

To all interested parties,

Future supply market arrangements – response to our call for evidence

In November 2017, we published a call for evidence asking stakeholders whether the current regulatory arrangements that govern the retail energy market will best serve the needs of future consumers, or whether these will need to change in light of the significant technological change already affecting the sector.¹ Following consideration of respondents' views we now consider there is a strong case for fundamental reforms to be explored. This letter provides a summary of the evidence we received and sets out our conclusions on what changes need to be considered further. It also sets out the next steps we will be taking in line with our conclusions.

Context

Our ambition is a retail market that works for all consumers, both today and tomorrow. It is a market that helps drive the full benefits of the energy transition², with greater system efficiency helping to lower overall costs. It is a market where competition constrains prices, drives efficiency and delivers the range of services and products that consumers need. And it is a market where disengaged consumers are also able to share in the benefits of competition.

Too many consumers are not seeing the full benefits of competition. That is why we are consulting on the introduction of temporary price protection for domestic customers on default tariffs.³ In parallel, we are also taking steps to promote competition and consumer engagement, as in the long-term a competitive market will get the best outcomes for consumers. At the moment, barriers to innovation – like access to data, complexity of industry codes and the entrenched role of traditional suppliers within the energy system – mean that it can be difficult for market participants to bring beneficial, and potentially disruptive, propositions to market.

¹ Ofgem (2017) [Future supply market arrangements – call for evidence](#).

² Our overall aim is to ensure there is a regulatory framework that drives innovation, supports the transition to a low carbon energy system and delivers the sustainable, resilient, and affordable services that all consumers need. The challenges and opportunities we expect the energy system transition to present, and the priority actions we are taking, are outlined in: Ofgem (2017) [Our strategy for regulating the future energy system](#).

³ Legislation which requires Ofgem to design and put in place a temporary cap on all standard variable tariffs and fixed-term default tariffs received Royal Assent on 19 July 2018. Consultations can be found on our [website](#).

Programmes like smart metering, half-hourly settlement, faster switching and our Innovation Link⁴ will do much to modernise the market, drive greater innovation and deliver better consumer outcomes. Off the back of this work, technological advancements like microgeneration, energy storage, electric vehicles and smart appliances will increasingly mean that consumers can start engaging with their energy supply in new and exciting ways. But these opportunities – and the consumer protection challenges they present – were not fully understood when the market was originally designed some 20 years ago.

Now is the time to take a step back and consider whether the regulatory framework underpinning this market is fit for purpose. We must ensure that the extensive work we are already doing to improve outcomes for today's consumers continues at pace. Looking beyond this, into the longer-term, we must also ensure that consumers remain protected no matter how they engage in the market, and put in place arrangements that meet the needs of all consumers – including the vulnerable.

What our call for evidence asked for

We have seen increasing evidence (including via the engagement we have with innovators through our Innovation Link and previous consultation on non-traditional business models⁵) that aspects of the current 'supplier hub' model have been getting in the way of innovation and competition. We call this the 'supplier hub' because the supplier is positioned as the primary intermediary between consumers and the energy system. With this position comes a wide range of social, operational and commercial roles and responsibilities that have become entrenched in legal frameworks, licensing arrangements and industry rules. For consumers, it means they are obliged to access the energy system through a licensed supplier, with these firms recovering costs arising through their energy use.

In the context of a rapidly evolving retail market – and the growing potential for consumers to engage with their supply and benefit from innovation in new and exciting ways – our call for evidence asked for views on the following:

- **Are the current supplier hub arrangements fit for purpose?** Will they deliver our overall objectives in the context of the rapid change in technology and business models we are seeing and expect into the future? Are there any barriers to innovation?
- **Where should any regulatory change be focused and why?** Is fundamental change required or can the current supplier hub model adequately adapt? And, if changes are required, what would this mean in practice and what impact would this have on consumers, including the vulnerable?
- **How can any changes to the supplier hub model best align with and ensure wider market activities continue to be performed efficiently?** This included things like balancing and settlement activities and recovery of network costs.

More specifically, we also sought views on four areas: (1) proposed **guiding criteria** to evaluate a successful supply market; (2) the most significant **barriers to innovation** for disruptive new business models operating in the retail market; (3) **alternative default arrangements**⁶ for disengaged consumers (ie other than retail price regulation), to

⁴ Ofgem's [Innovation Link](#) is a 'one stop shop' offering support on energy regulation to businesses looking to introduce innovative propositions to the energy sector. We want to support ideas that bring benefits to consumers. This also helps us understand emerging trends in the sector and identify areas in which our regulation may need to change to sustain innovation.

⁵ Ofgem (2015) [Non-traditional business models – supporting transformative change in the energy market](#).

⁶ These are the arrangements in place to ensure that consumers are always able to access supply and protected, regardless of their level of engagement.

ensure these consumers are protected adequately; and (4) whether it is an issue that we do not currently regulate **intermediaries⁷ in the energy market.**

Stakeholder views

We thank all of those who have taken the time to attend workshops, speak with us bilaterally and provide us with written responses. The appendix to this letter summarises the evidence we have received. Research and consumer testing conducted throughout this evidence-gathering phase has also been published on our website.⁸

We note that, given the early stage of this work, much of the evidence we received was high-level and pointed to broad issues with current market arrangements. However, from the evidence received, most stakeholders agreed that a review of the supplier hub model is timely. They told us that change needed to be considered because of the following issues:

- There is growing potential for innovation in technology and business models to transform the market and improve the consumer experience, but aspects of the supplier hub model are hampering the realisation of benefits. For example, one stakeholder considered that current arrangements are based on a single supplier settling system costs on behalf of a consumer, and this is a blocker for business models that rely on transactions from multiple parties occurring at a single meter point.⁹
- Rules that impose a multitude of roles and responsibilities on licensed suppliers have evolved around the supplier hub model. These rules – which include those in the supply licences and codes – can be extremely complex, difficult to change and can present constraints for propositions that do not align neatly with traditional ‘supplier’ business models and tariff offerings. All of these issues create difficulties for innovators who need to obtain a supply licence in order to bring unique propositions to market.
- Data is likely to be a key enabler of innovation in the future market, as it could enable new products and services that not only challenge the primary relationship suppliers currently have with consumers, but also allow system costs to be better managed. However, the data currently available to licensed suppliers can be difficult for other market participants to access, is often of poor quality, and is fragmented across the sector. This can make it hard for innovators to develop propositions that could drive greater competition and improve system efficiency.
- Currently, most of our consumer protection framework¹⁰ is designed to manage risks posed by the traditional ‘supplier’ business model. The continued emergence of new types of third party intermediaries (TPI) and services mean that protections need to evolve so that risks to consumers can be managed in an effective and proportionate way, without creating an uneven playing field or unnecessarily constraining innovation. Many stakeholders considered that our move to principles-based regulations, rather than prescriptive rules, is a welcome step and should continue.

Although most stakeholders highlighted some fundamental issues with the current arrangements and called for reform to be considered, they also emphasised that significant

⁷ Intermediaries are typically third-party organisations or individuals that give energy related advice, aimed at helping consumers to buy energy and/or manage their energy needs. Third Party Intermediaries can include switching sites, energy brokers and any company that offers support with energy procurement. In our call for evidence, we note that, as the market evolves over time, intermediaries could also include other types of energy ‘suppliers’ (and associated service providers).

⁸ Ofgem (2018) [Future supply market arrangements – response to our call for evidence](#) (subsidiary documents) and Ofgem (2018) [Consumer First Panel, year 9, wave 3, Future Energy Markets](#).

⁹ Business models that could benefit from multi party settlement could include Electric Vehicle (EV) manufacturers wishing to sell energy to car owners, or peer-to-peer trading platforms looking to enable consumers to buy another household’s excess solar energy. We note that Elexon recently published a [white paper](#) on a potential approach for allowing multiple suppliers at a single metering point. We also note that Ofgem’s work concerning faster switching and half hourly settlement is considering how to make sure any system changes made as part of these reforms is not an impediment to such business models over time.

¹⁰ By ‘consumer protections framework’ we mean the system of rules and enforcement powers which supports us in protecting the interests of consumers, including those who are vulnerable, in the retail market.

changes to the supplier hub model cannot be made lightly. For example, some stakeholders considered that the current model has provided important benefits as it ensures consumers know who is accountable for their supply, and who to contact when things go wrong. Many stakeholders also told us that we must continue to ensure that there is some form of 'default' supply that all consumers can easily access if they choose to (or need to).

Some stakeholders thought we should hold off on major reforms (particularly regarding default arrangements), until we could assess what impact the work already underway with industry (such as smart metering and faster switching reforms, and work to encourage consumer engagement) has had on consumer participation and competition in the market. There were also views that any major changes to market arrangements could be costly for industry, and therefore consumers, particularly given the significant reforms already underway. Subsequently, several stakeholders also agreed that a robust assessment of the impacts of any potential reforms will need to be undertaken.

Our conclusions

We consider that the current supplier hub model may not be fit for purpose for energy consumers over the longer term. Specifically, we are not confident it will enable consumers to benefit fully from the greater levels of innovation, digitalisation and competition made possible by the energy system transition. We are also not convinced that the consumer protections framework in place under the current supplier hub model will be able to ensure existing and emerging risks are effectively managed into the future. Therefore, we have concluded there is a strong case for considering fundamental reforms to the supplier hub model, and for evaluating how alternative arrangements might operate in practice.

We need to make sure that any future retail market design can unlock the full potential for innovation and competition, over the longer term. Given the scale of change we are seeing in the sector, we consider that seeking to adapt a model put in place 20 years ago may not be enough. While the most significant innovation opportunities are materialising in the electricity market, it is likely that fundamental reforms would also need to be considered for gas supply. This would ensure as much regulatory consistency exists in these markets as possible.

The scale of the potential consumer benefits from innovation and competition on offer in the retail market over the longer term is large, and there could be significant lead-times involved in moving to any potential alternative retail market model. For these key reasons, we do not feel it would be prudent to wait for existing reforms to be completed, before exploring how further improvements for consumers could be delivered. Instead, we consider that reforms to the supplier hub model could help to optimise the benefits of other reforms already underway, including our work aimed at improving consumer engagement levels in the current market. We remain committed to doing this – including through our supplier-customer communication rule changes¹¹ and improving prompts used to engage those on default tariffs.¹²

We also appreciate that we will need to assess rigorously the impacts of any significant reform options. We will ensure that any reforms are proportionate and do not jeopardise the successful and timely completion of other retail market reforms, such as the smart meter rollout, half-hourly settlement and faster switching programmes.

¹¹ Ofgem (2018) [Domestic supplier-customer communications rulebook reforms](#).

¹² Ofgem is currently exploring consumer response to an '[Active Choice](#)' collective switch model. In this trial, disengaged customers are offered a collective switch tariff and then choose whether or not to switch, either to the collective switch tariff or one from the open market. Results will be published later in summer 2018.

Areas of focus moving forward

Reforming the supplier hub model

Having concluded that fundamental reforms to the supplier hub model need to be explored, we will now work to assess and, where appropriate, redesign the retail energy market. This will include work to understand how the unbundling of functions from current suppliers – as mandated by the supply licence, codes and related legal frameworks – might stimulate more innovation and competition.¹³ It will also require thinking about how the mechanisms used to pass-through system costs to the consumer can enable different types of business models to compete. At the moment, firms that are not able or willing to conform to the supplier-hub model cannot easily access the mechanisms that allow them to pass through underlying costs to consumers. This could be preventing higher levels of innovation and competition that benefits consumers.

In parallel to considering how the current supplier hub model may need to be reformed, we will also be exploring how the retail market arrangements that have emerged around this model may need to change – so they remain fit for purpose into the future. Specifically, we are keen to investigate what reforms might be necessary to ensure:

- The obligations placed on firms seeking to supply energy to consumers, including supply licence rules and industry code arrangements, are not preventing innovative propositions that could engage and add value to consumers from making it to market.
- The availability, accessibility, quality and consistency of data across the energy sector improves. This will help ensure market participants have appropriate opportunities to use data in a way that engages consumers and increases overall system efficiency.
- The consumer protections framework is appropriately targeted, proportionate, and flexible to change. This was seen as being particularly important given the growing prominence of intermediaries participating alongside traditional suppliers, in both the domestic and non-domestic retail energy markets.

To ensure we are acting as quickly as possible in progressing any fundamental reforms, while also taking into appropriate account the changes already underway across the energy system, it is likely that any new reforms will need to be iterative, and approached in phases. Over the coming weeks and months we will engage a range of stakeholders on (1) our objectives for reform in these areas, (2) the new market design options that could be explored, and (3) specific implementation approaches that could be adopted. As changes to supplier hub arrangements could interact with wider energy policy outside of Ofgem's direct control or remit, we will be seeking the views of government on areas of shared interest before progressing any reform options.

Alternative default arrangements for the disengaged

Energy is an essential service and we need to ensure all consumers can access a reliable supply of gas and electricity at a reasonable price, with an appropriate level of service. The default tariff cap being consulted on aims to extend price protection to all consumers who do not engage in the market frequently, but government legislation sets out that this is a temporary measure (until 2020 with the ability to extend once a year until 2023). We will continue exploring options that ensure consumers on default arrangements are appropriately protected over the longer term. A research report, looking into some of the different default arrangements and approaches used internationally has been published alongside this document.¹⁴

¹³ On page 5 of the [call for evidence](#) we set out a range of functions suppliers currently perform. These include (but are not limited to) customer service, metering, cost recovery, risk management and social obligation functions.

¹⁴ For the avoidance of doubt, we note that this research does not necessarily reflect the views of Ofgem. It is evidence that we will scrutinise as part of our ongoing work on alternative default arrangements.

Consumer protections for intermediary activities

In the call for evidence, many suppliers and consumer groups expressed concern about the detriment that poor conduct from intermediaries can create for consumers, and the more limited protections that apply to these activities. Stakeholder concerns were most pronounced in relation to TPI's dealings with microbusinesses, with some calling for Ofgem to more directly regulate these activities.

We agree with stakeholders that intermediaries are already playing a prominent role in the market, and this can lead to risks for domestic and non-domestic consumers. With this in mind we have expressed strong support for government's recent Consumer Green Paper proposal to extend consumer law fining powers to sectoral regulators so that domestic consumer protections are strengthened, and we have additionally proposed that this also be extended to non-domestic protections.¹⁵ We are engaging now with government to explore how additional powers to enforce consumer law that protects microbusinesses could help us to tackle misconduct from intermediaries in this part of the market. We consider that this approach will help us more easily take action where needed.

As part of our consideration of more fundamental reforms to the supplier hub model, and associated retail market arrangements, we will carefully consider how the scope and form of our regulation may need to change in the longer term. We are determined to ensure that the interests of both domestic and non-domestic consumers are protected when dealing with existing and new types of intermediaries in the future retail market.¹⁶

Near-term actions to promote innovation and competition

We are keen to develop, consult on, assess and implement any fundamental reforms in the aforementioned areas as quickly as possible – while recognising that these reforms are likely to be significant and complex. To move this forward at pace we will look to implement changes iteratively and in phases, building on other market reform programmes already underway.

However, we are also keen to unlock greater innovation and consumer benefits in the near-term. We will therefore be immediately taking actions intended to reduce some of the key barriers to innovation and competition within the current market. Our package will focus on three of the priority areas identified by stakeholders: (1) improving customer access to data, (2) reducing code complexity, and (3) assisting innovators to enter the market and test propositions. The near-term actions we are taking are:

- **Enabling customer data access** – We will draw on the evidence gathered and policy development undertaken so far as part of government's midata initiative, to accelerate new arrangements that make it easier for consumers to share their data easily and securely with energy service providers. We have published an open letter that sets out our intent to act in this area and delivers a call to action to the energy sector.¹⁷ We will be holding a series of events that give people an opportunity to feed into and shape a data access solution over the coming months.

¹⁵ Government has announced that it intends to introduce legislation to give civil courts the power to impose financial penalties on companies for breaches of consumer law. See Department for Business Energy & Industrial Strategy (2018) [Modernising Consumer Markets – Consumer Green Paper](#), pp. 59-60. Our response to this green paper is available at: Ofgem (2018) [Ofgem's response to government's consumer green paper – modernising consumer markets](#).

¹⁶ We will take into account past work that has considered how the scope of our regulatory powers might need to evolve – including relevant lessons from other regulators. We note that the CMA has recommended that government look to bring intermediaries like digital comparison tool providers within the scope of Ofgem's formal regulatory powers (see: CMA (2017) [Digital comparison tools market study – Final Report](#)). The CMA has also recently announced recommendations regarding heat networks, including that a statutory framework be set up that underpins the regulation for this sector (see CMA (2018) [Heat Network Market Study – Final Report](#)).

¹⁷ Ofgem (2018) [Enabling customer data in the energy market](#).

- **Improving retail code arrangements** – We will aim to simplify the regulatory landscape by exploring how to accelerate the consolidation of relevant industry code provisions into the Retail Energy Code.¹⁸ Importantly, this will mean that more code provisions are located in a single space and subject to ‘best-in-class’ governance arrangements that are better at safeguarding the consumer interest – by promoting innovation and competition. We are engaging with industry to see how quickly this can occur. Our ambition is to have achieved full consolidation as soon as possible after, if not at the same time as, go-live for new switching arrangements (currently planned for the end of 2020).
- **Enabling more seamless market entry for innovative propositions** – We are keen to develop a framework that better enables innovators with disruptive propositions that benefit consumers to enter the market (within the existing licensing framework and code arrangements). This will build on lessons from our work to enable innovation via the Innovation Link regulatory sandbox.¹⁹ As part of our commitment to accelerating how we develop policy, in August we will undertake a discovery exercise with innovators which will ensure we better understand their experiences in trying to enter the market and have clearly articulated their user needs. This will then inform the design of the potential solution(s) to support them, and allow us to move more quickly to formal policy consultation on detailed proposals in autumn 2018.

We expect all of the above actions to create opportunities for more disruptive innovation within the current market model, while teaching us lessons that can help us as we develop more fundamental, longer term, reforms.

Next steps

Over the summer and autumn, we will give stakeholders more detail on how we will take forward our near-term actions, as well as how we will progress the development of more fundamental reforms. Given the potential linkages with wider energy system work and the potential for more effective joined-up working, we will be engaging with government to link in with other policy initiatives, where it would be appropriate.

We encourage all stakeholders to embrace the challenge that improving retail market arrangements represents, and continue engaging with us on this work. To ensure we are developing robust reforms, we will look to engage with stakeholders in new ways, to ensure they are able to shape proposals as our thinking develops.

If you would like to discuss the initial proposals outlined in this letter, or our general direction of travel, please do not hesitate to get in contact with the team at FutureSupply@ofgem.gov.uk.

Neil Barnes
Deputy Director
Consumers and Markets, Ofgem

¹⁸ For more information on the Retail Energy Code, see: Ofgem (2018) [Switching Programme: proposed modifications to regulation and governance](#).

¹⁹ Ofgem’s [Innovation Link](#) regulatory sandbox is designed to allow innovators to trial innovative business propositions that will benefit consumers by temporarily lightening regulatory requirements. This provides a single point of contact for innovators wishing to explore sandboxes. However, we recognise that a joined-up approach across the industry is required to support innovation. Code administrators have recognised this as well, and have drafted a new Code Administrators Code of Practice principle to jointly support innovation. Elexon, code administrator for the Balancing and Settlement Code, has also raised a modification to allow for a sandbox, which will further enable a joined-up process for testing innovative ideas in the sector.

SUMMARY OF STAKEHOLDER EVIDENCE

Context

This appendix summarises the key themes in the responses to our call for evidence, as well as feedback we received during stakeholder meetings and workshops. It does not necessarily represent the views of Ofgem.

We received a total of 48 responses to our call for evidence.²⁰ We held over 50 bilaterals and presented at a number of workshops with stakeholders. We also talked to consumers on how they felt about different default supply arrangements and how they may engage in a future energy market where they buy their energy in different ways.

Through the call for evidence itself, we specifically sought stakeholder views and evidence on:

- appropriate guiding criteria for potential reforms
- barriers to innovation
- alternative default supply arrangements for consumers that do not engage in the market
- protection for all consumers regardless of how they access their energy supply.

The questions put to stakeholders and the key themes in their responses are set out below.

Question 1 – What are your views on the below criteria? Are there other criteria that should guide our assessment of current and possible future market arrangements?

- a) Consumers can access energy supply and energy services however they choose to do so, without undue restriction.
- b) Consumers that do not actively engage in the energy market still receive a good quality of service and pay a reasonable price for their energy.
- c) Consumers, including the vulnerable, are adequately protected no matter how they access energy services.
- d) Bearing in mind relevant data protection regulations, there are no undue barriers for consumers and wider market participants seeking to share access to their energy system data with other market participants.
- e) Firms offering intermediary and other services to consumers can compete on an equal basis.
- f) Costs of operating the energy system are recovered in a cost-reflective manner, and risks allocated and managed effectively.

The call for evidence set out six preliminary 'guiding criteria' that could steer the development of future supply market arrangement reforms. The criteria were broadly supported by stakeholders, although useful insights were provided regarding how they could be adapted to reflect some additional dimensions of the energy market, and clarify their intent. For example, some stakeholders said that we should be careful not to imply that firms offering supply in the future must offer 'all things to all people,' and that we should be clear that we are seeking to ensure competition between all firms, not just intermediaries, can occur on an equal footing. Ensuring transparency of data flows, and incentivising consumer engagement (alongside consumer protection) were also highlighted as needing greater emphasis.

Several responses highlighted tension between the aims of seeking to adequately protect consumers and promoting diversity of business models and innovation. It was noted that innovation could potentially lead to a range of new products and services, thereby enabling

²⁰ Non-confidential responses to the call for evidence are available on our [website](#).

consumers to make more sophisticated choices that provide them with benefits. However, greater sophistication would then almost certainly make the market feel more complex to some, risking further disengagement. Conversely, if the market is designed for maximum protection, we may miss out on the wider benefits from engaging consumers with new products and services.

Stakeholders also called for us to be clearer on who should be protected, and from what. Several stakeholders pointed to the need to regulate energy services or activities, rather than specific market participants, and that this focus on services should be reflected in the criteria. There was broad agreement that all consumers should be able to access a safe and reliable energy supply, no matter how they engage. There was also agreement that energy is an essential service and as such, should be affordable with adequate standards of service provided. Some respondents argued that because energy is an essential service, consumers shouldn't be required to engage in a complex market unless they really want to.

Question 2 – What are the most significant barriers to disruptive new business models operating in the retail market? Please draw a distinction between regulatory barriers and commercial barriers (eg there may not be enough potential consumer demand to justify market entry).

Below are the key themes stakeholders raised regarding barriers to new business models and innovation in the retail market. The barriers identified across stakeholders were:

- regulatory complexity and code arrangements,
- difficulties accessing data, and
- the centrality of the traditional supplier within market arrangements (which often means that innovators must either partner with a supplier or become a supplier in order to bring new propositions to market).

During the call for evidence, we also commissioned independent research into some of the non-traditional business models in energy markets outside the UK. A report and case-studies, which may contain views that do not necessarily align with those of Ofgem, are published alongside this letter.²¹

Regulatory complexity and code arrangements

Regulatory complexity was identified as a barrier to innovation in most stakeholder responses. For example, many respondents considered that the complexity and breadth of the supply licence and the fragmented and distributed ownership of code provisions was a significant problem for existing and prospective market participants. There were views that this status quo can make it difficult to identify who regulates what in the market.

New entrant suppliers in particular considered that understanding the linkages between a variety of licence obligations, codes, market participants and IT systems was a big challenge. This complexity can make it difficult for them to direct enough resources towards developing and executing innovative propositions that are significantly different to the traditional supplier offering. Barriers to innovation was the focus of a workshop discussion held with smaller suppliers at the recent Independent Suppliers Forum. The overriding theme from this discussion was the detrimental effect burdens from regulatory complexity and code arrangements has on their ability to innovate.²²

In tackling the issue of code complexity, a couple of stakeholders emphasised their support for the proposed creation of the Retail Energy Code, but wanted to be assured that this initiative would result in a reduction of the overall number of codes and simplify the regulatory landscape. At the Independent Suppliers Forum, it was noted that the Retail Energy Code presents an opportunity to rectify problems with codes and enable more

²¹ Ofgem (2018) [Future supply market arrangements – response to our call for evidence](#) (subsidiary documents)

²² Ofgem (2018) [Ofgem-BEIS Independent Suppliers Forum 18 May 2018](#).

innovation from smaller suppliers. In relation to code governance arrangements, stakeholders noted that some codes have voting systems based on number of meter points supplied, which does not allow all participants to exercise an equal and balanced level of influence over changes to codes. Some considered that this could be hindering innovative changes proposed by new entrants with relatively small customer bases.²³

More generally, the perceived lack of regulatory and policy direction for the future of the energy sector was identified as a barrier. High uncertainty about what rules might apply in the future can either prevent investment entirely, or make it more expensive to develop new products (as this risk can increase costs).

Data access

Access to data was identified as a significant barrier to innovative proposals reaching the energy market. For example, one response highlighted peer-to-peer transactions as an example of an innovation being hindered by poor data access. Another stakeholder thought that incumbent suppliers being a gateway to metering data prevents others from delivering innovation that could benefit consumers. While stakeholder views were mixed regarding what changes might be required to data management systems, most agreed that issues with data access must be tackled as quickly as possible – especially in order to unlock benefits from energy, capacity and flexibility services on the network.

Initiatives that enable customers to have clear and unfettered access to their data, and grant others access, was highlighted as a priority. The midata initiative conceived by government was singled out for support by some stakeholders, as it would allow a customer to grant access to a third party that required the data for a particular service.

Some respondents suggested solutions to better enable data flows elsewhere in the energy system (ie between market participants). One respondent noted that Norway has an energy market data hub that market participants can use to facilitate data transfer. Another respondent urged Ofgem to champion a modern, data-driven energy system, and not be constrained by current technical requirements – as they considered this will perpetuate issues with data quality and likely favour large incumbent service providers.

Several stakeholders considered that the digitalisation of the energy sector will make data protection increasingly important to market performance and consumer outcomes. They considered that these protections must balance the need to both enable innovation and manage risks to consumers. A number of responses also considered that the sector's general approach to data access arrangements, privacy and cyber security will be critical to ensuring consumer trust and active engagement in a smarter, more digital market.

Centrality of the supplier

The central role the supplier is mandated to fulfil under the current 'supplier hub' market model was identified as a significant barrier to disruptive business models and innovation. A consequence of this has been that the current framework can force innovators to partner with suppliers in order to access parts of the market, or result in them needing to water down their ideas or not enter the market at all. Ofgem's regulatory sandbox was seen as a welcome step towards challenging this reality. The Licence Lite policy framework was also identified as a good concept, but one that could be simplified to ensure that innovators can more easily access the market.

Conversely, some stakeholders considered that many of the roles market players must fulfil in order to undertake supply have been put in place for very good reasons, and felt that it

²³ In our [2018-19 Forward Work Programme](#) we committed to improving the functioning of the industry code arrangements, including by developing a 'strategic direction' to guide code panels and code administrators on priorities and coordinated working, and the establishment of a cross-code oversight board. In order to focus on the most urgent areas of our FWP, we will not be progressing this work until the end of the year.

was right for different business models to conform to these rules. For example, applying rules which ensure transparent recovery of costs were highlighted as being necessary for all parties involved in energy supply. Many stakeholders stressed to us that market arrangements needed to not only prevent new market participants from avoiding costs, but also stop them from avoiding responsibilities for managing risks to the effective operation of the energy system.

An academic who responded observed that industry have invested large amounts of money in creating and operating a wholesale market and balancing system that results in consumers facing a price signal that bears no relation to marginal costs. They considered that smart meters, decentralised generation, growth in Electric Vehicle (EV) ownership and smarter appliances is creating opportunities for the more economic delivery of energy to the customer. The main challenge of any supplier hub reforms was therefore to get existing and new market players to buy into a new market model that ensures the benefits of a more efficient energy system reach the consumer in a manner that does not jeopardise the security and safety of supply.

Some respondents observed that various legacy issues within the market mean that it is currently structured to favour those with the economies of scale to take on these responsibilities, thereby making it difficult for smaller retail market participants to introduce innovative products and gain a foothold in the market. It was noted that the processes in place for changing and influencing the supplier hub market model can also favour those who are able to resource large compliance teams.

A few stakeholders drew our attention to the fact that supply licences are based largely around the one definition of 'supply' (and related provisions) set out in legislation. It was thought that we may need to consider how this definition should change so that it keeps pace with the technological developments seen within the energy system. At the moment, it was thought that this definition may be blocking new, innovative business models that could benefit consumers. There were also calls for Ofgem to carefully consider whether enabling radically different business models, such as those that rely on multiple supply at a single metering point, would be practical and/or result in a positive consumer experience.

Question 3 – What other supply market arrangements would provide a better default for disengaged consumers, whereby they are protected adequately and are able to access the benefits of competition?

Importance of default arrangements and protecting disengaged consumers

Respondents recognised the importance of having default 'access to supply' arrangements²⁴, particularly in the context of ensuring that the Universal Service Obligation (USO) was upheld.²⁵ They thought there will always be some consumers who cannot or will not engage in the market, and these consumers should be protected through the USO.

With respect to default arrangements to ensure that disengaged consumers (specifically) are not worse off, several respondents emphasised the need to continue focusing on driving improved engagement in today's market – for example by improving prompts to engage. During the call for evidence, we also commissioned independent research into default supply arrangements deployed in other international markets. A report and case studies, which may contain views that do not necessarily align with those of Ofgem, have been published alongside this letter.²⁶ Separately, we also engaged with consumers (via our

²⁴ These are the arrangements in place to ensure that consumers are always able to access supply and protected regardless of their level of engagement

²⁵ Because electricity and gas supply are essential services, suppliers are expected to provide minimum levels of customer service and offer universal supply.

²⁶ Ofgem (2018) [Future supply market arrangements – response to our call for evidence](#) (subsidiary documents).

Consumer Panel) to seek their views on potential default supply arrangements. We have published their views alongside this letter.²⁷

Alternatives to current default arrangements

Few respondents put forward alternatives to the current default arrangements. Of those that did:

- One supplier suggested that a supplier's standard variable tariff's prices should be capped at no more than 6% above its cheapest deal. This could protect the disengaged and allow suppliers to compete on price.
- One supplier suggested that another entity could provide the universal service function, and that customers could be transferred to this entity if they did not choose to remain with their current supplier. The entity could provide this role for a limited period of time. Entities could also bid via an auction to provide the default service.
- One aggregator suggested that Ofgem (or another independent body or panel) could create an index that ranks companies based on their procurement of low carbon energy, innovation in business models and low bills for consumers. Companies would be granted business tax relief on a sliding scale, with those highest in the index securing the biggest percentage of relief. The default tariff would be provided by the companies highest in the index, and disengaged consumers would be transferred to them unless they opted out.
- One aggregator suggested that blocks of default tariff customers could be auctioned to the supply market. An independent panel would assess the bids against the criteria used to form the index.

Views on opt-out collective switches

While some respondents were attracted to an opt-out collective switch model, all that commented on this highlighted legal and practical implementation difficulties. The large suppliers in particular expressed significant concerns. Issues raised by stakeholders included:

- Unless there is substantive legislative change, it would be difficult for customers to be allocated a new supplier without their knowledge and acceptance of the new terms and conditions.
- Removing the choice from consumers suggests that others know what is best for them, which may lead to complaints.
- Disengagement could increase, as consumers come to expect that they will always be on a good deal.
- Consumers switched away to another provider could in turn be exploited by that provider due to their 'sticky' nature.
- Opt-out collective switches would aim to secure the best price, but consumers can also value non-price factors. For example, they may be willing to pay more for good service.

Question 4 – How big an issue is it that we do not currently regulate intermediaries in the energy market? Is there a case for doing so? If so, how would we best do it? We are especially interested in frameworks that enable a wider variety and increased number of market participants to provide supply.

Intermediaries in today's market

Some respondents noted that third party intermediaries (TPIs) are the catalyst for some of the innovation seen in the market today and are increasingly challenging the position of the

²⁷ Ofgem (2018) [Consumer First Panel, year 9, wave 3, Future Energy Markets](#).

supplier as the primary intermediary between the consumer and energy system. Several respondents considered this situation can create risks, and consumer groups in particular were clear about wanting consumers to receive equal protections, no matter how they engage with the market. These stakeholders also had a strong desire for Ofgem to be proactive in how it manages the risks newer types of market intermediaries (such as switching or peer-to-peer platforms) could pose for consumers.

Several stakeholders were vocal about the need for regulation to address issues with TPIs offering brokering services in the non-domestic market.²⁸ Many considered that the majority of these TPIs provide material benefits to consumers, however it was also noted that serious problems for consumers can arise as a result of aggressive sales conduct, a lack of transparency on product offerings, poor complaint handling and the misuse of industry data. A view expressed about TPIs more generally was that the status quo – whereby TPIs either do not face sectoral regulation, or are regulated by proxy through a licensed supplier – is already distorting competition and creating consumer protection risks. Of particular concern to suppliers was the growing prevalence of TPIs who are managing a direct relationship with a consumer, without being accountable for consumer-facing obligations in the supply licence that provide valuable protection.

Rationale for change and options to consider

Several stakeholders highlighted that a lack of direct regulation created two fundamental issues:

- Gaps in protections - Consumers who use TPIs may face a lower level protection compared to those that engage primarily with a licensed supplier, and therefore face a higher risk of harm. When determining whether a lack of regulation is an issue, one consumer group noted that the ability of some TPIs to impact on a customer's health and well-being (much like an existing supplier) should be a key consideration.
- Distortions to competition – The imposition of different rules and obligations to entities providing the same service creates an uneven playing field in the market that could reduce competitive pressures, to the detriment of consumers.

These issues underpinned the view (held by many stakeholders) that our approach for regulating intermediaries should be reviewed. Some respondents considered that we should rely more on general consumer protection powers for licensees and TPIs, in order to reduce regulatory burdens and ensure there was a level playing field among market participants. These suppliers and TPIs felt that it will be important for Ofgem to have an open mind about the level of regulation required in the future market, and to be clear why consumer law alone would not be effective, before exploring additional or alternative approaches to regulating the retail market.

Other stakeholders thought it would be sensible for Ofgem to consider how our formal regulatory powers might need to be reformed, so that equivalent protections apply to consumers that engage with the market via TPIs. Some respondents told us that it will be increasingly appropriate to have a framework that targets regulation towards specific services or activities, rather than specific types of entities. They considered that an activity based approach could ensure a more level playing field, because regulatory obligations would depend on the activities a firm was authorised to undertake (eg marketing energy deals), rather than the type of firm you were (eg a supplier or a price comparison website). Some stakeholders told us that this type of approach could be an appropriate way to address issues seen in the non-domestic market.

There was strong support for any new framework to build on our moves towards principles-based regulation in the supply licences.²⁹ One stakeholder considered that a stronger

²⁸ Previous consideration of non-domestic TPIs can be found on our [website](#).

²⁹ More information on our future retail regulation reforms can be found on our [website](#).

assurance function, particularly for new entrants in the market, should also be explored as it could help protect consumers from some of the poor conduct that they see in the sector.³⁰ Another stakeholder suggested that Ofgem could use regulatory sandboxes to test how different types of protection frameworks would work in practice, both in terms of managing risks to consumers and promoting innovation and competition.

We note that there were stakeholders who were wary of making significant changes to the protections framework hastily. Some TPI stakeholders considered that regulating this part of the market could create burdens that negate the positive effects on engagement and innovation that is driven by these businesses. Some considered that the growing amount of self-regulation in the sector was appropriate for driving the continued improvements of outcomes for consumers. However, a consumer group stakeholder was dubious about the potential effectiveness of voluntary regulations, given past experience with such arrangements in the sector.

15 March 2018 workshop – #FutureSupplyLab

This was an interactive workshop whereby the expertise of the 50 attendees was used to generate ideas on how retail market design could best enable positive outcomes for future consumers. Attendees included a range of innovators, consumer bodies, academics, traditional suppliers and government.³¹

Session 1

Attendees were provided with an overview of our rationale for initiating the call for evidence, what we had heard so far from stakeholders and our updated thinking on the guiding criteria for future reforms. Following these opening remarks, attendees were then asked to give the current supplier hub market arrangements a rating out of ten, both in terms of how they serve consumers today, and how they will serve consumers into the future. The results from this exercise (included in our published workshop slides) mesh with what we've heard from a range of stakeholders during the call for evidence. The majority of stakeholders did not consider that current arrangements will be fit for serving future consumers.

During this first session stakeholders were shown a short video of consumers who participate in our Consumer First Panel research programme.³² The consumers in the video were asked a range of questions about their impressions of the current energy market. This emphasised the importance of putting consumer needs at the heart of any future reforms.

Session 2

During this session a recap of the current supplier hub model, and the challenges that this model can present for innovation, was given. This provided context for a presentation of a 'strawman' reference market model. This reference model was used to generate discussion about the potential scale of changes to the current model that could be explored, as well as some of the opportunities and constraints that could arise.

The presentation of the strawman reference market model led into a discussion amongst attendees about how changing where different functions within the current supplier hub model sit (such as meter provision and maintenance, vulnerability services and policy delivery) might impact on consumers and their experience in the market. Attendees then

³⁰ We are currently reviewing our approach to supplier licensing, to ensure that appropriate protections are in place to safeguard against poor customer service and financial instability. More information on this review can be found at: Ofgem (2018) [Review of Ofgem's approach to licensing suppliers](#)

³¹ Slides from this workshop have been published on our [website](#).

³² Our [Consumer First Panel](#) consists of 80 everyday domestic customers recruited from four locations across Britain. The panel meets regularly to discuss key issues impacting on their participation in the energy market, as well as other topics related to energy.

split into groups, and proceeded to work on creating their own retail market models. This exercise was facilitated by the use of different consumer personas, with attendees collaborating in their groups to identify what the requirements of particular consumers were, and how this would translate into design principles for a well-functioning future market model.

Session 3

This session was kicked off by guest presenter, Dr Jeff Hardy, who provided a presentation on the importance of putting consumers at the heart of any future retail market design. This presentation offered some high-level insights on the large scale of change occurring in the sector (in relation to system flexibility, data and business models). Dr Hardy then shared his perspectives on the challenges and opportunities this would create for the regulator and those it regulates (see p. 30 of workshop slides) – while also stressing that consumers need to be at the heart of any potential regulatory solutions. This presentation aimed to provide attendees with some unique perspectives that they could reflect on during the group session on retail market models.

Following the presentation attendees returned to their groups to complete the brainstorming exercise on retail market models. They were then asked to summarise the key, high-level conclusions they had drawn during this exercise. These conclusions included:

- Regulatory arrangements should (as much as possible) not hinder the types of business models that can enter the market.
- Regulation of existing and new business models needs to be proportionate to the activities carried out by market participants, and the risks these pose to consumers.
- We should consider and assess whether new or existing entities could carry out particular 'supply functions' more effectively than current suppliers. This includes considering how a new or existing entity could provide default access to supply for disengaged and/or vulnerable consumers (while not limiting innovation elsewhere in the market).
- Market design should seek to deliver positive outcomes for all consumers, not just those that are highly engaged or tech-savvy.
- The wholesale market costs that are passed on to consumers must be transparent and reflective of their impacts on the system.
- Data access must be enabled where appropriate, in an effort to reduce system inefficiency and drive more innovation in the market.

The brainstorming session – and subsequent group feedback presentations – were useful in highlighting a range of policy issues that will need to be focused on as our thinking on potential reforms to the supplier hub model develops.

In this last session, we also discussed how Ofgem might prioritise possible reforms, and how this would coordinate with existing work. We stressed that staying joined up with other reform projects would be key to the success of any potential changes to the current supplier-hub market model.