



Vlada Petuchaite & James Proudfoot,
Senior Managers,
Industry Codes & Licensing Team,
Ofgem,
10 South Colonnade,
London,
E14 4PU

2nd December 2019

Dear Vlada & James,

Consultation on Ongoing requirements and exit arrangements

Thank you for the invitation to respond to the above consultation. Bristol Energy is a national gas and electricity supplier that is making a positive difference by building a sustainable energy company that has social value at its heart. Bristol Energy has delivered over £12m in social value, since launch, and is committed to working with city partners to help Bristol hit ambitious social and environmental goals as set out in the Council's One City Plan.

Executive Summary

Overall Bristol Energy is supportive of most of the proposals although a greater level of detail is required on some so that we can properly assess the impact on our business.

We are strongly opposed to Ofgem's proposals on cost mutualisation protection because it will cause significant financial detriment to both Bristol Energy and our shareholder Bristol City Council as it will add significantly to the already onerous burden of credit collateral required to participate in this market. We would welcome an opportunity to give a more detailed view of the impact in a one to one meeting with Ofgem.

We also believe that at the point of supplier failure the protections set out to cover the amount proposed will not actually materialise, thus this measure will not only serve to act as a burdensome cost on well run businesses but deter potential new entrants and business models from entering the market without the achieving the claimed benefit.

It is not clear in the consultation documentation how PCG's, Insurance or cash in escrow will be secured so that it exists if a party fails. For example, normally PCGs are lodged with a counterparty which prevents them being withdrawn. As there appears to be no counterparty, assuming Ofgem is not going to take on this role, then what prevents a parent company withdrawing a PCG, or reassigning it to cover energy trades prior to failure? Equally, Insurance may be cancelled by insurers for non-payment of insurance premium. and what prevents cash held in escrow being removed or reduced below 50%? It is also not clear to us currently how Ofgem will ensure, even if the protections exist when a supplier enters administration, that any administrator of the failed supplier will release any money set aside to cover credit balances and obligations alone rather than liquidating it for all the company's creditors.

We have looked at the possibility of acquiring insurance as mentioned in the Impact Assessment and have been unable to find a provider, despite being a prudent business, meeting all its obligations on time and backed by one of the best performing local authorities in the country. We believe the impact assessment is fundamentally flawed in its assumption that such a product is available at a cost of 0.5% of the sum insured as this is based on an indication from just one provider, who may not offer this rate or any rate across the market.



We are also concerned at the short time frame for implementation as we have already agreed our business plan and funding with our shareholder for 2020/21 which does not cover this significant extra financial requirement.

To this end we believe Ofgem needs to find an alternative solution, such as an industrywide insurance scheme available to all suppliers at fair and competitive rates. So that it does not damage the competitive market and allow the market to return to a cosy cartel of the incumbent suppliers, particularly given the challenges to meet net zero will require fresh thinking.

Ultimately, this particular proposal on cost mutualisation protection does not in our view meet Ofgem primary duty to protect existing and future customers, as it will reduce choice in the market and, once the price cap is removed, will lead to higher prices caused by reduced competition for the incumbent suppliers, which we believe is the main reason they are generally supportive of this proposal despite the financial consequences to themselves.

We have answered your specific the questions below, expanding our response where necessary.

Q1. Do you think the proposed package of reforms will help to reduce the likelihood of disorderly market exits, and the disruption caused to consumers and the wider market when suppliers fail? Are there other actions you consider we should take to help achieve these aims?

We believed that some of the proposals, combined with Ofgem's strengthening of due diligence at market entry will significantly reduce the likelihood of failure, but where failure does occur it will continue, in most cases, to be disorderly. Most suppliers fail because they hit issues with cash flow, the cost of operating in the market combined with the over burdensome credit collateral requirements means that cash is key to survival and it is unlikely that suppliers will enter into administration without exhausting all the cash at their disposal including that which they are required by licence to maintain separately if they are able to do so.

For the same reason we believe maintaining a robust 'living will' is unlikely to be a priority if a supplier is in trouble, and we therefore question if in reality it will prove to be a cost on well run businesses without delivering the benefit when it comes to be utilised on a supplier's exit from the market.

We are supportive of the measures proposed to ensure administrators must take into account ability to pay when chasing accounts in debt and measures that give Ofgem greater insight and opportunity to step in earlier when it detects problems.

With regards to further measures, we strongly urge Ofgem to continue its dialogue with the Government to change the payment structure of the RO so that suppliers cannot accumulate large debts which must be mutualised where a supplier fails. We would also urge Ofgem to look to see if there could be an industry-wide insurance scheme which suppliers contribute to cover all or at least the largest mutualisation risks.

Q2. Do you agree with the outputs of our impact assessment?

We do not agree with Ofgem's costing of mutualisation protections. For such a draconian financial proposal which will result in the industry increasing costs by tens of millions of pounds, costing it at 0.5% of sum insured based on one provider rather than a range of providers willing to insure suppliers of different shapes and sizes is insufficiently robust. We have considered seeking credit protection and have been unable to find a provider at any cost. Unless Ofgem is certain all financially sound, existing suppliers will be able to access such provisions at that price then it cannot be used to calculate the cost of this measure.

Q3. What further quantitative data can industry provide to inform the costs and benefits of the impact assessment, particularly for cost mutualisation protections?

We believe Ofgem needs to better understand independent suppliers' access to credit collateral, and how much suppliers already provide and at what cost. For example, where suppliers are borrowing money to place in escrow, what rate of interest are suppliers paying? It should also do more research on the cost of parent company guarantees as this is often more than Ofgem's suggestion of an administrative cost. Prudent parent companies will also set limits on their financial exposure to their subsidiaries in terms of guarantees, and it may be the withdrawal of, or refusal to extend PCGs that send a supplier into administration.

We also feel Ofgem needs to take a longer timeframe in its assessment. Prior to 2017 there had been several years with no supplier failures, and one has to believe that Ofgem's increased due diligence at market entry and ongoing monitoring this will be the case in future. We therefore challenge Ofgem's assumptions on the number of supplier failures a year. Some of the measures proposed will reduce the likelihood of failure and we firmly believe that in future most years will see no supplier fail as has been the case previously. However, the cost of measures, particularly cost mutualisation protections will be constant. So, in some years there will be costs without any benefit and this needs to be considered.

The IA also fails to consider the impact of a number of suppliers exiting the market, controlled and uncontrolled at the point cost mutualisation protection comes into force. If Ofgem does wish to proceed with this option, then it should model a slower process where the amount protected starts at a much lower level and increases over time which will allow suppliers to adjust their business plans.

Finally, we believe the IA should look at other industries, in particular, the guarantee that banks provide to protect customer balances up to £85,000 which we understand is risk based rather than a blanket approach as proposed for the energy market. Ofgem should seek quantitative data from the relevant financial regulators as to how that scheme operates. Ofgem may also want to look at the Civil Aviation Authority bond which protects customers from airline failures and the ABTA scheme for travel agents.

Q4. Do you agree with the assumptions used to calculate the costs and benefits in our impact assessment? Please provide evidence to support further refinement?

We do not agree with the indicative fee rate of 0.5% of the protected amount per annum. We have approached the market and found no insurer willing to offer such insurance to us at any rate, never mind 0.5% per annum. Ofgem quotes one provider as the source of this information but does not make clear whether that rate would be available to all financially sound suppliers. Proposing such a draconian financial burden on market participants on such slim evidence is not acceptable. To proceed with this policy measure we believe Ofgem must satisfy itself that credit protection insurance is "typically" available (taking into account the recent judgement against Ofgem over the price cap costs) to suppliers from several different insurers at a level similar to the above otherwise it risks forcing suppliers into being non-compliant, or worse the unmanaged exit of several market participants, many of whom are sound businesses operating in the current market.

Q5. Do you agree with our proposed option to cost mutualisation protections? Are there other measures of implementing this proposed option? Please provide an explanation and, if possible any evidence, to support your position.

We are strongly opposed to Ofgem's proposals on cost mutualisation protections. In our view the cost of these proposals over the long term will be greater than the cost of mutualisation as these costs will exist every year,



whereas over the longer term, especially with other measures Ofgem has proposed, most years will see no mutualisation of costs, or very little. It is worth noting that since 2006 to 2017, a period of over 10 years there was hardly any supplier failures, and we expect this to be the norm going forward once Ofgem's other reforms kick in.

As stated above, we believe Ofgem has vastly underestimated the costs of these proposals as we do not believe most suppliers will be able to get credit insurance at any cost never mind the 0.5% that Ofgem is using in its cost calculation, this leaves suppliers without a well-funded parent no choice but to place cash in escrow significantly impacting its cash flow funding and possibly leaving some currently sound businesses with no choice but to exit the market, much to the relief of the incumbent suppliers.

We are also concerned, that for many suppliers the only way to meet this measure will be to reduce the collateral they use to trade by buying power and gas on a shorter hedging strategy. This will actually increase the risk of supplier failure as suppliers are unable to buy ahead for one-year and two-year fixed term tariffs to lock in the costs and if costs rise, they will be supplying customers at a loss.

If Ofgem did want to have this level of protection, then it should look to the possibility of an industry wide scheme that all suppliers could access. Such a scheme could operate on a tiered basis so that a supplier with a significantly higher than average domestic credit balance was required to pay a premium on that excess. However, we still believe such a scheme, over the long term (i.e. 10 years) would be greater than the cost of mutualisation.

Q6. Do you agree with our proposal to introduce new milestone assessments for suppliers? Do you think the milestones we have proposed and the factors we intend to assess are the right ones? Are there additional factors we should consider to help us identify where suppliers' may be in financial difficulty?

We support Ofgem's proposals and milestones although feel an additional milestone at 1M customers should be added. We also believe there should be an assessment if a supplier intends a significant step increase in customer numbers either by a trade sale or SoLR, noting the recent failure of TOTO Energy following the acquisition of Solarplicity's customers shortly before their failure.

We support Ofgem's proposal that suppliers should be able to be assessed in good time before they reach the milestone, and as such believe there should be a grace period after implementation (assuming Ofgem's process for assessment is ready on implementation day), where any supplier crossing a threshold within the first six months is exempted, or at the very least not prevented from crossing the threshold whilst they are undergoing assessment.

Q7. Do you agree with our proposal to introduce an ongoing fit and proper requirement? Are there additional factors, other than the ones we have outlined, that you believe suppliers should assess in conducting checks?

It seems sensible to us that the requirement on market entry to be a fit and proper person continues to apply as an ongoing requirement. We would suggest that Ofgem ensures the wording captures not just direct employees but also individuals employed indirectly, for example as a contractor or on an interim basis through a 3rd party.

Q8. Do you agree with our proposal to require suppliers to produce living wills? What do you think we should include as minimum criteria for living will content?



Whilst it would clearly depend on the content of the living will, we are not convinced that at the point of failure any living will could be relied upon to be accurate and could in fact be detrimental by providing inaccurate information. As a supplier heads towards failure its priority will be to try and prevent failure by focusing resource to increase cash flow. Maintaining a living will is unlikely to be a priority in the months before failure and thus will be of limited worth for a SoLR or administrator of the failed business. In several cases it is poor record keeping that has contributed to the failure, so the actual records are inaccurate even if properly reflected in a living will.

This being the case, maintaining a living will is likely to be a cost on sound businesses, but when required provides very little benefit. Before implementing such a scheme, perhaps Ofgem should look to see if such a living will process for businesses that fail has been successfully utilised in any other industry to help an administrator wind down the business.

Q9. Do you agree with our proposed scope for independent audits? Please provide rationale to support your view.

We are not opposed to this measure, but believe it must be used sparingly, and that any requirement to perform an independent audit is precise in what it should be auditing and not a broad “fishing trip”. We think it would be appropriate that where Ofgem wishes an independent audit to take place it must make its case to an Ofgem enforcement panel as to why such a request is an appropriate measure.

We do support Ofgem’s view that the choice of independent auditor should be up to the supplier provided they are suitably qualified and not involved in the day to day running of the business.

Q10. Do you agree with the near-term steps we propose to take to improve consumers’ experience of supplier failures? Are there any other steps we should be taking?

We fully support the requirement to include reference to debt recovery licence requirements in customers terms and conditions to bind administrators to behave responsibly, although Ofgem should seek a legal opinion on whether a customer’s contract with a failed supplier can bind an administrator.

Longer term we believe Ofgem should look to see what it can do to make a trade sale more attractive to other market participants when a supplier is struggling rather than waiting to collect the customers through the SoLR process. One solution may be for Ofgem to share its SoLR contact list, subject to suppliers on the list consenting, with suppliers who would like to sell their business. That supplier could then contact the suppliers concerned to see if there is any interest in buying the business as an ongoing concern and thus avoiding SoLR. Whilst Ofgem would not be involved in these discussions it would retain the option to do an assessment if it was concerned by the potential transaction.

Q11. Do you think there is merit in taking forward further actions in relation to portfolio splitting or trade sales? What are your views of the benefits of these options? Are there any potential difficulties you can foresee?

We would support measures to improve the likelihood of failing suppliers going to a trade sale rather than SoLR, but this must be the sale of the businesses, not just the customers leaving the supplier to fail owing debt to the industry.

There may be merit in portfolio splitting. The easiest approach may be to split the portfolio by region thus



allowing more parties to come forward to take on the customers. The biggest hurdle is the speed at which customers need to be transferred and as such limited time to do the splitting and transfer. Ofgem should consider using its powers to request special administration status where an administrator believes it has a reasonable chance of an immediate sale of some or all the business negating the need to go down the SoLR route.

Q12. Do you think our draft supply licence conditions reflect policy intent?

We have not carried out this assessment, and therefore do not have an opinion.

I hope you find this response useful. If you have any queries, please do not hesitate to contact me.

Kind regards,

A handwritten signature in black ink that reads "Chris Welby".

Chris Welby
Head of Regulation