Flexible and responsive energy retail markets

Introduction

Founded in 2009, OVO Energy is the leading independent energy retail company in the UK and OVO Group's flagship energy brand, offering an unparalleled scope of digital energy services, solutions and technologies to its pay-monthly customers. Kaluza is an intelligent grid technology company leading the digital transformation of the electricity system. Kaluza's mission is to securely connect all devices to an intelligent zero carbon grid and facilitate a global transition from fossil fuels to renewable energy. It was created to solve the challenge faced by grid operators, energy suppliers and device manufacturers of integrating millions of energy intensive appliances such as electric vehicles onto the grid.

OVO Group are in a unique position in responding to this consultation as OVO Energy has partnered with Kaluza to offer the energy services outlined in this consultation. Through this partnership, OVO Energy customers benefit from the propositions and services Kaluza offer, creating a simple customer experience and one point of contact for the customer.

The energy industry is going through profound change and with that comes new business models, increases in customer demands and the opportunity to provide new propositions. We believe that to ensure quality of service, security of our energy system and guaranteed customer protection, everyone should compete on a level playing field.

Reviewing the Regulatory Framework

Consultation Question 1. Do you agree with our vision for the future of the energy retail market, the outcomes we are seeking to achieve and our characterisation of the key challenges we need to overcome?

The UK's energy market is rapidly changing and government policy has been at the forefront of many of the positive changes. There are now over 60 energy suppliers in the market, all competing for customers. This is coupled with the change in the grid mix, with the UK now having over 30% of its electricity supplied by renewable generation. The transition of the UK energy market is only just beginning, and we will see an even more dramatic change in the next decade.

Government and Ofgem consultations in the past two years have certainly grasped the huge potential of this change. The Smart Systems and Flexibility Plan set out a vision of a smarter system, which is more responsive, dynamic and intelligent, and will ultimately reduce costs. This is partly out of necessity and the need to decarbonise the sector but

also reflective of the new technologies and opportunities we have to update our aging energy infrastructure.

This consultation continues with the ambition to deliver the change required. The old ways of supplier/consumer interaction are already changing, as well as the technologies in the home. Kaluza is already operating in an innovative way to provide market leading energy services. New products that support domestic energy management are already on the market, including our work with home energy storage and smart EV charging. Residential flexibility will be key to decarbonisation but will also have huge benefits for grid balancing and other system services. Research by Imperial College London demonstrates that effective use of residential flexibility could save the whole energy system costs of up to £6.9bn[1].

We envisage substantial growth in this market, as well as an evolution of the traditional interactions with consumers, which includes Third Party Intermediaries entering and thriving in a new and more competitive market. This will be beneficial both to consumers, as well as the wider energy system.

This, however, will also present a much more complex offer for consumers, which if handled poorly by the industry and regulators could lead to mis-selling, poor customer service, loss of service and damage consumer trust and confidence.

There is an optimum level of regulation that ensures competition, opportunities for new entrants and freedom to innovate, while guareenting there is a fair and level playing field for all. OVO believes removing obligations for service providers does very little to improve the playing field, but significantly increases the potential for worse customer experiences. This is important, as we will need all customers to be involved in the energy transition. If we lose that trust, it will make the transformation of energy services considerably harder.

It should also be reiterated that it is increasingly difficult to look at a single part of the energy system without taking a holistic view of the whole market and policy environment. One of the major drivers of energy policy is the need to decarbonise coupled with achieving the Government's target of net-zero by 2050, yet this consultation is lacking in consideration to this goal. The transition to zero-carbon energy system is reliant on the increasing penetration of renewables, which in turn is increasingly reliant on infrastructure, grid changes and consumer behaviour. To necessitate this change, we need more joined up thinking between different actors and a shift in mindset across government and regulators, especially around what grid model will best serve the energy system of the future. We need strong signals that show this transition facilitates more efficient use of cheap, renewable and abundant energy on the system.

[1] Imperial College London, Blueprint for a Post Carbon Society ,https://www.ovoenergy.com/binaries/content/assets/documents/pdfs/newsroom/blueprint-for-a-post-carbon-society-how-residential-flexibility-is-key-to-decarbonising-power-heat-and-transport/blueprintforapostcarbonsocietypdf-compressed.pdf

These outcomes, which OVO believes we share with the Government and Ofgem, do not need to come through extensive policy interventions or sweeping regulatory reform, but rather through addressing the market dynamics sent through price signals. A wide choice of energy services would be available if strong granular, locational and temporal price signals that reward the use of local, renewable energy generation were in place.

Our experience through Kaluza is that the barriers to bringing new business models to market are not supplier obligations, but instead these innovative businesses struggle to make the margins they needed to grow. This is about the way the market enables revenue making, rather than customer access.

It should also be highlighted, that decarbonising the energy system in the most cost effective and efficient way means the energy system should be flexible and responsive to make sure consumers take advantage of the cheap, decentralised energy on the system. This should be a key principle in future consultations.

Consultation Question 2: Are there examples of new products, services and business models that would benefit current and future consumers, but are blocked by the current regulatory framework?

The UK energy market, whilst ahead of most countries, is still at a nascent stage of the consumer offer for innovative energy products and services when you consider the opportunities presented by the energy system of the future. This is partly due to the fact that many of these services are still being developed but also that the economic drivers are not giving a clear enough incentive for consumers.

We strongly believe that any regulatory changes should look at technical barriers to flexibility and better use of data, rather than weakening supplier obligations or protections. Smart Meters are a good example of smarter infrastructure being a catalyst for innovation. Half Hourly Settlement (HHS) is another area that has facilitated better use of data resulting in positive outcomes for consumers. The introduction of elective HHS has been a key trigger for the release of innovative propositions which have both improved consumer acceptance and supported the route to market of flexible technologies.

Consumers have already benefited from new products offered by Kaluza, such as OVO's 'EV Everywhere' bundle due to the HHS changes. We are supportive of Ofgem's work to establish market-wide HHS in the coming years, and Ofgem should look to increase - and incentivise - suppliers to roll-out elective HHS in the interim, and remove existing industry and infrastructure blockers to this process.

On the substantive issue of existing barriers, our experience through OVO and Kaluza shows that suppliers are fully able to provide customers with these products and services without complicating the process for consumers or reducing consumer protections. A much bigger issue is customers being held back by the lack of value being passed through in the current market design.

Away from the significant issue of decreasing consumer protection and the risk of creating two-tiers of consumer, removing supplier obligations from some market participants providing energy services and not others, would also lead to an unlevel playing field between "primary suppliers" and "secondary suppliers" and could create anti-competitive dynamics.

OVO demonstrates that the existing system already allows for new products without forgoing customer service responsibility and fulfilment of necessary supplier obligations. There are already many examples of new data initiatives underway that will allow new business models to develop.

Current departmental workstreams point to a disconnect in BEIS/Ofgem's other work on making the supplier licence process more robust and resilient to prevent unsustainable businesses entering the market through the supplier licence reform, while at the same time trying to make it easier for new customer facing businesses to avoid supplier obligations. This is sending mixed messages, as well as distorting what is already a competitive market.

Consultation Question 3: Are there current or emerging harms to energy consumers which are currently out of scope of the regulatory framework? Do these differ for domestic and nondomestic consumers?

The biggest challenges Kaluza has experienced surround the market pricing structure and how incentives are placed on the existing system to use innovative products.

It is crucial that energy products not currently within a traditional regulatory framework but key to future domestic offers (such as EV charging, heat balancing, data optimisation and the plethora of 'smart' products that are entering the market) are not being undervalued in the future market structure. This ultimately will lead to a less efficient energy market, resulting in higher bills for all. Imperial College London research showed households could benefit from as much as £206 per year if residential flexibility was partnered with electrification and decarbonisation[2].

If domestic consumers cannot access the value of flexibility they have installed, they will miss out on the benefits these technologies can bring. This will harm any incentive to purchase such products in the first place, slowing down the transformation needed.

OVO supports the Government's aims of increasing the ease in which people can switch, and greater automation and technology should be used wherever possible. However, with some auto-switching services, the customer relationship with their energy supplier is secondary, despite the supplier retainaining full responsibility for all obligations and

[2] Imperial College London, Blueprint for a Post Carbon Society ,https://www.ovoenergy.com/binaries/content/assets/documents/pdfs/newsroom/blueprint-for-a-post-carbon-society-how-residential-flexibility-is-key-to-decarbonising-power-heat-and-transport/blueprintforapostcarbonsocietypdf-compressed.pdf

requirements related to the relationship. The regulatory requirements governing auto-switching sites do not offer consumers the same levels of protection as suppliers are required to provide. This could lead to customer detriment, for instance with customers being misinformed or mis-sold tariffs with incomplete information.

We also think there is a problem specific for home energy storage looking to export stored energy back to the grid at times excessive demand. Under current obligations customers who wish to participate in delivering these services are billed twice for their electricity obligations. This harms the business case for residential storage as it eats in to the spread between the total import and export prices for electricity supply. This reduces the value that can be generated through, for example, HH wholesale arbitrage optimisation. The government should look to address this market distortion.

Consultation Question 4: Would it be beneficial to allow suppliers to specialise and provide products and services to targeted groups of customers? If so, how can this be delivered while balancing the need for universal service?

OVO agrees with moves to make it easier to deliver innovative and non-traditional energy offers and services but believes consumers should be at the heart of any change. With that in mind, we strongly disagree with any policy changes that hive off consumers, or create separate classes of customer, which would have several negative consequences that would hinder the aims of this consultation.

Watering down the Universal Service obligation would firstly create uncertainty in terms of consumer protections (regarding qualification for energy/service provision), as well as adding unnecessary complexity into what will be a new area for many consumers.

Secondly, retailers already have many tools to target specific groups and offer tailored services, while still maintaining the obligation to serve all customers. If this was removed, it could create a dangerous precedent of service providers turning down consumers, creating a two-tier market, which could open up the potential for consumer exploitation and disenfranchisement from the smart energy revolution.

It could also present a market distorting situation in which two neighbouring houses, both with EVs, electric heating and smart devices end up paying different social and environmental costs because one is supplied by a Universal Supply/Primary Supplier and the other by a Secondary Supplier not obligated to pay these costs. The latter option would not be guaranteed for all customers and would further skew the costs of the grid.

This is further exacerbated by the fact that an EV user with a distinct secondary supplier for that asset could have the same electricity load as many households, adding to the required capacity and network costs but not paying for these. This would appear unfair to many, eroding public trust in this process.

Consultation Question 5: Are incremental changes to regulation sufficient to support the energy transition and protect consumers? Or does this require a more fundamental reform, such as moving to modular regulation?

OVO believes that the current incremental changes are heading in a positive direction and any added complexity or significant overhaul would be detrimental to the momentum that is already driving forward this market.

It should be a firm principle that there is parity between any players in any given market and that secondary licences should be in-line with primary licences. There is an ongoing separate workstream to improve the supplier license, and to do that while simultaneously excluding segments of the market from these obligations would create a significant market distortion.

We believe that the supplier obligations around Standards of Conduct and interactions with customers should be applied equally to all suppliers to ensure that there is no degradation in customer service and consumer protection. The Government should ensure that reforms to "Secondary Supplier" obligations do not create a market distortion of creating an inherent advantage in being a "Secondary Supplier".

Consultation Question 6: Are there any other potential market distortions we should be considering as part of our review?

The Government should look at the policies that are needed to facilitate a more responsive grid and provide market signals that that incentivise a flexible, more efficient, renewables based energy system.

Currently, we are seeing the opposite approach taken outside of this consultation in a number of other workstreams. The current series of Network Charge reforms being undertaken by Ofgem is an area where market distortions against flexibility, such as DUOS and TNOUS reforms, are running contrary to the objectives of this consultation.

We should also be looking at encouraging greater residential flexibility and faster roll out of HHS in order to catalyse identification of 'peaky' customers who are currently undercharged, and dynamic households and small businesses who are undervalued.

There is also a market specific distortion for home energy storage looking to export stored energy back to the grid at times excessive demand. Under current obligations customers who wish to participate in delivering these services pay policy obligations when they import this energy. When the energy is exported back to the grid, the next importer of this energy then pays the obligations again. Effectively energy that's been stored domestically is billed twice for its electricity obligations. This market distortion disincentivises efficient use of energy on the system.This has the effect that it harms the business case for residential storage as it eats in to the spread between the total import and export prices for electricity supply. This reduces the value that can be generated through, for example, HH wholesale arbitrage optimisation.

Market Distortions and Complexity

Consultation Question 7: Would removing the thresholds for the Energy Company Obligation and Warm Home Discount help remove imbalances in the retail market, and could this be done without significantly increasing barriers to supplier entry or expansion in the retail market?

We agree that the thresholds for ECO and WHD should be reformed with a preference that they should be removed to avoid market distortions in what is now a very crowded and competitive market. We believe that the newly adopted ECO taper mechanism, alongside the longer ECO3 legislative period and existing inter-supplier trading mechanism significantly limits the burden on newly obligated suppliers. Removal of thresholds should be part of a wider reform of the retailer obligations, which also looks at issues over self-identification, ECO/WHD calculations, the potential for more brokering of services, as well as more freedom to innovate in the delivery of these activities. The latter could be a significantly positive move, especially in respect to the goals of this consultation, and could open up more flexible and smart technologies to a wider range of consumers.

For self-identification, there are more technologically advanced options, such as those discussed in the 2018 Warm Home Discount consultation and enabled by the Digital Economy Act. This includes the proposal to create a centralised identification process that detects eligibility for such schemes. This requires Ofgem and BEIS to work further on data matching.

Consultation Question 8: How could the delivery burden on suppliers from the Energy Company Obligation be reduced, for example through the introduction of a buyout mechanism?

OVO believes a buyout mechanism could work in theory but it would be important to ensure all parties are competing equally and have matching obligations in practicality, even if this looked different from supplier to supplier.

There will be challenges over buyout mechanisms and how prices should be set. It could shift an existing administrative burden into a price burden but effective monitoring and assessment of such schemes could prevent this dynamic from emerging.

OVO also has concerns with an existing transfer and trade policy being open to third parties. We believe it would be more efficient to keep this as a supplier service as it is easier to find customers and would be an appropriate responsibility given the obligations to customers.

Consultation Question 9: What effect does the range of Energy and Climate Change Policy Levies have on the retail market?

OVO would advocate for more frequent payments for environmental levies. The increase of SOLR events in the past 18 months have made it challenging to price the

probability of non compliance with RO payments, something that has significantly distorted the market.

Consultation Question 10: What actions could the government take to reduce any negative impact of Energy and Climate Change Policy Levies?

We would advocate creating more regular payments as part of the RO process. We'd also suggest Ofgem use the Supplier Licence Reform consultation currently underway to introduce regulation that more carefully monitors the use of credit balances as capital for levies.

As highlighted above, we also think there is a problem specific for home energy storage looking to export stored energy back to the grid at times excessive demand. Under current obligations customers who wish to participate in delivering these services pay policy obligations when they import this energy. When the energy is exported back to the grid, the next importer of this energy then pays the obligations again. Effectively energy that's been stored domestically is billed twice for their electricity obligations, a market distortion which disincentivises efficient use of energy on the system. This has the effect that it harms the business case for residential storage as it eats in to the spread between the total import and export prices for electricity supply. This reduces the value that can be generated through, for example, HH wholesale arbitrage optimisation.

Consultation Question 11. Do you agree that now is not the time to make further changes on system and network cost recovery, metering and access to data as part of this retail market review?

OVO strongly agrees with this position and have made representations of our position through the Access and Forward Looking Charges consultation.

Consultation Question 12: What total costs do suppliers face with regards to bad debt and supporting consumers who struggle to pay for their energy?

OVO are supportive of the Treasury's "Breathing Space" workstream and have been working with BEIS on the specifics of high cost to serve customers.

Consultation Question 13: How could any potential distortions related to high cost-to-serve customers be addressed, for example by the provision of additional support services for customers struggling to afford their energy?

OVO works with debt charities and has programmes designed to support customers who are struggling with affordable payment plans.

We proactively engage with consumers struggling with debt and look to give advice on any government schemes or support they may be entitled to. We also signpost customers to the Step Change debt charity if they have financial problems which are broader than just issues with paying for their energy.

In addition to this, we have an internal programme in place to help those in debt through the OVO Fund. This helps clear customers debt if they meet certain eligibility criteria, and make spread payments over a more manageable period of time.

Energy is an essential service to millions of households across the UK, and we will always advocate for measures that help those in fuel poverty. Often customers who struggle to afford their energy, are also in need of additional support with other bills and household costs. The Government should assess whether issues with affordability should be moved away from suppliers and be addressed through taxation / benefits. This discussion and topic should stand outside the scope of this consultation.

Consultation Question 14: Would addressing market distortions (for example size-based obligation thresholds for some policy schemes, supporting those who are struggling to afford their energy bills) help reduce incentives for suppliers to adopt pricing strategies that lead to excessive prices for loyal consumers? If so, to what extent (providing quantitative evidence, where possible)?

We are supportive of measures to address issues of consumer overpayment and advocate for the price cap to continue, which we believe prevents overly excessive prices for loyal customers.

We believe strongly that prices should be more reflective of the true cost to serve and that the market design should encourage competition between sustainable companies. Market intervention should not be used to protect distortions caused by inefficient business models, high debt or slow adaptation to new technologies. Nor should we look at introducing more distortions or watering down consumer protections, which could damage trust in the industry.

Although some of the above proposal address some market distortions, our view is that it would not address the dynamic whereby suppliers could take advantage of loyalty as a profit maximising approach. While this temptation remains possible in the market there is still a need for regulation.

Consultation Question 15: What are your views on the measures being considered to address loyalty penalties in different markets? What approach or – combination of approaches – would be most effective in the energy retail market?

We would not want the introduction of regulation that would carve out sections of the market. With more bundled packages and services emerging, this could prevent customers from accessing energy service deals and cross-utility bundles.

Consultation Question 16: What other approaches could be adopted to ensure loyalty penalties do not reemerge?

The Price Cap is designed to prevent excessive pricing. Until market dynamics are introduced to prevent customers from being overcharged to cross subsidise unsustainable customer acquisition strategies, both in order to compete with companies who are not pricing their tariffs sustainably or within companies own

portfolios, we believe the price cap should not be removed. We also strongly advocate the principle of treating all customers equally and fairly and that we should not look to create two tiers of consumer or have an ability to pick and choose segments of the market. All customers should have access to all companies' tariffs, services and offers.

Consultation Question 17.What protections or support may be required to engage consumers in vulnerable situations in the future market?

View answer to Q7.