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Dear Dan

## **FUTURE OF THE BAN ON ACQUISITION-ONLY TARIFFS (BAT) POST-MARCH 2024**

We welcome the opportunity to respond to your non-statutory consultation on the future of the BAT. Our responses to the stakeholder questions are in Annex 1 to this letter, however we would like to highlight the following points:

- There is no way to be sure that recent, relatively benign, wholesale prices will persist. The BAT provides a form of future-proofing against volume risk in a scenario of further wholesale price spikes that may threaten market resilience. The recent period of relatively stable wholesale price has been contingent on the weather – an unexpected cold snap may bring further price spikes. There is also considerable uncertainty around the implications of geopolitical instability.
- We are disappointed that Ofgem has decided to allow the MSC to lapse, however given this decision, retention of the BAT is now of increased importance. The BAT reduces the incentive for suppliers to offer aggressive acquisition prices and so reduces the risk of large and unexpected movements of customers on default tariffs, with the associated risks for supplier financeability.
- While Ofgem is considering the future of the price cap and waiting for implementation of key measures such as the capital targets and market-wide half hourly settlement, the BAT should be retained as protection for inactive customers who are more likely to be in vulnerable situations.
- The BAT does not affect innovation as suppliers are more likely to test new tariffs on existing customers with an established baseline. We do not see any reason, as some have argued, why innovative tariff offerings should not be made available only to existing customers.

- We consider the ban on acquisition-only tariffs should be a permanent feature of the regulatory framework and we think it is important that a bespoke licence condition is written and ask that Ofgem amends licence condition 22B accordingly.
- Uncertainty over the continuation of the BAT could drive unnecessary costs for consumers through supplier hedging. In the absence of the BAT, financially responsible suppliers who hedge to the cap may factor in their exposure to unexpected reductions in customer numbers as a result of aggressive acquisition-only pricing tactics from competitors.
- Appropriate lead times for regulatory change should be factored in to Ofgem's strategic planning, with each element of change considered as part of Ofgem's strategic retail policy. Implementation planning should reflect impacts on supplier hedging and on regulatory risk in general.

Yours sincerely,



**Richard Sweet**  
Director of Regulatory Policy

## FUTURE OF THE BAN ON ACQUISITION-ONLY TARIFFS (BAT) POST-MARCH 2024 – SCOTTISHPOWER RESPONSE

### 1) Do you consider there is merit in keeping the BAT in place post March 2024, after the discontinuation of the MSC?

The BAT reduces suppliers' incentive to offer aggressive, loss-leading deals aimed at building up their customer base, bringing volume risk for the wider market. In periods of wholesale price volatility, these loss-leading offers could threaten the viability of both the gaining and losing suppliers. This means that the BAT helps to maintain market stability and resilience. This stabilising influence is particularly valuable given uncertainty regarding the direction of broader price regulation in retail markets.

Ofgem's consultation on the BAT notes that "the optimal level and type of competition required for a healthy market" is under consideration, and that an example will soon be published, setting out how the proposed competition framework was applied to the decision to let MSC expire. As the competition framework has not yet been finalised and some key concerns were raised by stakeholders regarding Ofgem's proposals,<sup>1</sup> it would be appropriate for Ofgem to set out which aspects of the framework have been finalised and how they are being applied to the decision on whether or not to keep the BAT in place. More clarity is also needed around Ofgem's assessment of the optimal level and type of competition for a "healthy market". A clear understanding of what Ofgem means by this is necessary to understand the expected impact of the BAT in this context.

Retention of the BAT is in line with Ofgem's Consumer Interests Framework, as it will:

- help ensure that **undue price discrimination is prevented** (Fair Prices)
- will work to **minimise consumer welfare risks** by preventing consumers who are not in a position to seek out loss-leading deals from effectively cross-subsidising highly engaged customers (Fair Prices) and allow suppliers to achieve greater cost efficiency by reducing both hedging and regulatory risks (if retained on an enduring basis). This **helps overall resilience to market shocks** by reducing the risk of large and unpredictable SVT movements if wholesale prices are volatile (Resilience)
- risk reduction due to the presence of **the BAT helps ensure the sector is investable** (Resilience)

Ofgem should be more transparent about how it will assess whether to keep the BAT or not. If Ofgem were to use Value at Risk, as with the Market Stabilisation Charge (MSC), it should consider how future volatility is incorporated into decision making. Whilst markets are currently more stable than last year there is current geopolitical instability, with uncertain impacts on energy markets in 2024 and beyond.

A stable supply market is in the best interests of consumers as it enables suppliers to plan and invest to deliver the system of the future. We agree that it is in accordance with the Authority's principal objective that market stabilisation measures be retained if there remains concern regarding market stability.<sup>2</sup> We think there is merit in keeping the BAT in place on an enduring basis, because this will go some way to supporting market stability, and this is particularly important post discontinuation of the MSC.

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<sup>1</sup> For example, in the response from Energy UK: [\\*Energy-UK-Response-to-Ofgems-call-for-input-on-the-Competition-Framework-20.9.23.pdf](#)

<sup>2</sup> See, for example, para 2.7 [Decision on changes to market stabilisation charge | Ofgem](#)

## **2) Market Stability**

### **(i) Can you provide your thoughts on/evidence of the impact of the BAT to date in terms of market stability?**

While there is a clear logic as to how the BAT will have helped maintain market stability, quantifying the impact it has had over the time it has been in place would require modelling of a counterfactual scenario. Similarly, quantification of the benefits it may have if it was to be retained would require modelling. As the current version was implemented alongside the MSC, separating the impacts of these would be particularly challenging.

Good evaluation of the effects of an intervention requires a thorough understanding of the theory of change.<sup>3</sup> Effective evaluation of the benefits and costs of retaining the BAT would necessitate exposure of the assumptions on which any decision is based and the strength (or weakness) of the evidence supporting those assumptions.

The approach that has been taken to date with extension decisions made close to the deadline (for example, an extension decision in August 2022 for continuation from September 2022) means that suppliers have been exposed to much uncertainty and risks of non-continuation. This has increased regulatory risk and meant that the realised benefits of the BAT are likely to have been lower than they might otherwise have been.

The BAT reduced the prevalence of loss leaders for simple tariffs; however it is still possible for suppliers to have loss leaders for innovative time of use tariffs.

### **(ii) Can you provide your thoughts on/evidence of the BAT's likely impact on market stability, if it was retained post March 2024 as a standalone measure?**

We would expect the BAT to have a stabilising influence by reducing incentives to suppliers to offer loss leading tariffs during periods of market volatility that could threaten market stability. Whilst markets are currently more stable, Ofgem cannot assume this will continue to be the case in the future and constructing a new licence condition to give effect to the BAT would future proof some protection for suppliers. Indeed, there is current geopolitical instability, with uncertain impacts on energy markets.

The extent of the impact on market stability will be dependent on the wider regulatory framework that is in place post March 2024. For example, whether there is an energy price cap for default tariffs. The BAT could play a role as part of Ofgem's exit strategy from the current price cap policy.<sup>4</sup> Without a price cap in place, there is a risk that a loyalty penalty would develop for inactive customers across Great Britain. A wider transformation of the regulatory framework for retail markets is also underway, with consumer flexibility expected to play a key role in the sector's transition to net zero. Fundamental changes are being delivered through Ofgem's Market-Wide Half Hourly Settlement Programme and the Government's Review of Electricity Market Arrangements. All of these changes are fundamental to the context in which the future of the BAT is being considered.

Ofgem's work to improve resilience in retail markets has resulted in the introduction of a minimum capital requirement Floor and Target effective from 31 March 2025.<sup>5</sup> Before this

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<sup>3</sup> See chapter 2 of the Treasury's "Magenta book", which sets out government guidance on evaluation: [\\*HMT Magenta Book.pdf \(publishing.service.gov.uk\)](#)

<sup>4</sup> This is particularly important given that Ofgem's chief executive has called on ministers to rethink the price cap: ['Change is needed': Ofgem chief calls on ministers to rethink energy price caps | Ofgem | The Guardian](#)

<sup>5</sup> [Strengthening Financial Resilience- Minimum Capital Requirement and Ringfencing CCBs by Direction \(ofgem.gov.uk\)](#)

date, Ofgem should certainly not remove the BAT since it limits the cost associated with the volume risk that a supplier might be subject to in a falling market.

As noted in our response to Question 1, there is a lack of transparency regarding the status of the Competition Framework that Ofgem consulted on in August 2023. Ofgem has applied this draft framework in their decision to remove the MSC, and to consult on retention of the BAT. In this context, it is concerning that Ofgem is not yet able to provide more information on the strategic direction for retail markets so that suppliers can provide feedback on expected impacts of the BAT, based on a better understanding of the expected regulatory context.

The benefits of the BAT for market stability can be maximised if Ofgem provides confidence on the enduring regime. The current approach, with the potential for removal of the BAT at short notice, and without clarity on the approach to assessment, increases regulatory risk. Financially responsible suppliers that attempt to mitigate the risk of potential switching in a scenario where the BAT is not retained may face increased costs.

Overall, the BAT brings few potential downsides for consumers and could have some positive effects on facilitating the development of longer-term customer relationships and innovation to meet customer needs. This, combined with the benefits for market stability and reduced volume risk for market participants makes retention in the best interest of consumers.

### **3) Competition: impact on suppliers and consumers**

#### **(i) What impact would the BAT's existence post-March 2024 have on market competition for a) existing suppliers and b) new suppliers seeking to enter the market?**

For existing suppliers, the BAT reduces suppliers' exposure to falling wholesale prices by reducing the risk of mass defection to competitors, since it would limit their ability to promote loss leader tariffs. Without the BAT, these aggressive tariffs could lead to a "race to the bottom" as was evident prior to the energy market crisis in 2021. Maintaining the BAT would reduce the risks to financially responsible suppliers who would therefore have lower costs of managing this risk, allowing savings to be passed on to customers.

For new suppliers, an enduring BAT may not have an initial impact since they can promote loss leaders to try to build up a customer base. However, at some point in their customer acquisition, an enduring BAT would force them to offer longer-term propositions to their customers. This reduces new market entrants' opportunity to take what is effectively a "one-sided bet" with consumers bearing the risks.

Ofgem has acknowledged that promoting competition in retail markets has not always delivered value for consumers, especially those who are less engaged.<sup>6</sup> We welcome Ofgem's intention of using its new competition assessment framework to assess options for regulatory reform. A resilient and investable market is essential for sustainable competition and delivering the best outcomes for consumers.

#### **(ii) What impact do you consider the extension of the BAT would have on a) active and b) inactive consumers (i.e. less likely to switch), in terms of realising the benefits of any competition?**

a) The BAT reduces the scope for **active consumers** to move tariffs on the basis of aggressive price reductions, and so means that they miss out on loss-leading offers. However, it also means that they benefit from increased supplier stability.

b) The BAT reduces the scope for **inactive consumers** to be in a position where they cross-subsidise active consumers. These customers also benefit from increased supplier

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<sup>6</sup> See para 1.3 [The development of a competition framework for the domestic retail market \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/consult/condocs/comp/comp230123/comp230123.pdf)

stability. Supplier failure is costly to all consumers, and inactive consumers are more likely to be in vulnerable situations, as indicated by Ofgem's consumer archetypes.<sup>7</sup>

**(iii) What are your thoughts on the BAT's role in making discounted deals available to a supplier's existing customers, and are you able to provide evidence to support this? Do you consider that there is benefit in having the BAT in place to provide this function while the price cap is also in place?**

We consider that there are benefits from suppliers being able to offer existing customers discounted deals or retention tariffs. The price cap was motivated in part over concerns about the perceived loyalty penalty in the market. Offering low prices to existing customers could be seen as a reward for their loyalty and therefore we consider that a new BAT licence condition should be drafted in a way that does not preclude this. Retention tariffs may also be valuable in developing longer term supplier-customer relationships. Price is only one of the elements that drive customer choice of supplier and retention tariffs could be more tailored to the supplier's customer base. Our concern regarding the removal of the BAT is that existing customers may then face a perceived loyalty penalty.

**(iv) What are your thoughts on the existing policy and process for market-wide derogations for fixed retention tariffs?**

We suggest Ofgem drafts a new licence condition that appropriately ringfences retention-only tariffs offered to existing customers only, rather than maintaining the current market-wide derogation for tariffs targeted at existing customers only. In future consultations, Ofgem should also consider the BAT's benefits for the development of innovative time of use tariffs, which we expect to be a feature of the future retail market.

We think the current draft licence conditions could be adjusted relatively easily to ensure suppliers would not be precluded from offering tariffs only to groups of existing customers. We propose Ofgem makes the following amendments to SLC 22B.1 and 22B.2:

22B.1 Subject to paragraph 22B.2, the licensee must ensure that all its Tariffs are available to, and are capable of being entered into by, ~~both new and existing~~ Domestic Customers.

22B.2 Paragraph 22B.1 does not apply to:

- a. A Closed Fixed Term Tariff;
- b. A Collective Switching Tariff;
- c. A Dead Tariff which complies with standard condition 22D; and
- d. Tariffs only offered to a particular group of Domestic Customers defined on the basis of criteria specified by the licensee, provided that the criteria do not in any way ~~exclude all existing Domestic Customers relate to whether or not the Domestic Customer is a new or existing Domestic Customer.~~

#### **4) Impact on tariff offerings**

**(i) Can you provide your thoughts on/evidence of the BAT's likely impact on supplier tariff offerings?**

The BAT reduces incentives to undercut the market through aggressive acquisition-only tariffs. It does not prevent suppliers from offering innovative tariffs, and may even facilitate this by enabling longer term relations between consumers and their suppliers.

Ofgem has suggested that it has "seen instances where the BAT may be restricting tariff innovation and development, including possible low carbon technology tariffs (LCT) tariffs and

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<sup>7</sup> [Ofgem energy consumer archetypes - final report 0.pdf](#)

business models supporting the transition to net zero.” We are unsure why the relevant supplier would not want to offer these tariffs to existing customers or to existing customers only and seek a derogation for a retention tariff. We note that Ofgem’s Energy Regulation Sandbox is also available to help innovators trial or bring to market new products, services, business models and methodologies without some of the usual rules applying.<sup>8</sup>

Ofgem has suggested that the BAT could lead to reduced dynamism overall, which could “result in worse deals for most consumers”.<sup>9</sup> Presumably this is intended to mean that the BAT could result in worse deals potentially being *available to* most consumers rather than deals that most consumers are actually on being worse. In evaluation of what is in the best interests of consumers here, we consider that the BAT is overall likely to be beneficial to most consumers and that robust analysis should support this.

Published impact assessment guidance sets out how Ofgem’s goal is to assess the impact of policy using the energy spend and income data in each consumer archetype, supplemented with qualitative assessment using the information on vulnerability in each of the archetypes.<sup>10</sup> Given that the non-switching consumers who are most protected by the BAT are more likely to be in Ofgem’s low-income archetypes, bringing this quantitative and qualitative analysis together would provide a structured framework to inform Ofgem’s decision on retention of the BAT.

**(ii) What are your thoughts on whether changes should be made to the BAT in order to make it a more effective policy to encourage competition (rather than as a policy to support market stability)?**

Ofgem should clarify whether or not the BAT will be enduring in nature and how assessment of the BAT’s role in future retail markets will be undertaken. If there is a decision to make the BAT an enduring obligation, the licence condition should be rewritten with consideration for the impact on innovation and sustainable competition.

A key element to encouraging the investment needed for net zero is a stable and predictable regulatory framework for suppliers and consumers. This facilitates long term investment by ensuring that investors can expect to receive a reasonable return, subject to both the normal risks inherent in markets and the appropriate consumer protections. As noted in the UK Government’s recent policy paper on Economic Regulation, “transparent and predictable regulatory frameworks are vital to facilitating investment, protecting consumers, and delivering sustainable growth.”<sup>11</sup>

**ScottishPower**  
November 2023

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<sup>8</sup> [Innovation Link | Ofgem](#)

<sup>9</sup> Pg 3 [Ofgem Call for Input on the Future of the BAT post-March 2024](#)

<sup>10</sup> [Impact Assessment Guidance | Ofgem](#)

<sup>11</sup> [Economic regulation policy paper \(accessible webpage - HTML\) - GOV.UK \(www.gov.uk\)](#)