

Daniel Newport
Retail Price Regulation
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

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Dear Danny

Market Stabilisation Charge licence condition

We welcome Ofgem's statutory consultation on reinstating the Market Stabilisation Charge (MSC) condition in the supply licence, to provide optionality to activate an MSC at pace if required in a falling wholesale market. When used proportionately and in clearly defined circumstances, the MSC has the potential to support positive long-term consumer outcomes by underpinning a stable and competitive retail market. We strongly support Ofgem's proposal to reinstate the licence condition. Our answers to Ofgem's two consultation questions are in Annex 1.

Timeliness of MSC activation

Although reinstating the MSC licence condition is a necessary first step to protecting the stability of the retail sector, the effectiveness of this intervention will depend critically on Ofgem's ability to trigger the MSC in time, given the speed at which customer behaviour and switching patterns can respond to changes in relative pricing. We urge Ofgem to publish a decision on licence amendment as soon as possible following closure of this consultation, and to use the 56-day period before the licence condition takes effect to consult on activation, including consultation on guidance and parameters to be applied as appropriate.

MSC guidance and parameters

Ofgem invites early feedback on the MSC guidance or the MSC parameters, which are not covered in the current consultation. We understand that, in the interests of speed, Ofgem expects to retain the MSC parameters set out in its most recent MSC guidance of 20 March 2023.¹ While we agree with the need for speed, the MSC guidance should in our view be updated to (i) include ex post allowances in the price cap in the calculation of both the trigger and the MSC charge, (ii) amend the format of the trigger from a percentage decrease in wholesale costs to an absolute £/MWh threshold, and

¹ [Ofgem, \(2023\) 'Market Stabilisation Charge Calculation Methodology v4.0'](#)

(iii) increase the de-rating factor from 85% recovery to preferably 100% but at least 90%.
This is explained further in Annex 2.

Yours sincerely,

A handwritten signature in blue ink that reads "Richard Sweet". The signature is written in a cursive, flowing style.

Richard Sweet
Director of Regulatory Policy

**MARKET STABILISATION CHARGE LICENCE CONDITION
– SCOTTISHPOWER RESPONSE**

Q1. Do you agree that an MSC could help to manage the impact of falling wholesale prices?

We agree that reinstating the Market Stabilisation Charge (MSC) could help to manage the impact of sharp falls in wholesale prices, particularly in mitigating risks to market stability and supporting efficient customer switching. We support Ofgem's assessment that it is in consumers' interests that suppliers are able to hedge responsibly for default tariff customers, and that mitigating unmanageable losses in a sharply falling market can help reduce the risk of disorderly exits and associated costs socialised via Supplier of Last Resort processes.

Ofgem's consultation outlines how periods of rapidly falling wholesale prices can result in suppliers being exposed to irrecoverable losses if customers switch to new products that reflect lower wholesale prices than those hedged under the price cap. This in part reflects the inability of suppliers to charge an exit fee for customers moving off SVT tariffs that reflects the economic loss incurred by the supplier, which would be a normal practice in other markets not subject to the same consumer protection considerations. In this context, an MSC could act as an important safeguard (and alternative to an exit fee) by moderating short-term pricing differentials and helping to maintain a level playing field across the market, supporting financially sustainable competition.

However, we note that the effectiveness of any MSC intervention will depend critically on Ofgem's ability to trigger the MSC in time. Given the speed at which customer behaviour and switching patterns can respond to changes in relative pricing, there is a risk that Ofgem's timelines may not be well aligned with retail market dynamics. We urge Ofgem to publish a decision on licence amendment as soon as possible following closure of this consultation, and to use the 56-day period before the licence condition takes effect to consult on activation.

We therefore consider that, while an MSC could provide an important tool for managing risks associated with falling wholesale prices, its effectiveness in practice will depend critically on the clarity, predictability, and timeliness of its activation framework. As drafted, there is a risk the licence condition signals protection but delivers it too slowly, reducing its practical effectiveness under the market conditions it is designed to address.

We support the proposed approach to licence drafting (proposed new SLC24A.2A and revised SLC24A.3/24A.4), including:

- that the provisions in Condition 24A shall take effect on a date specified by Ofgem publishing a statement;
- that the provisions shall cease to have effect on and from a date as may, following consultation, be specified by Ofgem in a subsequent statement; and
- the continued administration of the MSC through the Retail Energy Code.

Ofgem does not propose including a specific period before which the MSC may be activated following the published statement by the Authority. As wholesale prices have increased significantly due to the conflict in the Middle East, we would urge Ofgem to activate the MSC

at the earliest possible opportunity as the future trajectory of wholesale prices is highly uncertain.

Q2. Do you have any comments on the consumer impacts of an MSC?

We consider that, on balance, the reintroduction of a Market Stabilisation Charge (MSC) would be beneficial for consumers, particularly when assessed against the counterfactual of heightened market instability during periods of sharp wholesale price falls.

While some highly engaged consumers may lose out on the opportunity to take advantage of a reduction in wholesale prices, this is outweighed by the likely increase in system costs due to further supplier insolvencies or reduced investability and innovation. By reducing the risk of disorderly market exits and associated consumer harm, an MSC can help protect customers from longer-term detriment arising from supplier failures and market disruption. Even in relatively stable market conditions, the presence of an MSC as a contingent measure can increase suppliers' confidence to hedge prudently in line with the price cap methodology. This, in turn, supports more sustainable pricing outcomes for consumers over time.

There is, however, a risk that, if not well understood, an MSC could be perceived by some consumers as an additional charge that dampens the pass-through of falling wholesale prices. This risk is particularly acute given the heightened sensitivity to bill impacts following recent market volatility. Clear and transparent communication would be important to ensure that activation of an MSC is clearly explained and maintains consumer confidence and trust.

We agree with Ofgem that set-up costs for the central arrangements to make payments between suppliers and administrative costs are unlikely to be significant, especially as the Retail Energy Code Company (RECCo) has previous experience of implementing the MSC and has had the opportunity to draw lessons from its operation.²

We also agree with Ofgem's assessment that, relative to the counterfactual, an MSC may temporarily dampen switching. However, the extent of any such impact would be limited by design as the MSC would only apply in a context of sharply falling wholesale prices. We also agree that an MSC reduces the opportunity for suppliers to gain customers quickly but that the overall benefits of this kind of competition are unclear where customer acquisition is driven primarily by short-term market dislocations rather than by the provision of genuinely better products for consumers.

Finally, as Ofgem notes, an MSC may support competition over the longer term by reducing the risk of failure of otherwise viable suppliers during periods of exceptional market stress and improving the investability of the market. While it is not generally the role of economic regulation to prevent market exit, in the context of an energy crisis it is appropriate to consider measures that mitigate the effects of extreme market conditions where doing so is in the overall interests of consumers.

² [Reflecting on the conclusion of the Market Stabilisation Charge - The Retail Energy Code Company](#)

FEEDBACK ON MSC GUIDANCE AND MSC PARAMETERS

1. Introduction

Ofgem has indicated that it would welcome early feedback on the MSC guidance and on the specification of the MSC Parameters, which are not covered in the current consultation (paragraph 3.13). We welcome this opportunity, as the calibration of key MSC parameters is central to the effectiveness of the mechanism. The specification of key MSC parameters determine:

- the scale of the price fall which triggers the MSC; and
- the % of hedging losses beyond this point which determine the value of the MSC.

Ofgem's current expectation is that the parameters applied at the time the MSC lapsed would be retained if the mechanism were reintroduced. Ofgem has also indicated that any update to the MSC guidance would be consulted on. While we recognise the benefits of retaining the previous guidance in the interests of speed, we consider that aspects of the previous parameter design risk materially understating suppliers' economic exposure in falling markets.

Under the existing MSC design, the trigger and charge are based solely on movements in wholesale prices. However, this does not reflect any ex post adjustments that may have been used to allow suppliers to recover certain material and systematic costs over periods that may extend beyond a single cap period.

These additional allowances are recovered exclusively from SVT customers and do not form part of the cost stack for FTCs. As a result, when customers switch from SVT to FTC following a sharp fall in wholesale prices, suppliers face a real economic loss associated with the non-recovery of these lagged costs. Maintaining a sufficiently stable SVT customer base is therefore critical for effective cost recovery. On this basis, we consider that the MSC should be calibrated to reflect not only wholesale hedging losses, but also the broader economic exposure created by any deferred cost recovery under the price cap.

The previous design of the MSC did not offer sufficient protection to suppliers in falling markets. In particular, we encourage Ofgem to consult on the following targeted technical changes to the MSC parameters:

1. **Include ex post price cap adjustments** for deferred cost recovery in the calculation of both the MSC trigger and the MSC charge itself. Where such allowances are excluded, the MSC may fail to trigger despite suppliers incurring substantial economic losses through accelerated switching. Including these allowances would better align the MSC with the full set of costs that suppliers should be able to recover under the price cap framework. We provide more detail on this in section 2 below.
2. **Amend the format of the trigger** from the current percentage basis to an absolute £/MWh threshold. A purely percentage-based trigger risks activating the MSC only after the majority of customer switching has already occurred, particularly following periods of elevated wholesale prices where even relatively small percentage movements can equate to large absolute price changes. An absolute threshold would provide earlier and more predictable protection.

3. **Increase the de-rating factor** from 85%. We consider that this level of de-rating materially reduced the effectiveness of the MSC in protecting against hedging losses. We therefore encourage Ofgem to consult on increasing the recovery rate to at least 90%, and preferably closer to full (100%) recovery, to ensure the MSC provides meaningful protection in the circumstances it is intended to address.

2. Inclusion of ex-post price cap adjustments in MSC methodology

Ofgem has previously signalled that where costs are deemed “material and systematic”, ex post adjustments remain a tool under the price cap framework. Potential ex post adjustments could be positive or negative for suppliers and may arise from a range of issues, including:

- **Historical debt-related costs true-up (April 2022 – June 2025):** Ofgem is consulting on its review of the temporary debt-related costs allowance added to the price cap during the energy crisis. While Ofgem is not minded to introduce a further adjustment, this position could change following consultation responses, and the consultation notes the possibility of a new adjustment to future cap periods if the allowance is found to have been mis-calibrated when compared to outturn supplier costs.
- **Backwardation recovery following removal of the deadband:** Ofgem has decided to remove the backwardation deadband in the wholesale cost allowance and to allow qualifying backwardation costs to be recovered over a rolling 12-month period. Implementation is scheduled for cap period 16b (July–September 2026), which means previously unrecovered costs may flow through as lagged recovery, functionally similar to an ex post adjustment, which may be positive or negative.
- **Balancing Services Use of System (BSUoS) cap breach:** BSUoS costs are highly sensitive to system conditions, and actual outturns can diverge materially from forecasts within a charging year. Under the current arrangements, the NESO is able to reset BSUoS charges during a fixed period where it forecasts a material under-recovery of costs. Recent geopolitical instability has resulted in increased balancing costs accelerating the drawdown of NESO’s BSUoS Working Capital Facility. Latest forecasts indicate that this could be fully exhausted by October or November 2026, increasing the likelihood of a BSUoS reset and a need to recover costs ex post.

We believe these ex post allowances should be reflected in the MSC in two ways:

- **The trigger point:** if any substantive additional allowances are not included in the calculation of the trigger point this increases the risk that suppliers incur substantial economic losses as a result of customer losses without the MSC being triggered.
- **The level of the MSC:** the economic loss from non-recovery of ex post costs could be significant and should be reflected in the level of MSC.

If ex post allowances are included in the MSC methodology, we would suggest it should be done in a symmetric way. So if an ex post adjustment has a negative value, its inclusion may reduce the level of the MSC and may even prevent it from being triggered. However, the MSC should be subject to a zero floor to avoid the situation where a losing supplier is required to make a payment to the gaining supplier.