CORNWALL INSIGHT

CREATING CLARITY

Ofgem's statutory consultation on removal of the BAT

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1. Assessment and recommendation

On 14 May, Ofgem published a *statutory consultation on its proposal to remove the ban on acquisition-only tariffs* (BAT). The consultation explores whether the BAT should be removed from 1 October 2024, i.e., six months following its extension, or if it should be removed from 31 March 2025 to allow the existing extension to expire after 12 months. The regulator's preferred approach is for removal from 1 October 2024. The market-wide derogation for fixed retention tariffs would also be removed.

We recommend that domestic suppliers respond to this consultation, to ensure Ofgem has fully considered the impact on the supplier pricing and subsequent tariff availability. Responses are requested by 11 June.

Cornwall Insight comment: The removal of the BAT will provide a positive step back toward greater competition in the market, and more room for innovative offers from suppliers to consumers. Having served its purpose, the timing of the BAT's departure should now work to align with supplier hedging for the upcoming cap period.

2. Background

The BAT, alongside the Market Stabilisation Charge (MSC), was first introduced in April 2022 as a temporary intervention to improve stability during a time of extremely high wholesale prices in the market. Since then, it has acted as a mechanism to reduce the incentive for suppliers to make aggressively low-priced offerings in what was a volatile environment.

The MSC was allowed to expire on 31 March 2024 after previous extensions, as Ofgem recognised it was no longer needed with market conditions improving. It also noted the potentially adverse effect it was then having on competition in the market. At the time of consulting on its removal, the regulator flagged its intention to maintain the BAT while the MSC was removed, as it had concerns that removing both mechanisms at the same time would introduce risk back into market stability. It also considered it necessary to identify the impacts of the BAT on a standalone basis, thus enabled the BAT to continue.

However, Ofgem still considers the removal of the BAT to be appropriate, as it has fulfilled its initial purpose from being introduced and would not be capable of maintaining market-wide stability on its own. The modelling discussed below explores the effects of keeping or removing the BAT. It is worth noting that the concept of an enduring BAT was discussed in Ofgem's paper on the *future of price protection*, issued in March 2024. This consultation however focuses on the short-term necessity of the BAT as it is, regardless of whether it may be reintroduced as a form of price protection in the future.

3. Proposals

This consultation looks at two potential options:

- Removing the BAT from **1 October 2024 –** this would mean a removal after six months of the extension and is currently Ofgem's preferred option
- Removing the BAT from **31 March 2025 –** this would mean the BAT extension continues to its full 12-month length

In coming to a preference for the first option, Ofgem modelled various reasonable scenarios of likely consumer and supplier behaviour with and without the BAT. Each scenario includes a set of coordinated assumptions about hedging volumes and about whether suppliers do or do not offer fixed term contracts and acquisition tariffs to new customers. Ofgem categorised the market into three groups based on size, then modelled the following:

- Expected levels of switching between suppliers, with and without the BAT;

- Implication for prices paid by consumers; and
- Implication for the financial position of suppliers, where they have to unwind hedges

On financial stability, Ofgem's analysis suggested that removing the BAT would largely benefit consumers through lower prices, greater competition and likely improved quality of service. It argued that the benefits to consumers from removing the BAT outweigh the associated supplier losses as a result of consumer switches. It also found that removing the BAT will not have a material impact on the risk of supplier failure. Having not seen evidence that the removal of the MSC has resulted in disproportionately risky discounting behaviour from suppliers, it does not anticipate the removal of the BAT to do so either.

It does take note of the importance of timing in this decision with the difference in shortening the extension to six months rather than 12. Removal of the BAT after 12 months would give suppliers more time to factor its absence into hedging and pricing strategies, which could in turn lead to a market with better prepared suppliers. Conversely, while a removal of the BAT after six months gives suppliers less lead time to implement these hedging decisions, the timing aligns well with the upcoming hedging window for the October 2024 price cap period. It therefore considers the timeline of a six-month extension instead of the full 12 would be sufficient for suppliers to make decisions for October.

Some additional considerations from Ofgem include the potential incentivisation of a 'sugar-rush' market, where removing the BAT could encourage consumers to take a shorter-term approach to their energy supply, prioritising lower costs and regular switching above factors like service quality. Other responses argued that removing the BAT may limit suppliers' ability and incentives to offer the cheapest possible deal to loyal customers. This is on the basis that acquisition-only tariffs are more likely to be cheaper if they are to be competitive, and these by definition exclude and therefore penalise loyal customers who can only be offered inferior retention deals. In response to these points however, Ofgem argued that the financial resilience rules that have been put in place for suppliers should push to mitigate these risks.

In conclusion, Ofgem is minded-to remove the BAT after six months of the extension have passed, with no compelling reason to retain it beyond this point and to allow what it considers as the net benefits of its removal to be realised sooner.

4. Next steps

It is anticipated that, after the consultation closes on 11 June, the feedback will be reviewed and the decision will be published by the end of July, with the SLC changes going live from October 2024, should the consultation conclude that is the appropriate course of action.

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