

Nesta response to Ofgem consultation - Supporting innovation in the electricity retail market

Question 1: Do you agree with our proposal to exempt suppliers with fewer than 50,000 domestic customers from the USO?

Yes, Nesta supports this proposal.

Innovation is vital to the energy retail market and reaching the UK's net-zero targets. In our 2024 report, [*Future of energy retail: how could the electricity retail market be designed to better support net zero delivery?*](#), Nesta explored how the current regulatory framework can limit the ability of new business models to enter the market and scale flexibility services. We view the removal of the Universal Service Obligation (USO) under Standard Licence Condition (SLC) 22 for smaller suppliers (fewer than 50k domestic customers) as a proportionate, low-risk, and constructive measure to lower market entry barriers and foster a more dynamic retail landscape.

Our support is based on the following key observations drawn from our research:

1. Encouraging business model innovation and specialisation

Under current rules, while established suppliers can restrict eligibility for specific tariffs (e.g., heat pump or EV tariffs), they are still required to maintain full operational and billing infrastructure to serve any standard customer who requests supply under the USO. Exempting smaller suppliers from the USO removes the burden of building extensive customer service, standard billing, legacy meter support, and debt management systems tailored for general or non-smart consumers. This would enable agile entrants to hopefully specialise in specific segments, such as bundled heat pump installations, dynamic automated demand response, or energy-as-a-service, accelerating the adoption of low carbon technologies.

2. Lowering capital and regulatory entry barriers

We recognise that the upfront capital required to prove operational readiness for the entire GB domestic population is a major barrier for innovators. By relaxing the USO for suppliers under the 50k threshold, Ofgem creates a safer environment for new entrants to test novel customer propositions without taking on disproportionate fixed overheads.

3. Market spillover effects:

We anticipate that these localised or specialised innovations will not harm the wider market. Rather, successful consumer propositions tested by agile, exempt entrants can

demonstrate commercial viability, encouraging incumbent suppliers to adopt similar business models and driving healthy market competition.

While Nesta advocates that Ofgem consider more radical, structural reforms to the retail market in the long term, we consider this consultation's proposal to be a sensible, immediate step within the current market architecture.

Question 2: Do you agree with our assessment of risks, and proposed mitigations?

Yes, Nesta agrees with Ofgem's risk assessment and proposed mitigations.

The proposed framework strikes an appropriate balance between enabling innovation and preserving essential consumer protections, and the 50k limit prevents the risk of retailers cherry picking consumers and distorting the market.

The requirement for growing suppliers to prepare for full USO compliance as they approach the 50,000 threshold ensures that market expansion is accompanied by appropriate operational capability, preventing sudden service failures or regulatory compliance gaps.