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### [ICoSS consultation response to Supplier Licensing Review: Ongoing requirements and exit arrangements](#)

The Industrial & Commercial Shippers & Suppliers (ICoSS) is the trade body representing the majority of the GB non-domestic energy market. Our members<sup>1</sup>, who are all independent Suppliers, in total supply in excess of three quarters of the gas and half the electricity provided in the highly competitive non-domestic market.

#### **Executive Summary**

- We agree with Ofgem that there is a need to address a number of weaknesses in the domestic market that significantly increases the likelihood of disorderly market exits with the industry covering the bad debt costs.
- The non-domestic market does not suffer from the same issues, with no costs being incurred through the exit of non-domestic suppliers. There is no need to introduce significant new controls in the non-domestic sector.
- Any new credit arrangements need to be aligned with Ofgem's best practice credit requirements.
- The costs of any disorderly exit should be targeted to the market sector in which they originate.
- Fit and Proper requirements will not achieve what is desired; instead Ofgem should seek to enforce existing provisions.
- Processes should be placed to allow portfolios to be split during an SoLR process to allow domestic only or non-domestic suppliers to participate in the bidding process.





## Response to Questions

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

The domestic energy retail market has experienced a rapid growth in the number of suppliers that currently operate in the market. Many of these new entrant suppliers had little or no operating capital, and no robust long-term operating plan. It was therefore inevitable that such organisations, reliant on initial direct debit payments from customers will exit the market in a disorderly fashion, leaving substantial debts for the market to address. We support Ofgem's proposals to address these issues in the domestic market.

By contrast the non-domestic retail market has not experienced the same uncontrolled expansion, with market entrants being in the main through trade sales (such as the purchase of Shell Gas Direct by DONG in 2011), or through controlled entry by asset backed organisations. Unlike the domestic market, there have been no disorderly exits by non-domestic suppliers that have resulted in bad debts being recovered from the rest of the market.

The consultation did not make it clear whether the credit proposals apply to simply the domestic sector, or all customers, though we note that the workshop on 26 November did indicate that it would for domestic customers only. We agree with this latter position. We do not see the case for there to be any substantial reform in the non-domestic sector; disorderly exits do not represent a significant issue. The proposals as currently written will simply result in significant additional cost in both credit requirements and operational burdens for no little benefit for the non-domestic market.

We note that the benefits from the expansion of domestic supply offering have primarily benefited the domestic market. Currently the costs of any disorderly exit are borne by all customers, even if they did not benefit from the increased competition that supplier brought. Cost recovery should be limited to the market sector originate from.

Currently these proposals do not distinguish between the market sectors. It seems appropriate that the domestic market should bear the costs of any costs from domestic supplier failures, and the non-domestic market likewise should bear the costs of any non-domestic failures. Though there has been some progress in doing so in the electricity and gas markets regarding the allocation to Last Resort Supply



Payments to the correct sector<sup>2</sup>, the costs of wider industry schemes are not addressed in this way. Ofgem should ensure that the costs of wider industry schemes can be targeted to the appropriate market sector to avoid cross-subsidies.

## **2. Do you agree with the outputs of our impact assessment?**

We do not agree. We welcome the assessment of the impact of SoLR costs on the industry, but there seems to be no assessment of the impact of covering government obligations in the impact assessment, or the impact on covering customer credit balances. As we set out below in question 3, the costs for doing so will be prohibitive and would have a material impact on assessing whether these proposals are ultimately beneficial to the market.

There is also no assessment on the cost to consumers on the additional paperwork that will need to be undertaken, which if all of these obligations are implemented will be considerable. There also needs to be separate assessments of the impact on the domestic and non-domestic sectors.

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

### **Gas**

We note that in the Impact Assessment there is very little information on the costs to the gas market regarding Supplier of Last Resort (SoLR) events. Though gas supply does not attract green levies such as the Renewables Obligation, the costs for refunding domestic customer credit balances in the gas market has been significant. Last Resort Supply Payment claims to date have comparable in gas to electricity as set out below:

<b>Claim</b>	<b>Gas</b>	<b>Electricity</b>
Together Energy (Retail) Limited <sup>3</sup>	£2.03m	£2.48m
Octopus Energy Limited <sup>4</sup>	£5.92m	£7.23m
Cooperative Energy Limited <sup>5</sup>	£6.3m	£7.72m

<sup>2</sup> DCP332 & DCP333 have reformed allocation of costs to customers from electricity Distribution Charges to allocate them to the correct market sector. UNC Mod 0687 seeks to the same in the gas market.

<sup>3</sup> <https://www.ofgem.gov.uk/publications-and-updates/decision-last-resort-supplier-payment-claim-together-energy-retail-limited>

<sup>4</sup> <https://www.ofgem.gov.uk/publications-and-updates/last-resort-supplier-payment-claim-octopus-energy-final-decision>

<sup>5</sup> <https://www.ofgem.gov.uk/publications-and-updates/last-resort-supplier-payment-claim-co-operative-energy-final-decision>



We believe that a full assessment should be undertaken for gas as well as electricity so that the impact for both markets can be fully assessed as many of our members do not operate in both markets.

#### *Credit Balance*

Ofgem should seek to use information on domestic credit balances that are currently held by domestic suppliers to assess the impact of any additional credit requirements based on covering 50% of credit balances.

In addition as stated above, the cost of covering government schemes should also be assessed as we believe them to be material. Using the 2019-2020 ROC buy-out price of £48.78/ROC, with the liability of 0.484ROC/MWh<sup>6</sup>, result in a cost of £23.61/MWh. Even covering 10% of this cost will be greater than multiple SoLR events and so this needs to be included in any assessment.

#### ***4. Do you agree with the assumptions used to calculate the costs and benefits in our impact assessment? If not, please provide evidence to support further refinement.***

The current cost calculations do not include the potential of covering government schemes, which will believe will be a significant cost if these proposals are taking forward. In addition the assumed third party of 0.5% does not correspond with the true cost of Letters of Credit for suppliers, with typical annual funding rates of 3-4% being more typical.

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

There are three key factors that need to be taken into account in developing any new regime to avoid cost mutualisation:

1. *The current proposals do not take into account the differing levels of risk that suppliers represent.*

Domestic suppliers have a track record of failing and leaving bad debt behind for the industry to cover. No non-domestic supplier has done so. We agree that in the domestic market there is an apparent need to ensure that domestic customers are not exposed to the costs from imprudent suppliers exiting the market, leaving substantial liabilities behind them. Such an issue does not exist in the non-domestic market and these additional requirements should be place upon the domestic market only.

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<sup>6</sup> <https://www.ofgem.gov.uk/publications-and-updates/renewables-obligation-ro-buy-out-price-and-mutualisation-ceilings-2019-20>



2. *This blanket obligation will penalise all organisations by imposing substantial operational costs on them for little benefit.*

As stated above, we do not see the need for any additional credit requirements in the non-domestic market, which will add significant costs to the market, even if Parent Company Guarantees are utilised.

3. *Credit Tools could add significant cost to the market.*

We note that Ofgem has recently stated in CMP311 discussions that its existing best practice credit cover guidelines<sup>7</sup> are still valid and these allow a wide range of credit tools to be utilised, including basing a level of unsecured credit on payments histories and use of Parent Company Guarantees. It would seem reasonable that the same principles are applied in this case. If not, then the market will incur significant costs in sourcing cash or letter of credit which would not be warranted.

When taken together, it is clear that the current proposals are disproportionate and that any proposals are confined to where they are needed, the domestic market, to minimise cost to consumers overall.

#### *Timescale for implementation*

Our comments above notwithstanding, the timescales proposed for deliveries are too short. With the standard notice period of any licence changes, 3-6 months after implementation is insufficient time to allow suppliers to put in place new credit processes based on dynamic cost assessment which this process would require. Realistically it will take 12 months from the new licence obligations becoming live for any new process to be put in place.

#### ***6. 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 to identify where suppliers' may be in financial difficulty?***

As we are a non-domestic trade body we do not have a view on the proposal for domestic suppliers to undertake milestone assessments as they grow. We do not think such assessments would be appropriate in the non-domestic market considering the widely varying size of customers and the difference regulatory landscape.

It is not explicit in the consultation that this proposal to assess suppliers in financial difficulties applies only to domestic suppliers. As stated above we consider the issue of disorderly exits from the market is applicable to domestic suppliers only.

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<sup>7</sup> <https://www.ofgem.gov.uk/publications-and-updates/best-practice-guidelines-gas-and-electricity-network-operator-credit-cover-conclusions-document>



We therefore do not see the need for any additional requirements for suppliers in financial difficulties to engage with Ofgem in the non-domestic market.

***7. 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?***

We do not agree. Current corporate legislation requires that directors are “fit and proper” and that unsuitable individuals can be banned<sup>8</sup>. The proposed additional criteria do not have the same force, and as currently drafted can be ignored by unscrupulous suppliers.

We are also concerned about placing restrictions on any individual who has worked for a company that has been subject to enforcement action or an SoLR event. It is not proportionate to penalise such individuals who may have been attempting to remedy any issues.

Focus should be enforcing existing regulations, rather than creating new ones.

***8. 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?***

We do not agree. We fail to see the benefit of this information as it is likely to be invalidated prior to the collapse of any supplier. We understand that Ofgem engages with “at-risk” suppliers to obtain information in anticipation of any event and formalising this process seems more proportionate than imposing a blanket requirement on all suppliers, which simply adds cost.

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

We agree that Ofgem should have the power to undertake financial audits when identified, but this must be only undertaken when a supplier is seen as representing a high risk to the market.

***10. Do you agree with the near terms steps we propose to take to improve consumers’ experience of supplier failures? Are there other steps you think we should be taking?***

These proposals only apply to the domestic market and so we have no views on them.

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<sup>8</sup> <https://www.gov.uk/guidance/money-laundering-regulations-apply-for-the-fit-and-proper-test>



**11. 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 steps? Are there any potential difficulties you can foresee?**

We believe that a process to allow domestic and non-domestic customers to be assigned to separate organisations in a SoLR event should be created. The current process restricts the ability for suppliers who are active in only one market from engaging in the SoLR process. This limits the potential number of bidders and so increases the costs for the market through socialised costs. We do not believe that the process changes to allow portfolio splitting will be excessive.

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

We have not fully reviewed the legal text, though we note that the drafting does not provide a comprehensive set of legal drafting so the full impact is difficult to assess.

Should you wish to discuss any aspect of this response please get in touch

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