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2 December 2019

Dear Sir/Madam,

### **Ofgem Supplier Licensing Review: Ongoing requirements and exit arrangements**

I write in response to the consultation on the Supplier Licensing Review regarding ongoing requirements and exit arrangements. We would like to thank you for the opportunity to comment.

Our response is structured as follows:

- our recommendations to help Ofgem and the sector meet the policy intent behind the proposed package;
- a summary of our response, and, in particular, our view that the best way to reduce the consumer detriment of market exit is early identification of failing suppliers;
- general comments on Ofgem's proposed package of measures; and
- answers to the specific questions set by Ofgem.

### **Recommendations**

To help meet the policy intent behind the proposed packages of changes we put forward the following recommendations:

- prevention is better than cure and it should be possible – through key stakeholders in the sector working collaboratively to share data and insight – to identify more quickly energy suppliers that are likely to exit the market;
- this package, as well as the market entry package, should be developed and implemented with consumers at the heart of it, so that it is fair by design; and
- the true cost of supplier failure goes beyond outstanding consumer credit balances and Government Scheme costs: these should be looked at holistically so that the impact on consumers can be reduced.

### **Summary of our response**

In our response, we have provided general comments around how we support the proposed package of changes in principle and how we think the package can be developed to ensure that consumer protection is at the heart of the design of the package. We also focus on how the package can be fair to suppliers, by allowing well-prepared suppliers to run effective businesses while targeting ineffective or failing businesses. We then answer the specific questions set out in the consultation paper where we can add most value. We have also included at Appendix A background information about Ombudsman Services.



We fully understand that this work, coupled with the previous work Ofgem has undertaken on entry requirements and the on-going work between the Department of Business, Energy and Industrial Strategy (BEIS) and Ofgem on the Future Energy Retail Market Review, means that there are a lot of moving parts here and there is no simple answer or silver bullet. We very much want to play our part in helping to put in place a package of reforms that achieves the policy intent here. We do think that because of the number and depth of proposals in the package, and the necessary balancing of market competition and consumer protection, that it will be important to review the effects of the package once implemented.

Like Ofgem, we agree that prevention is better than cure and that early identification of suppliers struggling financially is key. This would provide the opportunity for suppliers in that situation to stabilise, as well as ensure that any exit arrangements for suppliers minimise consumer detriment and the impact on other suppliers – and therefore other consumers – in the market. With this in mind, we would encourage Ofgem to consider how organisations across the industry could come together to discuss how we can identify measures that would indicate, sooner, companies that are struggling to sustain their businesses. This would necessarily need to be a cross-industry initiative involving suppliers as well as consumer organisations; as the Energy Ombudsman we have been able to build a picture of what happens to consumer redress when suppliers begin to enter difficulties; similarly, Citizens Advice and the Extra Help Unit will have their own indicators. We think this work would help Ofgem to understand how it might be possible to identify, and protect against, consumer detriment before suppliers fail. We would welcome the opportunity to be part of such an initiative.

#### **General comments:**

We welcome the fact that Ofgem is reviewing the ongoing requirements and exit arrangements of suppliers in the market. We responded to the earlier Ofgem consultation on market entry requirements on energy suppliers, which also discussed many of the measures proposed in the current consultation. Over the past 18 months, the energy market has experienced an unprecedented number of exits by suppliers who have been unable to remain in the market. While we agree that supplier failure is to be expected from a competitive market, this needs to be balanced with the harm that consumers face with this disruption to an essential service. Consumers need to be protected, especially consumers in vulnerable circumstances, and the effect of cost mutualisation on the wider sector needs to be managed and reduced as far as possible – ultimately consumers end up paying for these costs.

In principle we support the package of measures being suggested by Ofgem and think that, as a package, it will help improve due diligence, the on-going monitoring and compliance required to help build a sector that is focused on the ethos that prevention is better than cure, and to build a regulatory system that is fair to consumers and suppliers.

We took part in the Ofgem Supplier Licensing Review Workshop on 26 November and we also held a Supplier of Last Resort (SoLR) Workshop on 11 September, to look at what kind of data is required for an appointed SoLR to best manage taking on consumers from a failed supplier in a way that reduces consumer detriment. The Workshop included many suppliers, Citizens Advice and Ofgem.

We set out below some general comments on what we consider to be the key themes of Ofgem's consultation.

#### *Cost mutualisation:*

We appreciate why the consultation document, when it comes to looking at reducing the impact of cost mutualisation on the sector, focuses on consumer credit balances and Government Scheme costs. And we do agree that it is not sustainable that other suppliers (and their customers) pick up the costs of supplier failure. So, the option of suppliers putting in place protections around certain payments seems sensible. We think the focus should be around what needs to be protected and to what degree.

However, we do think it is important to look at what the full costs of supplier failure is and how that is being mutualised. Without understanding this, the true impact on consumer protection, in terms of being appropriately funded to reduce consumer detriment, in situations of supplier failure is unknown. Also, the reality is that the full mutualisation costs paid by suppliers is more extensive than that of consumer credit balances and Government Schemes.

From our experience of operating the Energy Ombudsman, for example, we have seen considerable consumer detriment where consumers have not been able to benefit from the remedies they may have been awarded via an Ombudsman decision as there is no obligation on an appointed SoLR to implement any remedy aimed at the supplier that has failed. We would therefore encourage Ofgem to consider a more rounded view of consumer detriment associated with supplier failure.

#### Continuous review:

We do understand that a draft impact assessment has been produced to accompany the proposals outlined, and it will be important to update that impact assessment following this consultation exercise as appropriate. We think that this package, along with the other links and dependencies outline in the consultation paper, involve numerous important changes and that it will be essential to review how this does work in practice. We think it will be essential to involve key stakeholders in that review and we would welcome the opportunity to take part.

#### How the proposals are implemented:

As the consultation paper highlights, it will be important that the monitoring and compliance around the new proposals is proportionate so that the most important areas of risk are addressed and consumer detriment reduced, but also that inappropriate burdens are not placed on suppliers. We think that by the sector working together this can be achieved, for example, via the Tripartite working between Ofgem, Citizens Advice, including the Extra Help Unit and the Energy Ombudsman and also through industry group meetings more widely.

#### Prevention is better than cure:

As highlighted above, we agree with Ofgem that prevention is better than cure. We think that there is an opportunity to use industry data to help tackle and spot the early signs of supplier difficulty and ensure better outcomes in such scenarios for consumers and the sector more widely.

There is existing data sharing through the Tripartite working between Ofgem, Citizens Advice, including the Extra Help Unit and the Energy Ombudsman. We think this Tripartite working can be built upon and more joined up policy thinking could be useful here. There is also scope, as we highlighted earlier, for wider industry groups to come together. For example, the SoLR Workshop that we facilitated this year discussed these challenges in detail. This collaboration could be replicated to cover other proposals in the package, and we would welcome the opportunity to be part of this.

#### **Answers to the specific questions raised:**

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

In principle we agree with the proposed package of reforms. It is important that they are looked at as a whole and alongside the new entry requirements on suppliers.

We do think that consumer protection should be at the heart of the reforms and that they should ensure that consumer protection is adequately funded to provide consumers with fair outcomes in what can be distressing and confusing circumstances when a supplier fails and a SoLR is appointed. We do know that there is consumer detriment, wider than the issue of credit balances, that needs to be protected and addressed, for example, the non-implementation of remedies from an Ombudsman decision, some debt collection practices related specifically to supplier failures, and aggressive selling activities that may amount to mis-selling. These activities, as well as causing general consumer detriment will have a proportionately higher impact on consumers in vulnerable circumstances.

We also think that there could be a more dynamic and flexible approach taken to monitoring and enforcement. Enforcement can appear to involve a very high threshold bar to be reached before action can be taken, or it can focus on a very specific area. The result can be that if enforcement action is not taken then things get even worse

within a supplier that is failing. Or the supplier focuses on the bit that is being enforced, for example, dealing with a Government Scheme payment but does so at the expense of other consumer protections, such as Energy Ombudsman remedy implementation. We wonder if there are other lower level enforcement options available, such as warnings? This would allow a more flexible and dynamic approach to enforcement being taken. It could even involve warnings being published.

We do think that the link and work with administrators when a supplier fails is important. We appreciate that Ofgem is setting out expectations around the approach of administrators, however, we wonder if there needs to be further work done with the Insolvency Service and the various regulators for administrators to look at any necessary changes to the Insolvency legislation. For example, a bigger focus on consumer protection, banning aggressive debt collection practices, ring fencing of monies that are essential to deliver holistic consumer protection (wider than consumer credit balances as outlined in our response), and working with appointed SoLRs (there may be the situation in the future where a number of suppliers are appointed as SoLR for a supplier that has failed) in a partnership approach.

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

In terms of looking at the true cost of mutualisation for suppliers as a result of supplier failure we can provide information around the costs suppliers, from 2020, will be required to mutualise for unpaid case fees to the Energy Ombudsman. We have been engaged with Ofgem, suppliers and other stakeholders on the approach we are taking here. For 2018 the cost of supplier failure to the Energy Ombudsman was £1.3 million and as of Autumn 2019 it was £1.6 million for 2019. From 2020 we will require suppliers to mutualise the cost of supplier failure to the Energy Ombudsman for the costs for 2019.

We appreciate that mutualisation in this way is far from an ideal situation, especially since 2017 we have, by finding efficiencies, been able to pass savings back to suppliers of around 16.5%. However, we are being proactive in trying to tackle this situation and reduce mutualisation where we can, for example, we will:

- require the setting up of direct debits for monthly case fee payments;
- publish the name of any supplier with bad debt outstanding for more than 120 days; and
- commence winding up action against any supplier with significant (more than £10,000) debts that are more than six months old.

Despite this action, we do think that it is sensible to add these mutualisation costs to the impact assessment, as suppliers are meeting these costs. We also propose that mutualisation protections might be appropriate in this area, in the same way that it is proposed they do to consumer credit balances and some Government Schemes.

**Question 5: Do you agree with the 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?**

We support the proposals around cost mutualisation protections. We noted at the Ofgem Workshop on 26 November that stakeholders had differing views as to the level of protection for customer credit balances. An attractive option that was raised was, to allow suppliers time to plan for this the approach could be one of phasing, so the start is 25% protection, then 50%, then 75% possibly leading to 100% protection and that this phasing could be over a two-year period.

This would meet the ambition of 100% protection but enable suppliers to put in place the appropriate arrangements to meet this. It may well be harder for some suppliers than others to provide protections, whether as deposits or part of an insurance product.

We do wonder if a percentage figure should be put against Government schemes and clarity around what Government schemes are included. We also support the idea of the option of Government Scheme payments being more regular than yearly or longer, for example, quarterly might help provide more protections. Though we do appreciate that this decision lies with the Government and BEIS.

Again, as we have highlighted already in our response, we think that the true costs of mutualisation need to be factored in here so that consumer protection is properly funded and the true impact on suppliers in terms of protections is known.

**Question 6: Do you agree with our proposal to introduce new milestones assessments for suppliers? Do you think the milestones we have proposed and the factors we intend to assess are the right ones? Are there any additional factors we should consider, to help us identify where suppliers' may be in financial difficulty?**

Yes. We think that milestone assessments are sensible. We also agree with the milestone factors. However, we think that there will be other factors that can be looked at in terms of suppliers being in financial difficulty. For example, things like a spike in consumer complaints, or consumer complaints types change and there is an increase in certain complaints such as payments and debt or transfers. We have done modelling around the changes in complaints types that suppliers receive as they have gone into administration. We are happy to share this with Ofgem again to help here.

We also think that factors such as poor signposting by suppliers is also another indicator that a supplier may be failing. By signposting we mean where suppliers explain to consumers who have made a complaint that 8 weeks has passed and their complaint hasn't been resolved or the consumer and supplier have reached deadlock on the consumers complaint and that the consumer can now take their complaint to the Energy Ombudsman. We think this is relevant because it can show that a supplier is facing financial difficulty because they do not want to signpost to the Energy Ombudsman as they may lead to a decision providing the consumer with a remedy, including financial remedy and there is a case fee cost to the supplier. There is a secondary point as to why signposting might be a key factor in that if the Energy ombudsman receives a reduced number of complaints because of poor signposting then the potential data and insight from those complaints is lost. This can affect our ability to provide appropriate insight to the wider sector including Ofgem but also may affect Citizens Advice Energy Suppliers Performance Rating Tool.

As outlined in the consultation paper the implementation of the proposals should be about proportionality and we agree with that. For example, it may well be the case that suppliers fluctuate in and out of milestone in terms of customer numbers so a practical solution will be needed here. Also, it will be important to guard against unintended consequences, for example, milestones becoming too demanding that a supplier may well actively seek against falling into a new milestone category because of more onerous checks and balances.

We do like the suggested approach around dynamic assessment. This fits well with our suggestion that monitoring and compliance might benefit from having more options to provide a more dynamic and flexible approach. Other factors that could indicate a supplier is in financial difficulty is missing payments to third parties and this can include not paying case fees to the Energy Ombudsman.

**Question 7: Do you agree with our proposal to introduce an ongoing fit and proper requirement? Are there any additional factors, other than the ones we have outlined, that you believe suppliers should assess in conducting checks?**

Yes. We think this is a sensible measure and fits well with the wider package of proposals, for example, the principle of being open and transparent with the regulator. Whilst, we think these elements must be implied within the current licensing and regulatory framework it is an opportune time to firm these parts up and have the open discussion with the sector.

The suggested factors outlined in the consultation document around looking at whether an individual is fit and proper seem sensible. We assume that as well as suppliers self-reporting their checks on fit and proper persons for key individuals within their organisations that Ofgem will be monitoring this with at least sample checks or looking at key people newly appointed within a company of a closer look at companies coming into the sector.

**Question 8: Do you agree with our proposal to require suppliers to produce living wills? What do you think we should include as a minimum criteria for living will content?**

We think that this option, as part of the wider proposed package, is a good idea. We agree with other stakeholders that if this proposal was a stand-alone proposal then it may be questionable as to how effective it would be in practice. We do think that there is merit in suppliers outlining what should happen if the supplier goes into liquidation.

For example, key staff contact points, access to relevant data sets, third parties involved and financial arrangements to meet some of the other proposals in this package, for example, if there is a requirement on suppliers to cover a percentage of credit balances and Government Schemes or other protected costs.

We think, as well as the points highlighted in the consultation paper, if it might be helpful for suppliers to identify in their living will what monies should be protected in order to reduce consumer detriment, for example, if they do have consumer complaints and those complaints are being considered by the Energy Ombudsman – is there a way to protect financial remedies or case fees?

If living wills are introduced, and the consultation paper makes clear they will be written when suppliers are in a stable position, it may be sensible for suppliers to update their living will within a certain time period, for example, every two years or if the supplier's business model/customer base changes significantly. Again, as with many of the proposals within this package effectiveness comes down to how this is monitored by Ofgem.

We do think that living wills should be kept as simple as possible and that they should focus on the key areas. In terms of publication, so that consumers and other stakeholders are aware of what is included, we think this needs to be handled carefully. Whilst we would support transparency, there are several factors to consider, for example:

- there may be commercially sensitive information;
- suppliers, like most other companies, do not enter the market with the idea that they will fail, therefore what they put in a living will may not reflect what is the reality or what is possible;
- there would need to be some context behind anything made public so that consumers and others have a fuller picture and that all suppliers are producing a living will; and
- what is in a living will may provide consumers with more comfort than what is likely to happen in reality. If this is the case, then this could lead to reduced consumer trust and confidence in the energy sector rather than the desired improved trust and confidence.

One option would be to promote the fact that all suppliers are working with Ofgem to produce plans to help reduce consumer detriment if any supplier fails in the future.

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

Yes. Independent audits would be a good addition to the regulatory toolkit for Ofgem. We do agree that this option should be used in a proportionate manner and be there to target very specific risks as identified in the consultation paper.

**Question 10: Do you agree with the near term steps we propose to take to improve consumers' experience of supplier failures? Are there any other steps you think we should be taking?**

We think what is proposed in the consultation paper is a good start. However, we do think that the more interaction and discussion there is between Ofgem, the Insolvency Service and the other insolvency practitioner regulatory bodies the better. If possible, to reduce consumer detriment, it would be beneficial to have the requirements expected of suppliers to be the requirements expected of administrators when they are appointed to oversee a failed supplier. There are the obvious areas of protecting monies, and acting appropriately where there is a debt, however, again we think there is a role around reducing consumer detriment more holistically, for example, ensuring there is appropriate cover to have any remedies in decisions from the Energy Ombudsman implemented.

**Question 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 see?**

We think that it is worth exploring the option of portfolio splitting as outlined in the consultation paper. If it is a possible option, this could help benefit consumers and make the SoLR process more open and competitive to a wider range of suppliers.

Regarding trade sales, we have been working with Ofgem around potential guidance on this point. We agree with what is outlined in the consultation paper that a proportionate approach should be taken and the basis being to prevent further consumer risk or harm. The specific points we would make at this stage are that:

- both suppliers engaged in a trade sale will work with third parties, such as Ofgem, Citizens Advice including the Extra Help Unit and the Energy Ombudsman; and
- the acquiring supplier should honour remedies (financial and corrective action) for any in-flight complaints within the Energy Ombudsman's process which had been made against the supplier who is being bought out.

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

Broadly they do. The draft supply licence will need to reflect and changes that Ofgem may make following this consultation exercise.

The main points we are making is that:

- the true costs of suppliers failing news to be looked at. By doing this, key elements, such as consumer protection can be looked at holistically and properly funded to protect consumers fully;
- the true cost of supplier failure is also required to put in place a system or package of measures that is fair and workable to suppliers and ensure that suppliers are not burdened with heavy mutualisation costs and that individual suppliers have the appropriate checks, balances and protections in place; and
- prevention is better than cure and the use of data and insights from stakeholders should be used proactively to identify as early as possible where a supplier may be entering financial difficulty. We also think it is important that this package of proposals is reviewed in terms of how it works in practice – again, it will be important that stakeholders share their data and insights on that.

Please do not hesitate to contact us if you would like further information regarding our response. Our response is not confidential.

Your sincerely,

A handwritten signature in blue ink, appearing to read 'M. Vickers', with a long horizontal flourish extending to the right.

Matthew Vickers  
Chief Executive and Chief Ombudsman

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## **Appendix A**

### **About Ombudsman Services:**

Ombudsman Services is a not-for-profit private limited company established in 2002 which runs a range of discrete national ombudsman schemes across different sectors including energy, communications and an appeals service in private parking. Each scheme is funded by the companies under our jurisdiction and our service is free to consumers. In 2018 we received 174,855 initial contacts from complainants and resolved 68,063 complaints. In the energy sector we received 108,349 initial contacts and resolved 45,667 cases, and in the communications sector, we received 62,233 initial contacts and resolved 21,251 cases. We also received over 67,000 appeals in our private parking appeals service.

We are:

- to our consumers, the people they can turn to for impartial advice and solution that's fair;
- to our partners, the people they look to for knowledgeable and insightful ways to help them reduce complaints by enabling them to make the changes they need to deliver better customer services;
- to our regulators, champions in protecting rights as well as partners in information sharing, we share our analysis so that regulators and business partners can make improvements; and
- to our people, here to enable them to deliver clarity to consumers and partners through meaningful work.