



CORNWALL INSIGHT

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Ofgem consults on improving innovation in the retail market

Headline assessment	
Document:	Ofgem's consultation
Consultation dates:	02/10/24 – 27/11/24
Impact classification:	Medium: Domestic Suppliers, Non-Domestic Suppliers, Consumers
Action if desired:	Respond to the consultation

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Alex Jephson

Author



Alex Jephson

Analyst

a.jephson@cornwall-insight.com

For more information about us and our services contact us on enquiries@cornwall-insight.com or contact us on 01603 604400.

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1 Assessment and recommendation

On 2 October, Ofgem opened a [consultation on improving innovation within the retail energy market](#), seeking views on how it can remove barriers to innovations in the domestic and non-domestic markets that can best meet consumers' needs and enable the journey to net zero. It is specifically looking at how it can improve the route to market for innovative supply, setting out five potential areas for reform:

- The derogations regime
- Restricted licences
- Individually modified licences
- Licence Lite
- Licence exempt supply

The consultation closes on 27 November. We recommend that suppliers and other interested parties such as potential entrants respond to the consultation.

Cornwall Insight comment: This consultation is specifically focusing on how Ofgem can improve the less-traditional routes to market, to make it easier for parties to enter the market. It is hoping this will drive innovation within the market, particularly around low carbon technologies and smart tariffs, thereby enabling net zero, increased consumer engagement and greater flexibility.

2 Background

Since the retail energy market was opened to competition in the 1990s, there has been an emergence of innovative offerings, such as 100% renewable contracts and bundled tariffs. However, the energy crisis has reduced investment appetite and availability of new innovative products and services, with most domestic customers remaining on default tariffs (in June 2024, 81% of domestic accounts were on standard variable tariffs). Increasing diversity of tariff options in the domestic market is considered elsewhere by Ofgem, with its [ongoing work around standing charges](#). Ofgem also considers there to be limited tariff choice within the non-domestic market.

Despite this, there is evidence of increasing demand for innovation, with a growing number of domestic Electric Vehicle (EV) tariffs, and suppliers increasingly offering installations of low-carbon technologies such as heat pumps and solar panels to their customers. Ofgem noted it is also seeing licence exempt suppliers develop new, innovative products and services, but that there is varying levels of uptake among the less traditional routes to market, with stakeholders highlighting the limited routes as a barrier to new products and services.

3 Innovation in the retail market

3.1 Enablers and barriers to innovation

There are currently three broad categories of innovative products and services available or being trialled. These are:

- New types of energy supply – tailored or specialist energy supply such as local tariffs designed for customers living close to renewable generation, or energy as a service.
- Advisory services – insight and intelligence to help consumers make more informed decisions on energy products and services, such as smart price comparison websites or customer advice services.
- Energy management services – services that reduce or optimise consumers' energy consumption, generator or storage, such as demand side response (DSR) or behind-the-meter asset installation and management.

Ofgem is asking stakeholders what the scale of innovation is within the domestic and non-domestic markets, and what should happen to meet consumers' needs and net zero. It is also questioning the impact of new innovative products and services on consumers, and how Ofgem can maximise the benefits while minimising the risk. It is also welcoming evidence of consumer uptake around innovative products and services, and considering what it can do to help facilitate innovation in the market.

The regulator is also asking stakeholders what the most significant barrier to innovation is and what innovation is not happening as a result of regulatory barriers.

3.2 Routes to market

Ofgem wants to improve the routes to market beyond standard licenced supply, setting out potential options for improving them and the safeguards it would introduce to protect consumers. It considers that amending the routes to market could help new market entrants, or existing suppliers, with bringing innovative propositions into the market quicker and easier, thereby providing benefits for consumers.

The consultation sets out potential options for changing five routes to market, to improve their accessibility and better enable suppliers to offer innovative products and services. Ofgem noted that these options are not mutually exclusive, and it could progress more than one option. It asks stakeholders which of the options are most attractive, and which should be Ofgem's top priority. It is also asking which supply licence conditions (SLCs) would most benefit from being reformed, in order to facilitate innovation.

This consultation does not consider changing routes to market for non-supply activities, as the Government and Ofgem are looking to introduce a new load controller licence through the [Smart and Secure Electricity System \(SSES\) programme](#).

3.2.1 Reforming the derogations regime

The first option is that Ofgem could expand its ability to grant derogations to the SLCs, repurposing the derogations regime so it is more focused on supporting innovation.

Stakeholders have suggested that Ofgem could add derogation powers to SLC 22.3, which implements the Universal Service Obligation, to enable specialist suppliers that provide tailored, personalised services to meet the needs of specific customers, such as those with a heat pump. Another suggestion is to add derogation powers to SLC 27 'Payments, Security Deposits, Disconnections and Final Bills', as this could enable a supplier to enter the market that specialises in specific forms of payment such as mobile payment services, rather than the traditional forms of payment.

Ofgem considers that this could help enable more innovation trials, and that over time, it may be easier to amend a derogation than a licence. However, it noted that relieving a supplier of any obligation could create risk for consumers, or risk of market distortions. Compared to a restricted or individually modified licence, this option may also provide less certainty to investors. If this were to be progressed, it would be critical for Ofgem to ensure it only grants derogations in the consumer interest, and may add conditions to protect these, such as additional reporting requirements or limits on the length of the derogation.

3.2.2 Restricted licences

Ofgem could better enable restricted licences, suggesting changing its guidance to be more welcoming of restricted licence applications and agree a process for assessing them. It could also explore potential new ways of defining restricted licences.

A restricted licence could allow suppliers to develop specialist or local energy products and services. It may provide long-term certainty for innovators who only want to focus on specific types of premises or geographic areas. Ofgem considers this could be useful for enabling innovation in both the domestic and non-domestic markets.

However, this option could be perceived to carry more risk, as if a supplier does supply a customer outside the scope of its restricted licence, it would be in breach of licence conditions and statutory obligations, which is a criminal offence. Ofgem would also need to manage the risk of a premises changing definition to both protect

the supplier and ensure continuity of supply for the customer. For example, if a supplier is only licensed to supply prepayment households and the customer changes their metering arrangements.

3.2.3 Individually modified licences

Ofgem has the power to grant a licence with modifications to the SLCs that are only applicable to that licensee, which it considers could be better enabled to facilitate more innovation. The regulator could amend the licence application guidance to be more welcoming of individually modified licence applications and provide a more transparent process for assessing these.

This could result in bespoke licences that meet the specific requirements of the prospective business model. The exact products and services that could be unlocked would depend on which SLC is modified. However, the development of more individually modified licences would create a more complex and costly licensing regime for Ofgem to administer and operate. The regulator noted there are some licence conditions it would not be willing to modify.

3.2.4 Reforming Licence Lite

Licence Lite allows new suppliers to partner with an existing supplier to take responsibility for certain costly or complex aspects of being a licenced supplier, such as code compliance. This requires a commercial partnership with a third-party licensed supplier (TPLS). However, there has been little demand for this route to market to date.

Ofgem considers it could reform how Licence Lite works, improving the ability for new entrants to find a TPLS and expanding the scope of licence obligations that Licence Lite suppliers are able to outsource. The regulator also highlights the risk of losing customers if the TPLS exits the market and considers amending SLC 11.3 or how Supplier of Last Resort process works in order to allow for the Licence Lite to provide greater certainty if their TPLS services fails.

This could help address the high non-scalable set-up costs associated with establishing a licensed supply business, potentially enabling more viable, new supply undertakings. However, Ofgem stated that due to the historic low take-up, it is unclear about the extent to which reforming this route would meet the needs of innovators.

3.2.5 Enabling licence exempt supply

Current legislation allows supply without a licence up to certain thresholds, such as MWs of energy supplied, and in particular circumstances. While only the Government can alter the legislation to change who is exempt from requiring a supply licence, Ofgem could review the regulatory framework and codes which might be barriers to licence exempt supply, particularly where the supply occurs across the public network.

For example, Ofgem could raise a significant code review to consider how best to enable licence exempt supply in upstream markets, such as balancing or wholesale, through industry codes. It could also review the Maximum Resale Price requirements to ensure they are fit for purpose, as this could facilitate new, innovative, licence exempt supply products or services. The Maximum Resale Price has also been considered as part of Ofgem's [non-domestic market review](#).

As with Licence Lite, reducing the barriers to entry for small-scale suppliers, providing new and more tailored services and products to consumers. However, Ofgem highlights that licence exempt supply customers are not provided the same level of protection as licenced supply customers. If it were to take this option forward, it would have to consider how it can minimise potential risks for customers.

4 Next steps

The consultation closes for written responses on 27 November 2024. Alongside this consultation, Ofgem is also undertaking in-depth bilateral conversations with suppliers and innovators to better understand the barriers to innovation.



CORNWALL INSIGHT

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Cornwall Insight
The Atrium
Merchant's Court, St George's Street
Norwich, NR3 1AB

T: 01603 604400

E: enquiries@cornwall-insight.com

cornwall-insight.com

