To all interested stakeholders

Email: retailpolicyinterventions@ofgem.gov.uk

Date: 23 February 2024

Dear all,

**Future of the Ban on Acquisition-only Tariffs, and associated market-wide derogation, post-March 2024 – Written Statement**

The Ban on Acquisition-only Tariffs (BAT) was introduced as a temporary market stabilisation measure in April 2022. The BAT was intended to help protect consumers from the risk to market stability posed by high and volatile gas prices. In October 2023 we set out our plan to conduct further analysis on its potential role beyond March 2024 and invited comments and supporting evidence from interested parties to help inform our analysis.

In light of this consultation and our further work, we are minded to remove the BAT from the market within the coming year. We have not seen compelling evidence that retaining the BAT as an enduring measure is likely to provide significant benefits, as set out in further detail below. Our view is that retaining it in place is likely to result in net consumer costs.

We will, however, take a phased approach to the BAT's removal, both to provide greater notice of our direction and to stagger the removal of market stability support rather than letting both the BAT and the Market Stabilisation Charge (MSC) expire at once. We are therefore exercising our existing power to extend the BAT for a further year (with this letter representing our required written statement to do so). Separately, we are extending the existing market-wide derogation from SLC22B for fixed retention tariffs

We will subsequently issue a statutory consultation, most likely with a minded-to position, on whether this extension should end after six months.

Our position that the BAT should not remain a long term feature of the market assumes that the price cap will remain in place. We would revisit the BAT's merits as a consumer protection tool if policy options to remove the price cap were being considered.

Context: Consultation and Stakeholder Responses

Alongside the MSC, the BAT was put in place to avoid untimely supplier failures at a time of extreme market volatility. Their combined purpose was to stabilise the market during the wholesale price crisis, in order to avoid untimely supplier failures and the resulting costs for consumers. We judge that the two measures have succeeded in fulfilling this core purpose. The risks of market-wide instability and supplier failure are also much reduced - a critical factor in our decision to allow the MSC to expire in March 2024 - while remaining suppliers are more resilient and better capitalised than many who exited the market in recent years. We have therefore considered whether retaining the BAT for other purposes, independent of this reducing market stability role, would be of benefit for consumers.

We consulted between 27 October 2023 to 23 November 2023 on whether or not to retain the BAT as a standalone measure while the price cap remains in place. Specifically, we invited views on the BAT's existing and likely future role on market stability, as well as its impact on competition, fair pricing and tariff offerings. We received 14 consultation responses (nine from energy suppliers, one from a consumer body and four from price comparison websites (PCWs) and third party intermediaries (TPIs)).

All nine suppliers supported an extension of the BAT post 31 March 2024 and agreed that it had contributed to market stability. Suppliers felt an extension would offer more time to better observe BAT's stability impact in the absence of the MSC. Suppliers also expressed their concern that the BAT's status had not been settled ahead of the price cap observation window for Q2 2024 and that this uncertainty had negatively impacted their hedging decisions for the period.

Seven suppliers considered that the BAT's extension would help limit price discrimination amongst existing and new customers in the market alongside the price cap, helping to promote a level playing field. The consumer group also strongly advocated for the BAT's role in limiting price discrimination among all consumers. A majority of suppliers also contended that the BAT enabled more sustainable competition, better focused on non-price factors such as improvements in services and innovation. This point was also echoed by the consumer group, who argued that extending the BAT would allow us to improve our understanding of its impact as a standalone measure on market stability.

By contrast, all PCWs and TPIs strongly opposed an extension of the BAT. Three out of the four respondents acknowledged that the BAT had been a positive and necessary intervention for market stability purposes, but considered that a further extension would negatively impact consumers and the return to competition. Their collective view was that the BAT drives up prices for active consumers and minimises incentives to switch for disengaged customers. They considered that the BAT would have significant negative impacts on non-price factors, which would in turn affect suppliers' ability to compete to provide better overall service.

PCWs and TPIs were in consensus that the BAT does not play a meaningful role in limiting price discrimination for existing or new customers in the presence of the price cap.

On the market-wide derogation, four suppliers considered that this should be kept for as long as the BAT is in place, with two suppliers suggesting it be incorporated into the existing licence conditions and a further two suppliers calling for it to be redrafted to better suit the BAT's ongoing purpose. Amongst PCWs and TPIs one respondent suggested the market-wide derogation should exist for as long as the BAT is in place given that it could mean fewer or less competitive retention tariffs, whilst two argued that it was having unintended consequences on the market and should be removed.

Ofgem analysis

These consultation responses have informed Ofgem's dedicated analysis work in recent months to best establish the BAT's impact as an ongoing, standalone feature of the market. In line with our consultation, we have considered these issues in terms of its impact on price protection and tariff-setting, as well as on competition and market stability.

This research concludes that 'loyalty penalty' benefits from BAT are likely to be limited. Based on analysis of Consumer Impacts of the Market Survey data in 2022 and 2023 we do not see evidence that previously disengaged customers are more likely to switch with the BAT now in place. During 2022, previously engaged customers were approximately 4-7 times more likely to switch tariff with their current supplier and approximately 3-3.5 times more likely to switch to a new supplier, compared against previously disengaged customers. Similar results are observed for 2023. This result suggests that BAT is having a limited impact on addressing the loyalty penalty.

Disengaged customers are already protected from unjustified tariff rises by the price cap. As such, the rationale that they would benefit from reduced prices (in the absence of cheaper deals for more engaged customers) does not appear to bear out. So far disengaged customers are not paying any less under BAT, whereas retaining it as a standalone measure is more likely than not to have an adverse effect on active consumers through higher prices.

We have also considered the possibility that the reduction in price competition could encourage greater focus on non-price competition and better overall service. To date, this has not materialised and there is no compelling evidence that the retention of BAT would be likely to drive better non-price market outcomes. Service quality is more likely to be a complement to price competition rather than an alternative.

We have modelled a range of price and competition scenarios to assess the BAT's impact on supplier and market stability. This and related work indicates that in most scenarios comparing the costs and benefits of either retaining or removing BAT, the benefits for consumers of removing the BAT outweigh the associated supplier losses.

There are a small number of quite specific scenarios in which removing the BAT worsens supplier finances, and so could theoretically contribute towards supplier failure. In these scenarios, the resulting cost to all consumers could exceed the cost of higher prices paid by engaged consumers if BAT was extended. However, in most scenarios the incremental effect of BAT is relatively small. Even in the more extreme scenarios, it seems unlikely that BAT would materially contribute to future supplier sustainability. This is true even in modelled instances of mass switching, following large wholesale price falls in the absence of both the BAT and the MSC.

Our position

Ban on Acquisition-only Tariffs:

The initial rationale for introducing the BAT has largely fallen away. While the reasons for its introduction have not disappeared entirely, wholesale price volatility and instability have markedly reduced in the past year. We are allowing the MSC to expire as a result and remain of the view that the BAT is insufficient to achieve market-wide stability on its own. Therefore based on this initial purpose, and given that both measures were designed to be temporary, there is a persuasive case for allowing the BAT to expire as well.

We also do not believe there is a compelling price protection argument for retaining the BAT, while the price cap is in place. Retaining the BAT is likely to result in net costs to consumers through increased prices, which its purported benefits (via improved non-price competition and supplier stability) are not likely to offset. We therefore believe the interests of existing and future consumers are best served by the BAT not remaining an enduring feature of the market.

However, in respect of the timing of the BAT's expiry, we believe there are good market stability reasons why the BAT should not cease to have effect immediately at the same time as the MSC on 31st March 2024 (when the BAT is currently due to expire), chiefly the residual level of uncertainty in the market as we emerge from the crisis, combined with the uncertainty arising from the removal of the MSC on the same date.

With the above points in mind, although we are minded that the BAT should not become an enduring feature of the market, we will take a phased and clearly telegraphed approach to its removal. **At this time, we will exercise our existing power in SLC 22B.5 to extend SLC 22B. We will also extend the associated market wide derogation for fixed retention tariffs by a further year; this letter represents our written statement setting out that we will do so. We will subsequently issue a further statutory consultation, ahead of the Q4 price cap observation window, to consult on whether the extension to the BAT should end after six months.**

We will use the time provided by an extension to further analyse the impact of the BAT once the MSC has been removed from the market. This will be useful to verify whether the conclusions of our analysis were borne out by reality, as well as when considering the BAT if options to remove or replace the price cap are being considered.

For the avoidance of doubt, this document, insofar as it sets out the decision to extend the BAT, is the statement in writing as referred to in Standard Licence Conditions (SLC) 22B.5 of the electricity and gas supply licences.

Accordingly, the BAT is extended to 31 March 2025.

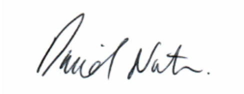
Market-wide Derogation:

We have also decided that the Market-wide Derogation from SLC 22B for fixed retention tariffs should remain in force alongside SLC 22B.

This accounts for the extension of SLC 22B until 31 March 2025, and is appropriate given that the reasons for allowing the Derogation for Fixed Retention Tariffs as set out in our Decision in April 2022 remained unchanged.

For the avoidance of doubt, the Directions (to Gas and Electricity Licensees respectively) that provide for the market-wide derogation from SLC 22B, and that have been in force since 14 April 2022, remain unchanged. This is because they provide, at paragraph 8 of each Direction, that they remain in force for the duration of SLC22B.

Yours faithfully,



**Dan Norton**

Deputy Director, Price Protection

**The Office of Gas and Electricity Markets**
10 South Colonnade, Canary Wharf, London, E14 4PU **Tel** 020 7901 7000
www.ofgem.gov.uk