperate ,particularly in the time period before the RO bill becomes due.

We have held bilateral meetings with Ofgem on this subject, where it was clear that Ofgem did not feel it possessed the powers to stamp out reckless business practices. As a result, we wholeheartedly support the concept of Ofgem acquiring these powers. While we feel there are elements of the Supplier Licensing Review proposals which can be refined, and efficiencies made, we are keen that the principle of stress testing is maintained. We would then urge Ofgem to act pre-emptively to prevent mismanagement and reckless pricing practices.

A final point on this subject is inextricably linked to the Price Cap. As we have already outlined, the market has never been more competitive, notions to the contrary are in our view political in nature. While slamming the industry as too expensive may poll well, the reality is that energy is an essential service and those who operate in it need to make returns to survive long term. The domestic price cap allows the most efficient of suppliers to make less than 2% return on sales. I would urge Ofgem to look at the grocery, telecoms or pharmaceutical industries as examples of other essential services and justify how 2% is reasonable. Suppliers must have a 'war chest' to deal with events such as 'the beast from the east' or upward fluctuations in the wholesale price of energy or to handle requests to support the vulnerable as has happened with COVID-19. In fact, the cost of looking after the vulnerable falls disproportionately on the incumbent suppliers where they have legacy portfolios of the least engaged consumers. They must be allowed to make a return that matches the costs and credit required to service those most in need. While we all agree that suppliers should not be profiteering, or taking advantage of dis-engaged consumers, running their operations on a shoestring is not beneficial in the long term, is likely to adversely affect the vulnerable and increases the likelihood of further SOLR events.

If you would like to discuss anything within this response, please get in touch by emailing [chris.g@geuk.com](mailto:chris.g@geuk.com)

Kind Regards,



Chris Greer

## 1. Promoting better risk management

### Cost Mutualisation Protections

We are very supportive of Ofgem's efforts to reduce the risk of cost mutualisation, as already stated these costs are unforecastable and are therefore extremely hard to mitigate. We appreciate that we have already given a view to Ofgem on the proposal, but we are still strongly in the camp that does not believe the current proposal goes far enough. A requirement on suppliers to maintain 50% of customer credit balances and 50% of government policy costs is a good start, however this still leaves the market exposed to the remaining 50% of a failing suppliers costs.

We have operated as a supplier in the market for 19 years and have seen a lot of companies enter and exit the market in that period, being responsible for their business models is not a risk we envisaged even 5 years ago. While we understand that cash is a severe barrier to entry, we operate in a cash hungry industry and as such we do not believe it is unreasonable to expect a supplier to be adequately financed without utilising customer cash.

An exacerbating issue here is the industry's lack of profitability. In order to gain customers and seek economies of scale, most suppliers in the market have pricing structures that return net or even gross losses. We do not seek to pass judgement on the business models employed by other suppliers, however as we are now partially responsible for the failure of them, it would be perverse to ignore the inherent risk in these models. We would therefore urge Ofgem to consider a hybrid option whereby suppliers who make an annual retail profit are required to maintain 50% of customer credit balances and government policy costs, whereas those who make losses are defined as riskier and therefore must maintain a greater proportion.

We would like to see the policy also cover industry costs which fall outside of the definition of government policy costs. We believe that a significant proportion of the DUoS and TNUoS costs should also be maintained. While these are usually paid on a monthly basis DUoS costs continue to accrue after a SoLR event until transfer, and as such there is a shortfall. We assume that TNUoS costs are under routinely under forecast in failing suppliers and therefore action should be taken.

From an administration perspective we would be keen for some insight as to how Ofgem believe this will operate. If this is a principle-based regulation what enforcement will be taken if it transpires a failed supplier did not maintain adequate balances? While we would encourage strong enforcement, it should be noted that the exact values both in terms of customer credit balances and government policy costs are a moving feast and can change significantly on a day by day basis. The RO value will reconcile each day as we move through settlement runs and so it is not a simple process to ensure compliance.

Finally, we would be very keen for Ofgem to take a closer look at failing suppliers accounts, and take enforcement action against individuals where it is clear actions have knowingly been taken that have detrimental impacts upon the market. We have heard of one SoLR where the directors of a failing supplier paid other companies they owned considerable sums in the weeks prior to failure, safe in the knowledge that the market would have to pick up the bill.

### Operational Capacity Principle

While we are fully supportive of the notion that suppliers should be adequately resourced to service their customers, we do not believe this is a new policy. While the license conditions may not explicitly state that suppliers must be able to service their customers the principle certainly is.

### Milestone Assessments

The concept of milestone assessments is one that Green Energy would support. We believe there should be closer links between the retail community and the regulator, and rather than purely seeking information Ofgem should be trying to understand the businesses that they regulate to a greater extent. Therefore, if nothing more comes of the assessments than Ofgem speaking to suppliers about their business models and aspirations then this should still be viewed as a success.

That said, we believe that suppliers should be interrogated at certain points in their lifecycle and have no qualms with the thresholds that Ofgem has selected. We would prefer that a caveat was added so that an assessment was also conducted prior to any trade sale.

Much like our response to the cost mutualisation principle, we would suggest that discretion was used by Ofgem as to the depth to which these assessments should go. While we believe all suppliers crossing these thresholds should be able to demonstrate their capacity to serve their customers and their compliance mechanisms, we believe integration of business models should be reserved for those suppliers who do not make a profit. Serious questions need to be asked about viability in the absence of profit, and roadmaps towards it must be adhered to. We have let suppliers reach considerable scale in the absence of profit which we understand has been viewed as a necessary evil, but political and media considerations should not allow the regulator to put the market at risk. The scale of some suppliers with risky business models could start a domino effect in the event of a SOLR. Ofgem must work towards ensuring robust financials within the retail market.

#### 2. More governance and ongoing accountability

### Ongoing fit and proper requirement

We do not believe that this proposal will have any impact on the market. We would expect that suppliers should already have systems in place to avoid employing individuals into positions of responsibility if they are not fit or proper.

The main issue with this proposal is the notion that an employee is required to question their directors as to their credentials. The employee has a vested interest in ensuring that a director passes any such test.

If this proposal is to carry any weight, we would suggest that Ofgem carries out the assessments with the board of each licensed supplier on an annual basis.

### Principle to be open and cooperative with the regulator

We fully support the proposal, while we agree with some respondents from the initial consultation that there may be some duplication within the principle of existing license requirements, this should serve to reinforce its importance. We would therefore expect Ofgem to take swift enforcement action against any supplier who does not meet this principle.

### 3. Increased Market Oversight

#### Customer Supply Continuity Plans

The policy of continuity plans is one that we support, and we are pleased to see the updates to Ofgem's thinking since the last consultation.

The one further element we would encourage Ofgem to consider is third party IT providers. We are in little doubt that the majority of suppliers will offset a number of facets of this policy by directing any potential incoming SOLR supplier to systems run by a third-party IT provider. This information is unlikely to be made easily available to the incoming supplier, and as such diminishes the value of any continuity plan.

#### Independent Audits

We wholeheartedly support extending Ofgem's vires to enable them to enforce an independent audit. We would suggest that Ofgem should arrange suitable auditors which would mean there would be no differential between auditors in terms of quality, and proper understanding can be guaranteed.

We would also urge Ofgem to use these powers to enforce audits onto those suppliers who make financial losses, this would ensure both the supplier and Ofgem understand the root cause of this, and Ofgem can then make enquiries as to whether that supplier has the necessary backing to continue with their business model.

#### Monitoring and reporting requirements

We see no issue with Ofgem being informed of changes of ownership. We believe that Ofgem should be conducting the fit and proper requirement, and this would enable them to do so. Furthermore, changes in ownership and board composition have been a regular precursor to supplier failure.

### 4. Exit Arrangements

#### Customer interactions with administrators

While we sympathise with the situation customers pursued by administrators find themselves in, we do not believe that an update to suppliers T&Cs will solve the issue. Ofgem's license conditions do not cover administrators who have their own regulatory framework to act within. Our view would be that Ofgem should act pre-emptively to guard against supplier failure, which would remove the need for administrators to chase consumer debts.

We are pleased Ofgem are aware that the supply license gives customers more protections in relation to debt collection than is the norm in other industries. We would suggest that if suppliers

could chase debts in a more comparative fashion the level of debts chased by an administrator would likely be lower and more manageable for the customer.

#### Customer book sales

We support Ofgem's view that the regulator should be notified of any intention to complete a commercial transaction that will result in customer transfer.

#### SoLR commitments

We agree with Ofgem that commitments from suppliers to honour the SoLR bids they make must be viewed as a positive step. Bids can only be as accurate as the information provided, which precedent tells us is often sparse, particularly in the initial days after a SoLR announcement. We hope that the continuity plans proposal should go some way to rectifying this issue. An all reasonable steps commitment to honour the bid seems reasonable, as if the data a SoLR bid was based upon is significantly flawed this would fall outside of the commitment given.

#### Portfolio splitting

We are keen to see proposals come to fruition that would allow portfolio splitting. While the industry works towards making the Central Switching Service a reality, we would urge Ofgem to push these proposals forward to that they can be enacted at the same time.