

September 2026

Energy Systems Catapult response to the Ofgem consultation on Supporting innovation in the electricity retail market: exempting small suppliers from the Universal Service Obligation (USO)

Contact: Tom Luff, tom.luff@es.catapult.gov.uk

Summary

The proposed exemption from the Universal Service Obligation for suppliers with fewer than 50,000 domestic customers is a small but welcome step towards greater regulatory diversity and should be the start of broader reform.

Energy Systems Catapult welcomes the opportunity to respond to this consultation.¹ We are an independent, not-for-profit centre of excellence established to accelerate the transformation of the UK energy system and help businesses and consumers capture the opportunities of clean growth. Working across industry, government, academia and research, we take a whole-systems approach to policy design and implementation, helping identify and address innovation priorities and market barriers to decarbonise the energy system at lowest cost.

Our key points in response to the consultation are:

1. This is a small but welcome step towards regulatory diversity. Exempting suppliers with fewer than 50,000 domestic customers from the USO is a sensible move that should make it easier for more specialised propositions and business models to enter and grow.
2. The ambition should go well beyond the USO. The proposed exemption should not remain an isolated carve-out. Ofgem should identify where regulation can be differentiated according to the functions businesses perform and the risks they create, including through activity- or project-based exemptions. This could enable specialist providers to deliver local energy, community energy or flexibility services alongside a customer's existing licensed supplier, rather than requiring every proposition to fit the traditional supplier model.
3. The test-and-learn approach is important. Ofgem should use the exemption to build evidence on innovation, competition, consumer choice and emerging risks, including how to mitigate risks to ensure vulnerable consumers continue to have reliable access to essential protections and suitable supply options.

We provide a response to the detailed consultation questions in the annex. We would be happy to further discuss this topic with you.

Sincerely,

Tom Luff (Head of Policy and Business Model Innovation)

¹ <https://www.ofgem.gov.uk/consultation/supporting-innovation-electricity-retail-market>

Response to detailed consultation questions

Q1. Do you agree with our proposal to exempt suppliers with fewer than 50,000 domestic customers from the USO?

We support the proposal but see it as a useful first step towards the more fundamental reform of retail regulation that will be needed.

We particularly welcome Ofgem's emphasis on enabling greater specialisation in the retail market. A future energy system with much greater consumer flexibility is likely to require a wider range of propositions, serving different consumer preferences and making better use of technologies such as EVs, heat pumps, batteries and smart controls. Requiring every supplier to be capable of serving every domestic consumer can create an unnecessary barrier to business models designed around particular technologies, services or customer needs.

Greater specialisation can benefit consumers directly, through propositions better tailored to their preferences and circumstances and indirectly by increasing competition and allowing new business models to enter the market, test propositions and scale-up.

We also strongly support Ofgem's test-and-learn approach. The 50,000-customer threshold provides a proportionate opportunity to test whether greater regulatory flexibility supports innovation and market entry while managing consumer risks. This should help ensure vulnerable consumers continue to have reliable access to essential protections and suitable supply options. The test-and-learn approach should be used to build an evidence base for further reform.

Ofgem should also consider whether supplier-level exemptions are sufficient. A complementary approach could allow defined activities or projects to benefit from differentiated regulation even where the specialist provider serves more than 50,000 customers across its activities overall. This could be particularly relevant where a specialist provider delivers a local energy, community or flexibility service alongside, rather than replacing, the customer's existing supplier.

However, reform should not stop with the USO. The current USO position is one example of a wider problem. A regulatory framework largely built around a traditional, full-service supplier model can make it unnecessarily difficult for alternative and specialist business models to participate.

Ofgem should therefore use the experience from this exemption to develop a more systematic approach to regulatory diversity. Different business models should be regulated according to the functions they perform and the risks and impacts they create for consumers, rather than being required by default to conform to the same full set of obligations designed for a traditional supplier.

The proposed exemption is therefore valuable not only because it removes a specific barrier, but because it provides an opportunity to demonstrate a broader principle. The next step should be to identify where other regulatory requirements unnecessarily constrain specialist propositions and consider whether differentiated requirements could enable greater innovation and competition while maintaining appropriate consumer protection.

Q2. Do you agree with our assessment of risks, and proposed mitigations?

Broadly, yes. The principal risks identified by Ofgem - including customer segmentation, impacts on competition, transition across the 50,000-customer threshold and incentives to avoid the threshold - are relevant, and that they appear manageable given the limited scale of the proposed exemption.

In particular, it is important that consumers continue to have access to universal supply through the wider market and that the exemption does not remove the other consumer protections applying to suppliers. Ofgem's commitment to monitor suppliers approaching the threshold and preventing corporate structures being used artificially to circumvent it is welcome.

However, Ofgem should be careful not to treat specialisation or differentiation between customer groups as inherently a consumer risk. This differentiation is also one of the principal intended benefits of the reform. Allowing businesses to develop propositions around particular technologies, consumer preferences or needs can increase choice and competition and enable propositions that would otherwise struggle to enter the market.

The key test should therefore be whether differentiation creates material consumer harm or undermines access to essential protections, rather than whether every proposition is available to every consumer.

We would also encourage Ofgem to evaluate the intervention against its positive objectives, not simply the absence of harm. This should include whether the exemption enables new entrants, increases the diversity of propositions, strengthens competition and supports greater consumer participation in flexibility.

Most importantly, the review should be used actively to inform the next stage of retail regulatory reform. The objective should not simply be to determine whether the 50,000 threshold has worked but also to understand what the experience tells us about where else regulation could be differentiated according to the activities undertaken and consumer risks created. This should include exploring activity- or project-based regulatory pathways and the market and settlement arrangements needed for specialist providers to deliver services alongside an the customer's existing licensed supplier.

The USO exemption should be the beginning of a more systematic move towards regulatory diversity, rather than an isolated exception to the existing supplier model.