

Maureen Paul
Deputy Director of Retail Market Policy
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

Sent via email: retailpolicyinterventions@ofgem.gov.uk

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Dear Maureen,

Energy UK response to consultation on extending the MSC and BAT

I am writing to you in response to Ofgem's "Statutory Consultation on extending the MSC and BAT beyond 31 March 2023".

We agree with Ofgem's plan to extend the Market Stabilisation Charge (MSC) and Ban on Acquisition-Only Tariffs (BAT) until 31 March 2024. This extension is important for the resilience of the retail energy market. The extension will enable suppliers to continue to prudently hedge in line with the price cap methodology and guidance, ultimately protecting customers against rising prices in line with the cap.

While the level of supplier switching in the energy market has decreased significantly in the last 18 months, there were still over 150,000 electricity switches in October 2022¹. We have also seen the first period where the MSC was required in November 2022 when wholesale gas costs fell more than 10% lower than the wholesale cost in the price cap. This context of continued switching and wholesale volatility highlights the importance of the MSC mechanism.

We welcome that Ofgem has committed to examining the methodology and necessary adjustments shortly. For the scheme to mitigate supplier risk in the way that it is intended, it is vital that the MSC accurately reflects the existing and evolving price cap liabilities for suppliers. We think that there is a need for a broad review of how the MSC is functioning and the extent it is insulating suppliers – and ultimately customers – from unstable and uncertain market conditions. Currently, the MSC is only triggered by the relative movement of wholesale prices rather than when switching occurs, and suppliers will be required to absorb the costs of selling excess volume, for customer losses, in a falling market before the MSC is triggered. We recommend that the methodology also takes into account losses suffered by

¹ <https://www.energy-uk.org.uk/index.php/publication.html?task=file.download&id=8361>

the losing supplier in respect of deferred cost recovery under the price cap (such as for backwardation, unexpected SVT and BSUoS transition).

Ofgem has framed the potential withdrawal of the MSC and BAT as an “as soon as is necessary” type approach. We note Ofgem are planning to review the MSC and BAT in April 2023 and October 2023 with the power to terminate at any time based on an assessment of the continuing rationale. Notwithstanding Ofgem’s wish to apply the scheme only when necessary, we encourage Ofgem to reconsider the risks for suppliers and value for consumers of adopting this approach in the current context, and to commit to consult ahead of any decision to terminate.

The way in which the scheme is being extended, for example, with an extension decision in August 2022 for continuation from September 2022 means that suppliers were exposed to the risk of non-continuation. Similarly, the regular planned reviews in 2023 and scope for removal, potentially at short notice, without clear predictable parameters, creates risk. While customer switching rates are relatively low, financially responsible suppliers that attempt to mitigate this risk will likely incur costs.

While the Energy Price Guarantee (EPG) dampens the immediate incentive for consumers to switch, the EPG does not apply to new fixed term contracts. Since the introduction of the EPG the number of customers on the price capped SVT has risen to 84%. These customers are now waiting to see when fixed tariffs will be a good option. The pressure on suppliers will intensify as more consumers’ fixed rates end and as consumer awareness and engagement with their energy increases due to the average bill doubling since 2021 and set to increase to £3000 from April 2023. This is not a risk a supplier can mitigate in isolation. The way in which wholesale volatility is managed by suppliers, the UK Government and Ofgem when movement to fixed rates occurs, will be important for the resilience of the energy market.

If the EPG is applied to new fixed tariff offerings, the MSC and BAT will be even more important to ensuring suppliers risk exposure does not dramatically increase, causing short- and long-term costs for consumers. The parameters of the MSC will need to be carefully assessed and likely strengthened due to the scale of risks when significantly higher numbers of consumers are switching supplier.

Given the uncertain environment in which suppliers are operating, we recommend Ofgem works with BEIS to consider how to improve clarity and confidence about the continued operation of the MSC and BAT over the next year and beyond. This could include providing greater confidence about the terms and process for termination. We think a more definitive commitment to managing the transition through market stabilisation should lead to consumer benefits.

Energy UK is happy to discuss anything in this letter further with Ofgem. Please contact me by emailing ed.rees@energy-uk.org.uk

Kind regards,

Ed Rees

Senior Policy Manager, Energy UK