

Last resort levy claims true-up process consultation

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When an energy supplier fails, Ofgem may appoint a Supplier of Last Resort (SoLR) for their customers and there is an industry process which enables a SoLR to seek to recover additional costs they face in supplying these customers (known as a 'Last Resort Supply Payment'). We are consulting on the fair approach to reflecting the costs suppliers faced in supplying customers of the large number of energy suppliers that failed in late 2021, and which it may be appropriate for them to seek to recover.

SoLRs we appointed have already made initial claims for Last Resort Supply Payments. The outcome of this consultation will determine what suppliers can seek to claim for in their final, true-up claim later this year. This true-up claim will cover the difference between the amount of incurred costs included in any initial claims received in late 2021 and the actual outturn costs. We would like views from all interested parties. We particularly welcome responses from gas and electricity suppliers, network operators, industry bodies, trade associations, generators, consumer groups and charities. We would also welcome responses from other stakeholders and the public.

This document outlines the scope, purpose and questions of the consultation and how you can get involved. Once the consultation is closed, we will consider all responses. We want to be transparent in our consultations. We will publish the non-confidential responses we receive alongside a decision on next steps on our website at [Ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations). If you want your response – in whole or in part – to be considered confidential, please tell us in your response and explain why. Please clearly mark the parts of your response that you consider to be confidential, and if possible, put the confidential material in separate appendices to your response.

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Executive summary

We are consulting on the recovery of wholesale costs under the Supplier of Last Resort (SoLR) levy (“the levy” hereon), as well as a number of other areas in relation to the levy claim true-up process.

In December 2021 we introduced a process to speed up the assessment of the initial levy claims submitted by suppliers. We limited the recovery of wholesale costs to energy that would be delivered within the 6-month window of a SoLR appointment, or up to the end of March 2022, whichever was earlier. However, we made clear that we would reconsider and consult on these issues ahead of the submission of Autumn 2022 true-up claims.

This consultation sets out the options and minded-to positions that, subject to our final decision, will apply to the Autumn 2022 claims. Responses to the questions in the consultation will inform our decision on how wholesale costs will be reconciled when suppliers submit true-up claims later this year.

Wholesale cost claims

We have considered four options to allow, if appropriate, the recovery via the levy of additional, unrecoverable wholesale costs that have been reasonably incurred.

Table 1: The options considered to allow, if appropriate the recovery via the levy of additional, unrecoverable wholesale costs that have been reasonably incurred

Option 1	Limit recovery to the cost of energy delivered within six months of being appointed. ¹
Option 2	Limit recovery to the cost of energy delivered by the end of March 2022, or within six months of being appointed, whichever is later.
Option 3	Limit recovery to the cost of energy procured within six months of being appointed and which will be delivered by the end of September 2022.

¹ This would limit recovery to energy delivered during the 6-month SoLR direction, which for some suppliers ends before the Summer 22 price cap adjustment. This would be consistent with the approach to our assessment of final claims that we took in our assessment of initial claims.

Option 4	Limit recovery to the cost of energy that will be delivered by the end of September 2022.
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Our minded-to position is to implement Option 2. This provides the best balance between the risk of adverse impacts on current consumers by allowing a longer recovery period in relation to which suppliers can claim costs, and the risk of adverse impact and costs to future consumers. This option will lead to a small increase in consumer bills across 2023/24.

It is also consistent with our broad principle that suppliers should be subject to no-gain/no-detriment if acting as a SoLR during the energy crisis. This will support the future viability of the SoLR regime and over all protect the interests of existing and future consumers.

Financing costs

When a SoLR is appointed, it incurs costs associated with taking on the new customers which need to be financed. There are a range of ways in which a SoLRs can finance this activity. Regardless of the finance option used, there is a cost in doing so. Suppliers may seek to claim through the levy to recover some of the financing costs that they have faced in acting as a SoLR.

Due to the scale of the claims submitted in December 2021, we have reviewed our process for assessing claims for financing costs to ensure it remains in consumers' best interests. We are clarifying our expectation of the standard of evidence suppliers must provide in relation to the financing costs being submitted through the SoLR levy process; we are asking suppliers to provide confirmation from a company Director that the company has fully considered the commercial options available to it and has chosen the option that represents the best value for money for consumers. Ofgem retains the right to challenge or disallow any claims that in our view do not meet this criteria.

Traditional Prepayment Meter (PPM) credit balances

SoLRs are unable to access accurate data on the credit balances held by traditional Prepayment Meter (PPM) customers they acquire. As a result, they need to estimate these credit balances in order to recover them through the levy.

Our minded-to position, in principle, is that SoLRs should be allowed to claim for traditional PPM credit balances that are additional and incurred as the result of acting as a SoLR. We are

inviting views on a proposed methodology for estimating these credit balances. The approach that we are seeking views on requires those SoLRs who wish to make claims for traditional PPM credit balances to average the credit balances of their existing smart meter PPM customers as a proxy for a typical traditional PPM customer's credit balance.

Audit requirements

Our minded-to position is that the true-up claim should be independently audited and signed-off by the company's internal audit team. This audit should be carried out with due rigour, and in accordance with recognised professional standards, should cover the Agreed Upon Procedures set out in chapter 4, and should be submitted alongside the true-up claim. The audit must be signed off by the directors of the company or the company board.

Temporary mitigation measures

Our minded-to position is that, in order to reduce the risk of overpayment and lessen the short-term impact of levy claims on energy bills, this temporary process should come to an end as early as possible after winter 2022/23.

Next steps

The consultation is open for responses until 4 August 2022. All responses will be considered, and non-confidential responses will be published on our website.

We aim to issue a policy statement and publish our final decision in September 2022.

Introduction

What are we consulting on?

0.1. We are consulting on our minded-to positions on the fair approach to reflecting the costs suppliers faced in providing energy to customers after being appointed as a Supplier of Last Resort (SoLR) between September 2021 and December 2021. This will determine what costs suppliers can seek to claim in their true-up claim later this year, should they choose to make a claim for any additional costs.

0.2. This consultation sets out options for the recovery of wholesale energy costs under the SoLR levy, as well as proposals and clarifications on the approach we intend to take in other areas in relation to the levy claim true-up process.

0.3. Where we state our minded-to position, we seek stakeholders' views on whether they agree. Where we present options, we seek stakeholders' views on their relative merits to help inform our final decision.

Context

0.4. The unprecedented rise in gas and electricity prices over the past year has put energy markets under severe strain. Wholesale market volatility means that energy suppliers have faced increased challenges in managing the risks of buying energy for their customers. This contributed to a large volume of supplier failures towards the end of 2021, requiring us to intervene and appoint a new supplier for customers whose energy supplier had failed (referred to as a 'Supplier of Last Resort' (SoLR)).

0.5. In carrying out this role, SoLRs incur additional costs which they may not be able to recover through normal cost recovery routes.² The Last Resort Supply Payment (LRSP) process (known as the 'SoLR levy' or 'the levy') is the "backstop" industry arrangement that enables a supplier to seek to recover the additional and unrecoverable costs that they

² In assessing whether a claim is reasonable, we need to consider whether the SoLR could have recovered the costs through other means. It would not be appropriate for us to allow the SoLR to claim for costs it could have recovered through the administration process or customer charges, for example.

reasonably incur when acting as a SoLR. This includes the reasonable costs incurred in purchasing the gas or electricity needed to supply these customers at short notice.³

0.6. In normal circumstances, and under the competitive process we follow to appoint a SoLR, the SoLRs may be expected to waive some or all of their right to make claims on the levy. Our preference is for a SoLR to absorb the costs of acting as a SoLR, or if they do choose to make a claim, to minimise the costs, as ultimately these costs fall to all consumers.

0.7. Recent market conditions have resulted in appointed SoLRs seeking to make claims on the levy for the additional and otherwise unrecoverable costs they have faced in supplying the customers of the large number of suppliers that failed in late 2021. As with the normal claim process, we would still expect suppliers to make all reasonable efforts to avoid these costs, or absorb them where possible. We acknowledge the higher costs suppliers have faced under recent market conditions, but we are also very conscious of the challenges faced by customers at this time. We expect suppliers to consider the ultimate impact on consumers' bills should they choose to make claims on the levy.

Measures we introduced

0.8. During winter 2021/22 we introduced a number of changes to the levy process which were designed to ensure that the SoLR process continues to protect consumers in the current market conditions. The changes included:

- The temporary introduction of a faster, multiple-claims levy process⁴
- Modifications of licences to allow for third-party financing of SoLR levies⁵

0.9. The multiple-claim levy process is intended to reduce the time taken for suppliers to submit claims and for us to make decisions, by allowing SoLRs to submit two claims per failed supplier: an initial claim for immediate costs faced in serving SoLR customers (typically wholesale commodity costs) followed later by a true-up. The true-up process is intended to

³ In purchasing any additional gas or electricity to supply newly acquired customers the SoLR is required to do so as economically as possible under the circumstances.

⁴ [Decision letter on supplier of last resort levy claims | Ofgem](#)

⁵ <https://www.ofgem.gov.uk/publications/decision-third-party-finance>

reconcile costs submitted by suppliers with the initial claims and determines what final payments should be made to them.

0.10. In line with our faster, multiple claims process, by December 2021 we had consented to SoLRs making initial levy claims totalling £1.83 billion. We set out that we would give further due consideration to a number of issues and consult with stakeholders before assessing final claims and any true-up.

Background

How do we appoint SoLRs?

0.11. We have a broad discretion in relation to our ability to appoint a SoLR. However, in order to get the best outcome for consumers, we undertake a competitive process to identify a SoLR to take on the customers of a failed supplier. We collect and consider a broad range of information in deciding which supplier to appoint as the SoLR. Among other things, we consider whether suppliers expect to make a claim on the levy, or whether it intends to waive all, or some, of its rights to do so.

0.12. The decision to appoint a SoLR involves Ofgem making a judgment taking into account the full range of criteria and all the information provided by suppliers, including any commitments they may have made in offering to act as a SoLR. We give very careful consideration to all relevant factors in coming to a view in the round on a decision that is in the best interests of consumers.⁶

Assessing claims

0.13. SoLRs submit claims and evidence of costs incurred to Ofgem, and we assess and determine the amount to be consented to. Once consented, SoLRs can start to recover the costs. To date, the earliest SoLRs have begun receiving payments is around 15 months post-appointment, with full repayment occurring around 12-15 months later. The multiple claim

⁶ The licence requires that the SoLR takes all reasonable steps to honour the commitment(s) it makes to the Authority before being appointed – SLCs 8.3 and 8.4.

process we set out in our 1 December 2021 decision letter⁷ was designed to speed up this process and allow SoLRs to begin recovering costs from April 2022.

0.14. Any SoLR making a claim on the levy should be clear about what the costs relate to. SoLRs are responsible for providing the evidence to support their claims, which should include demonstrating that the costs meet all our relevant criteria – ie that the cost it is seeking to claim for is additional, directly incurred as part of its role as a SoLR, otherwise unrecoverable, and that all reasonable efforts have been made to avoid or absorb the cost.

0.15. In assessing what costs are reasonable for the SoLR to recover, the licence requires us to consider all the circumstances of the case. This means that we will consider, among other things, market conditions at the time when the costs were incurred. We will also consider the commitments that the SoLR made prior to being appointed and the steps that it took to honour to those commitments and to reduce the overall cost to consumers.

Structure of this consultation document

0.16. We have used the document structure below to set out the issues and request responses to our questions:

- **Chapter 1: Wholesale cost claims:** We set out our analysis and minded-to position on the duration of the period in relation to which SoLRs should be able to recover any difference between the cost of purchasing wholesale energy, and the costs they are able to recover through charges to customers they are supplying as SoLR.
- **Chapter 2: Financing costs:** we set out our expectations in relation to the evidence that we will require to demonstrate that the financing costs claimed are value for money (VFM) and reflective of the true cost faced.
- **Chapter 3: Traditional PPM Credit Balances:** we set out our position on how levy claims for traditional Prepayment Meter (PPM) credit balances should be

⁷ [Decision letter on supplier of last resort levy claims | Ofgem](#)

treated and seek stakeholder views on the proposed proxy for quantifying the value of a traditional PPM credit balance.

- **Chapter 4: Audit Requirements:** we outline the audit requirements that each element of the claim will be required to meet.
- **Chapter 5: Temporary mitigation measures:** to reduce the risk of overpayment and lessen the short-term impact of levy claims on energy bills, we proposed ending the temporary process as early as possible after winter 2022/23.

Related publications

0.17. The faster SoLR levy claim process was introduced in winter 2021⁸ in response to challenging market circumstances because of high wholesale energy prices. We consented to a number of initial SoLR levy claims in December 2021,⁹ on the basis that suppliers would submit a second, final claim to be assessed in line with a true-up methodology.¹⁰

Consultation timings

0.18. We are seeking responses to this consultation by 4 August 2022.

0.19. We currently expect to make a final decision on the issues discussed in this consultation in September 2022, in order to allow final claims to be made and decided on by mid-December 2022.

How to respond

0.20. We want to hear from anyone interested in this consultation. Please send your response to the person or team named on this document's front page or supplier@ofgem.gov.uk.

⁸ Letter to suppliers on supplier of last resort levy claims, 29 Ofgem 2021:

<https://www.ofgem.gov.uk/publications/letter-suppliers-supplier-last-resort-levy-claims>

⁹ Decision letter on supplier of last resort levy claims, 1 December 2021:

<https://www.ofgem.gov.uk/publications/decision-letter-supplier-last-resort-levy-claims>

¹⁰ Guidance on supplier of last resort and energy supply company administration order, 21 October 2016: <https://www.ofgem.gov.uk/publications/supplier-last-resort-revised-guidance-2016>

0.21. We've asked for your feedback in each of the questions throughout. Please respond to each one as fully as you can.

0.22. We will publish non-confidential responses on our website at www.ofgem.gov.uk/consultations .

Your response, data and confidentiality

0.23. You can ask us to keep your response, or parts of your response, confidential. We will respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.

0.24. If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you do wish to be kept confidential and those that you do not wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published. We might ask for reasons why.

0.25. If the information you give in your response contains personal data under the General Data Protection Regulation (Regulation (EU) 2016/679) as retained in domestic law following the UK's withdrawal from the European Union ("UK GDPR"), the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 4.

0.26. If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

General feedback

0.27. We believe that consultation is at the heart of good policy development. We welcome any comments about how we've run this consultation. We'd also like to get your answers to these questions:

1. Do you have any comments about the overall process of this consultation?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Were its conclusions balanced?
5. Did it make reasoned recommendations for improvement?
6. Any further comments?

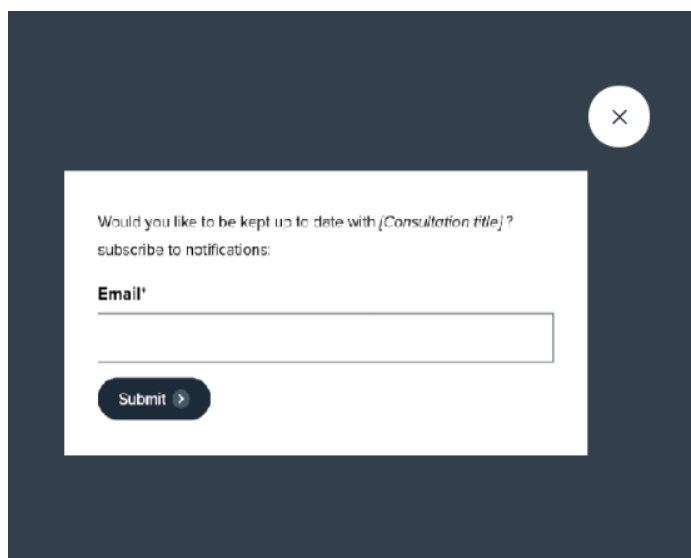
Please send any general feedback comments to stakeholders@ofgem.gov.uk

How to track the progress of the consultation

You can track the progress of a consultation from upcoming to decision status using the 'notify me' function on a consultation page when published on our website.

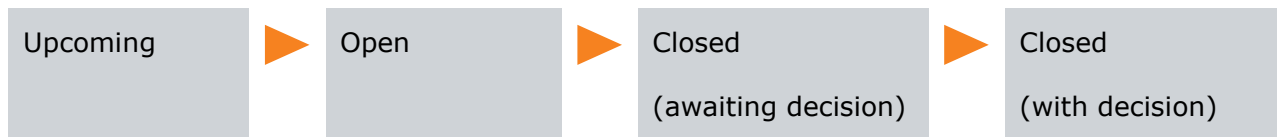
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Once subscribed to the notifications for a particular consultation, you will receive an email to notify you when it has changed status. Our consultation stages are:



Wholesale Cost Claims

Section summary

In December 2021, we allowed SoLRs to make initial levy claims for the immediate costs they incurred when hedging for their SoLR customers. To mitigate the risk of overpaying, we limited these initial claims to the costs relating to energy that would be delivered within the 6-month window of the SoLR direction, or up to the end of March 2022 whichever was the earlier. However, we committed to consulting on the appropriate duration of the period in relation to which costs may be claimed, ahead of suppliers submitting their final true-up claims in October, which will determine the final amount SoLRs can claim in respect to each failed supplier.

This section contains analysis of the different policy options available to address these questions and, where possible, quantifies the risks associated with each policy option.

Minded-To Position 1 (Option 2): all SoLRs appointed in the period from September – December 2021 should be able to recover additional and unrecoverable wholesale costs incurred relating to energy delivered up until 31 March 2022 or until the end of their 6-month SoLR direction, whichever is later (option 2).

Question 1: Do stakeholders agree with our minded-to position 1 (option 2)?

Proposals

1.1. Our minded-to position is that that all SoLRs appointed in the period from September – December 2021 should be able to recover additional and unrecoverable wholesale costs incurred relating to energy delivered up until 31 March 2022 or until the end of their 6-month SoLR direction, whichever is later (option 2).

1.2. This would mean that SoLRs who were appointed in September 2021 would be able to continue to recover the additional and otherwise unrecoverable cost of supplying energy to customers throughout March 2022, up until the Summer 22 price cap adjustment. We consider that this would represent a fair and proportionate outcome, which seeks to minimise the impacts on consumers overall, while also striking an appropriate balance between the interests of existing and future consumers.

1.3. If following this consultation we decide to confirm this position, then the decision to consider costs incurred for delivering energy beyond the 6-month SoLR direction period would be strictly limited to the particular and exceptional circumstances of this case and not intended to set a precedent for future SoLRs, which would always be considered on a case-by-case basis.

Context

1.4. When a SoLR is appointed, they must initially offer the customers of the failed supplier a deemed tariff that is in line with the retail price cap (RPC). The RPC assumes that suppliers can forecast their customer demand and hedge that demand in the market by purchasing forward contracts. In doing so, suppliers will account for any fluctuations in expected future volumes needed due to expected changes in its future customer base and seek to reflect that in purchases of forward contracts. This helps to manage the risks in buying energy.

1.5. However, when a supplier is appointed as a SoLR, it gains a large number of customers at once that it was unable to foresee when executing its hedging strategy, and therefore it was unable to purchase in advance, the volumes needed to serve these customers. This means that when a supplier is appointed as a SoLR, it immediately has to purchase energy to supply these customers, at the prices available in the wholesale market at the time of appointment.

1.6. If the price faced in the market for these products is higher than what can be recovered from consumers through the RPC, then suppliers are faced with an additional, unrecoverable cost in supplying its SoLR customers. We refer to the difference between the price paid in the wholesale energy market and the cost that can be recovered through the price cap as 'the wholesale differential'.

1.7. High and volatile wholesale prices created a substantial wholesale differential for SoLRs appointed between September – December 2021. This led to SoLRs, for the first time, seeking to make a claim on the levy for the wholesale differential and drove significantly higher levy claims than we have seen in the past.¹¹ These market conditions also risked impacting suppliers' ability to act as a SoLR, leading us to introduce the faster levy claims

¹¹ The right to claim for any incremental costs incurred is defined within Standard Licence Condition 9 ("Claims for Last Resort Supply Payment") of the Electricity Supply Standard Licence Conditions.

process¹² to speed up levy claims, securing continuity of supply to customers of failed suppliers.

1.8. This was also a key driver for introducing interim measures last year to allow SoLRs to make split levy claims in order to speed up the cost recovery of levy claims. In December 2021 we allowed SoLRs to make claims for the initial additional and unrecoverable costs they had incurred in supplying their SoLR customers. This was primarily the cost of purchasing wholesale energy, which we limited to the cost of purchasing energy that would be delivered within the 6-month window of their SoLR appointment, or up to the end of March 2022 whichever was the earlier.

1.9. We made this decision because it was not clear (at the time) what impact that the Summer 22 price cap and other potential interventions to stabilise the market would have, on the amount SoLRs could seek to claim through the levy.

1.10. In line with our faster claim process, we considered it appropriate to make our decisions on initial claims in time to enable SoLR's to receive consented costs in shorter timescales than is usually the case, where possible, and in this case from the start of the following network charging (financial) year. We therefore considered limiting the initial claims in this way the best way to protect consumers from the risk of overpaying on the levy, however committed to considering the issue further, prior to the true-up.

Analysis

Overview of options considered

1.11. We considered four potential options in seeking to identify the fair approach to reflecting the wholesale costs suppliers faced in providing energy to customers after being appointed as a Supplier of Last Resort (SoLR) between September 2021 and December 2021. In estimating the costs we have sought to understand the potential scale of the wholesale differential that suppliers may seek to claim under each option, and therefore estimate the potential increase in the levy of each option. These are summarised in table 2, below. Further detail can be found in annexes 1 and 2.

¹² [Decision letter on supplier of last resort levy claims.](#)

Table 2: Estimated Impact of Options on Consumer Bills

Option	Metric	Low	Medium	High
Option 1 – baseline: Limit recovery to the cost of energy delivered within six months of being appointed. ¹³	Total Levy Claim	£3m	£88m	£174m
	Impact on 2023/24 bills	£0.10	£3.10	£6.20
Option 2 – minded-to position: Limit recovery to the cost of energy delivered by the 31 st March 2022 or within six months of being appointed, whichever is later.	Total Levy Claim	£51m	£139m	£227m
	Impact on 2023/24 bills	£1.80	£4.90¹⁴	£8.10
Option 3: Limit recovery to the cost of energy procured within six months of being appointed and which will be delivered by the end of September 2022.	Total Levy Claim	£84m	£207m	£331m
	Impact on 2023/24 bills	£3.00	£7.30	£ 11.70
Option 4: Limit recovery to the cost of energy that will be delivered by the end of September 2022.	Total Levy Claim	£87m	£213m	£339m
	Impact on 2023/24 bills	£3.10	£7.60	£12.00

1.12. This analysis takes into account changes in the wholesale allowance that were introduced in the Summer 22 price cap update. In particular it takes into account:

- the updated wholesale allowances provided for the direct fuel costs within Cap Period 8, and
- the additional wholesale allowances provided for in Cap Period 8, to account for additional costs (such as shaping and imbalance) encountered in Cap Period 7.

1.13. This is because the wholesale differential is calculated by subtracting the amount that SoLRs can recover from consumers via the wholesale allowance in the price cap and the price SoLRs paid for energy in the wholesale market.

1.14. The adjustments outlined above have the effect of increasing the amount that can be recovered via the price cap, and therefore reducing the wholesale differential that suppliers may seek to claim through the levy. Adjusting the wholesale differential for these is critical to

¹³ This would mean taking the same approach to our assessment of final claims that we took in our assessment of initial claims.

¹⁴ Impact estimated based on expected total levy claim, apportioned to a GB dual-fuel Retail Price Cap representative customer. Total impact apportioned across April 2023 to March 2024.

ensuring that the broader actions we have taken in the market do not lead to SoLRs being over-compensated via the levy.

1.15. Ultimately, it is up to suppliers to decide what costs they seek to claim. However, we expect that suppliers act proportionately and fairly when submitting claims. There are factors which we expect suppliers to consider and, where appropriate, offset from their true-up claim. This includes any revenue acquired from the sale of any surplus energy initially purchased for SoLR customers, the cost of which was included in initial claims.

Our minded-to position

1.16. Our judgment is finely balanced between option 1 and option 2. However on balance, we consider option 2 to be the most proportionate approach to managing the cost to existing consumers, against the risk of adverse impact and costs to future consumers if our approach acts as a disincentive on suppliers to act as SoLR going forward.

1.17. This approach would allow SoLRs who were appointed more than 6 months before the Summer 22 price cap adjustment came into effect¹⁵ to claim for the costs of delivering energy to SoLR customers, up to the point of the adjustment.

1.18. We estimate it would result in levy costs of around £139m, or £4.90 per consumer bill. This is an estimated increase of £51m (or £1.80 per consumer bill) compared to the estimated baseline increase (ie compared to option 1). We consider Option 2 represents a fair and proportionate approach, which seeks to minimise the impacts on consumers, while also striking an appropriate balance between the interests of existing and future consumers.

1.19. If following this consultation, we decide to confirm this position, this decision would be limited to the particular and exceptional circumstances of this case and would not be intended to set a precedent for future SoLRs which would always be considered on a case-by-case basis, taking account of our principal objective to protect consumers.

1.20. We are entitled to exercise discretion on a case-by-case basis in accordance with our principal objective to protect the interests of existing and future consumers.

¹⁵ ie those appointed in September 202.

1.21. While Option 1 would result in the lowest costs to existing consumers (we estimate it would result in levy costs of around £88m, or £3.10 per consumer bill), our view is that it could significantly disincentivise or reduce the competitiveness of future SoLRs risking adverse impacts and costs for future consumers.

1.22. This is because under option 1 SoLRs appointed before the end of September 2021, would bear the full cost of the wholesale differential that existed up to the end of March 2022, prior to the Summer 22 price cap adjustment. It would particularly impact the suppliers who were first to volunteer to absorb customers early in the crisis.

Options we do not propose to pursue

1.23. Options 3 and 4 consider the case for allowing SoLRs to seek to claim costs associated with energy that will be delivered during the Summer 22 price cap period, which some SoLRs argued in our October 2021 consultation¹⁶ on the faster levy process, should be permitted. However, we do not consider this to be a proportionate approach when weighing up the costs and risks to SoLRs and consumers, in light of our principal objective to protect existing and future consumers.

1.24. The Last Resort Supply Direction ('the SoLR Direction') – the direction given to a supplier by the Authority requiring it to supply customers of a failed supplier – is effective for a period of 6 months from appointment. Following those 6 months, the customers acquired that remain with the supplier acting as SoLR are considered to be standard customers of the supplier.

1.25. This means that there is a well-established point in time at which the SoLR should no longer reasonably expect to be able to claim through the levy, the costs associated with supplying energy to these customers. Therefore in general any wholesale differential or other risk that exists when managing customer volumes out with the SoLR direction should be treated as normal risks that suppliers manage on a day-by-day basis.

Links and Interdependencies

¹⁶ [Consultation on Last Resort Supply Payment claim \(LRSP\) process](#)

1.26. The true-up process will lead to allowances flowing to suppliers to compensate them for additional costs incurred when supplying energy to SoLR customers. Alongside this, there are several other interventions to stabilise the market which impact supplier revenues. The interaction between these broader interventions and the SoLR levy creates the risk that suppliers acting as SoLR could be overcompensated.

1.27. To mitigate this, when assessing our options, we have taken into account the additional revenues which some suppliers are expected to receive due to these broader interventions.

Price cap interactions

1.28. There is a risk that suppliers may be overcompensated due to temporary cap allowances with CP8 & CP9 for unrecovered costs incurred within CP7¹⁷. Suppliers who took on SoLR customers might not have fully incurred these costs, given they took on customers after the beginning of the CP7 period, and are potentially already seeking to claim these incremental costs against allowances. These costs include:

- Additional shaping and imbalance costs driven by the volatility in energy prices incurred within CP7, which suppliers might not have wholly incurred.
- Additional backwardation allowances applied for provision of energy in CP7.
- Additional costs related to unexpected SVT demand, incurred up to the end of price cap period seven which suppliers might not have fully incurred.

1.29. As outlined within Appendix 1: Analysis of wholesale costs impact, we are looking to account for any additional allowances which suppliers might receive for shaping and imbalance. We will look to only allow additional claims for shaping and imbalance where these are proven to be in excess of the back payments suppliers are being paid.

¹⁷ [Price Cap - Decision on the potential impact of increased wholesale volatility on the default tariff cap](#)

1.30. We also want to hear stakeholders' views on the drivers of the additional claims for CP7 shaping and imbalance costs for their SoLR customers. We are seeking additional information around these costs which we outline within Appendix 1.

1.31. However, there are certain other interactions which might lead to a supplier being overcompensated, which we may not be able to mitigate and seek to account for as part of the final true-up payments. Specifically, for costs incurred during winter 2021 (cap period seven) related to backwardation¹⁸ and SVT demand drift, which the price cap will compensate SoLR suppliers for potentially incorrectly. It might not be possible to accurately seek repayment of overcompensation awarded to suppliers for these historic costs. This has fed into our decision on the preferred option (Option 2), which will mitigate against the risks of overpayment.

¹⁸ When the market is in backwardation the forward prices in the later six months are lower than in the first six (the actual price cap period). It brings the price cap level below the cost to suppliers of purchasing that energy for consumers (for that price cap period).

Financing Costs

Section summary

Due to the scale of the claims submitted in December 2021, we have reviewed our process for assessing claims for financing costs to ensure it remains in consumers' best interests. We are clarifying our expectation of the standard of evidence suppliers must provide in relation to the financing costs being submitted through the SoLR levy process; we are asking suppliers to provide confirmation from a company Director that the company has fully considered the commercial options available to it and has chosen the option that represents the best value for money for consumers.

Minded-To Position 2: SoLR to submit claims for financing costs reflective of their actual costs, but we will require SoLRs to further demonstrate, and provide evidence, that their financing cost claim delivers value for money to customers (and was the best possible rate they could have achieved given their individual circumstances).

Question 2: Do stakeholders agree with our minded-to position 2?

Proposals

2.1. Given the scale of the claims submitted in December 2021, we have reviewed our process for assessing claims for financing costs – ie interest on working capital – to ensure it continues to remain fit for purpose, and in the best interest of consumers. We are clarifying our expectation of the standard of evidence suppliers must provide in relation to financing costs being submitted through the SoLR levy process.

2.2. When making a claim for financing costs, we are asking suppliers to provide confirmation from a company Director¹⁹ that the company has fully considered the commercial options available to it and has chosen the option that represents the best value for money for consumers, and that the rate is reasonable in all circumstances of the case.

¹⁹ We will require such Directors' statements for the whole claim, not just financing costs. See the Independent Audit chapter for further detail.

This should be supported by evidence of the options considered and the basis on which the decision was made.

2.3. Ofgem retains the right to challenge or disallow any claims that in our view do not meet this criteria.

Context

2.4. When a SoLR is appointed, it incurs costs associated with taking on the new customers (purchasing energy for new customers, migration costs etc) which need to be financed. There are a range of ways in which SoLRs can finance this activity. Regardless of the finance option used, there is a cost in doing so. These financing costs vary based on the individual characteristics of the supplier (eg the size of the supplier, the perceived level of risk the supplier has, whether or not the supplier is part of group etc).

2.5. Suppliers may seek to claim through the levy to recover some of the financing costs that they have faced in acting as a SoLR. This is permitted by the licence, which is clear that interest on working capital used to finance the reasonably incurred cost when supplying SoLR customers may be included in a SoLR levy claim, provided that this cost cannot be recovered through customer charges.²⁰

Analysis

2.6. We recognise that suppliers face costs in financing their SoLR activities, and that some of the financing costs may not be able to be recovered through normal routes. Where this is the case, SoLRs may seek to claim this cost through the SoLR levy. Any amount the SoLR seeks to claim is subject to the Authority's consent, having carefully reviewed the amount claimed in each case.

2.7. We expect the SoLR to demonstrate why it is a reasonable to claim for such costs, and that doing so is in consumers interests, taking into account the prevailing circumstances. This includes demonstrating why such costs could not reasonably be absorbed and why it is fair

²⁰ Supply Licence Condition 9.4(a)

and proportionate to seek to recover such costs from consumers under the prevailing conditions.

2.8. The Authority can determine that a different amount to the one calculated by the Licensee is a more accurate calculation of the relevant amount to be claimed. In such cases, that is the amount (rather than the amount originally included in the SoLR's claim) that the SoLR must claim when seeking payment from the relevant networks company.

The appropriate financing cost rate

2.9. We recognise that there may be valid reasons for financing costs to differ between suppliers, and at different points in time. We therefore do not think it is helpful to publish benchmarks for the appropriate financing cost rate (%). However we will continue to use internal benchmarks to assess and challenge claims submitted to us to ensure value for money and to protect the interests of consumers.

2.10. We expect SoLRs to take steps to ensure the financing rate they obtain is value for money for consumers, and we will require evidence of the steps that SoLRs have taken to ensure this (explained in further detail below). This includes demonstrating that where intra-group loans were used to finance activities that the rate applied is fair to consumers.

Ensuring value for money

2.11. Regardless of the route through which SoLRs finance their SoLR activity, the onus is on a supplier to demonstrate that it has taken reasonable steps to minimise the costs it seeks to recover through the levy. SoLRs should provide evidence to support this and to demonstrate that the financing cost it has applied represents the best value for money for consumers. This should include evidence of the alternatives considered and the basis on which the decision was made.

2.12. This evidence should be submitted along with a signed statement from a Director of the company that the company has considered the financing options available to it, including

3rd party assignment of approved SoLR claims,²¹ and that the claim put forward represents the best value for money.

2.13. However, Ofgem retains the right to challenge or disallow any claims where we do not think sufficient evidence has been provided to demonstrate value for money.

²¹ <https://www.ofgem.gov.uk/publications/decision-third-party-finance>

Traditional PPM Credit Balances

Section summary

In a recent SoLR round, we received a levy claim for the credit balances of customers using traditional (non-smart) meters (PPMs). This section sets out that, in principle, subject to all the circumstances of the case, Ofgem considers it reasonable for SoLRs to seek to make a case to recover traditional PPM credit balances from the levy, where these are otherwise unrecoverable. This section also invites views on the proposed methodology SoLRs should use to estimate these credit balances.

Minded-To Position 3: In principle, subject to all the circumstances of the case, Ofgem considers it reasonable for SoLRs to seek to make a case to recover traditional PPM credit balances from the levy, where these are otherwise unrecoverable.

Question 3: Do stakeholders agree with our minded-to position 3?

Minded-To Position 4: Average credit balances from suppliers' existing smart meter PPM customers are a suitable proxy for a typical PPM customer's credit balance.

Question 4: Do stakeholders agree with our minded-to position 4?

Proposals

3.1. We agree in principle that, subject to all the circumstances of the case, it is reasonable for SoLRs to seek to make a case to recover traditional PPM credit balances from the levy, where these are otherwise unrecoverable. The customers of the failed supplier will have continued to draw down on existing credit on their meter and the SoLR would have been required to supply this energy without receiving payment for it. Enabling SoLRs to claim for this cost will reduce the risk that future SoLRs will not volunteer for failed suppliers with largely traditional PPM portfolios.

3.2. As SoLRs are unable to access accurate data on the credit balances held on traditional PPMs, this value needs to be estimated. We are, therefore, also inviting views on the

proposed methodology for estimating these credit balances. The option that has been proposed to us would require those SoLRs who wish to make claims for traditional PPM credit balances to average the credit balances of their existing smart meter PPM customers as a proxy for a typical traditional PPM customer's credit balance.

Context

3.3. When a supplier fails, if they have PPM customers, those customers are likely to have pre-existing credit on their meter at the point when the supplier fails. The SoLR becomes responsible for procuring the required volume of wholesale energy to supply those customers, with immediate effect, on the beginning of the gas and electricity day that they are appointed. However, the SoLR will not start receiving payments from the newly acquired customers until their pre-existing credit has reduced, and they top up the meter.

3.4. While the actual credit balance remains on the traditional PPM meter, and from a customer's perspective is not at risk when a supplier fails, the SoLR will not receive the funds in relation to the credit balance. The SoLR will, in effect, not be able to recover the costs associated with supplying energy to the equivalent value of the pre-existing credit balance.

3.5. In December 2021, we received a request for consent to a levy claim for the credit balances of traditional PPM customers the supplier had acquired through the SoLR process. Since it is not possible for the SoLR to accurately determine the credit remaining on customers' traditional PPMs, actual data could not be used to make or assess the claim.

3.6. The SoLR therefore proposed a methodology for proxying the value of credit balances to be claimed. The SoLR proposed to estimate the value of credit balances to be recovered by using the average credit balance of their existing smart meter PPM customers as a proxy for the average credit balance of the acquired traditional PPM customers' credit balance.

3.7. Although SoLRs have previously acquired customers on traditional PPMs, this was the first instance in which a SoLR had sought to claim these credit balances through the levy, and therefore the first time we have had to consider an appropriate methodology. We have removed these costs from the initial claim and committed to considering the issue and consulting on the proposed methodology.

Analysis

3.8. Our 'minded-to' position is that, in principle, SoLRs should be able to seek to claim on the levy for traditional PPM credit balances. In our view, this is a category of cost that may be capable of being demonstrated to meet Ofgem's criteria for SoLR levy claims, ie the cost is additional, directly incurred as part of the SoLR role, otherwise unrecoverable and should be demonstrated to be economic. We would still decide on a case-by-case basis whether to consent to any claims for such costs, subject to all the circumstances of the case, and whether it is in consumers interests to grant our consent.

3.9. We would expect SoLRs to demonstrate the steps taken to minimise the costs, for example seeking to claim credit balances from the administrator of the failed supplier and be satisfied they claim was economic. To mitigate the risk of suppliers 'double-claiming' for energy, our assessment process will also ensure that the costs of taking on customer credit balances are not also included in their wholesale claim.

Determining the value of traditional PPM credit balances

3.10. A risk with allowing levy claims to be made for traditional PPM credit balances is that claims may not reflect the true cost to the supplier as the lack of 'real' data requires claims to be based on estimates. We consider that putting in place a clear methodology, supported by evidence, should minimise the risk of any overpayment and we are seeking stakeholder views on this methodology (see question 5).

3.11. The information we have received from the appropriate PPM metering agents indicates that, when a SoLR takes on traditional PPM customers, it is not possible for them to access data on the individual credit balances associated with those meters (gas) or the available data is not reliable (electricity). Should the SoLR seek to claim for the credit balances in a levy claim, the total credit balance must be estimated.

3.12. We propose suppliers follow a defined methodology to calculate credit balances they will claim for. We invite views on the proposed methodology set out below and would also welcome suggestions for alternative methodologies.

3.13. The SoLR that made the claim has proposed that an estimate of traditional PPM credit balances should be based on the percentage of the SoLRs' portfolio of smart PPMs with a credit balance on the day of transfer of supplies, and the average credit balance of those

customers at midnight, on the day of transfer of supplies. Where a supplier is claiming for both gas and electricity customers, a separate figure should be calculated for each.

3.14. While existing Ofgem consumer research does not have direct measures of credit levels by PPM type, analysis of indirect proxy measures does not find evidence of differences between smart and traditional PPM customers. For example, existing research finds no difference in the frequency with which smart and traditional PPM customers run out of credit and are disconnected. However, these indirect proxies are imperfect measures.

3.15. In line with our approach to all levy claims, we will expect suppliers to provide a breakdown of the calculation and suitable evidence supporting the figures upon which the estimate was based.

3.16. We recognise that it is possible that a SoLR may not have a sufficiently large population of existing customers on smart PPMs and are also seeking views from stakeholders on whether there is an approach that could be taken in such circumstances.

Audit Requirements

Section summary

The section sets out our requirement for levy claims to be independently audited and the minimum standards any such audit must meet. We will require such audits to be signed off by the directors of the company or the company board.

Minded-To Position 5: SoLRs should have all claims independently audited and signed-off internal (or, where relevant, external) auditors. We will only request an external, independent audit if we have serious concerns about any part(s) of a SoLR's claim(s).

Question 5: Do stakeholders agree with our minded-to position 5?

Proposal

4.1. Our minded-to position is that SoLRs should have all claims independently audited and signed-off by internal (or external) auditors. We will only request an external, independent audit if we have serious concerns about any part(s) of a SoLR's claim(s).

4.2. This independent audit should be carried out with due rigour, in accordance with recognised professional standards and should cover the Agreed Upon Procedures (AUP) set out in table 3 below. The AUP should be performed for values relating to the final claim.

4.3. In carrying out the Agreed Upon Procedures, the auditors should have regard to International Standard on Related Services 4400 (ISRS 4400) – Engagements to Perform Agreed-Upon Procedures Regarding Financial Information

Context

4.4. The scale of expected levy claims that will ultimately feed through to consumer bills means that SoLRs submitting claims must maintain a clear and comprehensive audit trail of all costs and commit to working transparently with us.

4.5. We have made it clear that prior to final claims being submitted to us we expect all cost categories to be subject to an audit with due rigour that ensures all costs adhere to our criteria. This plays a key role in assuring us as to the quality of the evidence that is provided and to enabling us to carry out a robust assessment of all claims.

Agreed upon procedures

4.6. We would expect the internal audit to follow the Agreed Upon Procedures (below). These set out the minimum standards we expect the audit to meet and, as set out above, need to be signed off by the directors of the company or the company board.

Table 3: Internal audit agreed upon procedures

Cost component to which AUP applies	Agreed Upon Procedure (AUP)
All costs	<p>Confirm that all costs claimed for meet Ofgem’s criteria for SoLR levy claims, ie they must be additional, directly incurred as part of the SoLR role, unavoidable, otherwise unrecoverable and efficiently incurred and evidence has been provided to support this is efficient.</p>
Wholesale costs	<p>Verify that the wholesale trades being claimed for actually took place, and that the correct trades have been allocated to the levy claim, taking account of the period in respect of which the claim is being made.</p> <p>We do not plan to specify how SoLRs should evidence this as processes and methodologies can vary between companies. Examples of evidence SoLR’s could supply include (this list is not exhaustive):</p> <ul style="list-style-type: none"> • Demand forecasting • Regular positions reports • Management reports • End of day positions • Bulk trades <p>Auditors should take care to evidence any assumptions the SoLRs may have made and/or provide a rationale for the assumptions. Auditors should also confirm that the trades being claimed for were carried out in line with the SoLRs’ historic trading pattern and general approach to trading. Where this cannot be confirmed, rationale and</p>

	evidence has been provided to explain why this was appropriate in the given circumstances.
Credit balances	<ul style="list-style-type: none"> • Confirm that the amounts claimed meet the definition of credit balance in the licence, ie it relates to money the customer paid the supplier with the expectation of being provided energy in return. Reasonable efforts have been made to distinguish and exclude from the claim other payments such as incentive payments, warm home discount payments or guaranteed standards of practice payments. • Carry out checks to provide assurance that the credit balances have been incurred (ie they have been returned to customers either through a credit on the customers energy account or through returning the money directly to the customer). • Carry out checks to provide assurance that the credit balances are based on final customer account balances provided by the administrator. • The credit refunded was based on meter reads, actual or estimated. Evidence has been provided for any amounts that have been included within the claim, but which have been disputed by the administrator. • The credit refunded was based on meter reads, actual or estimated. • Evidence has been provided for any amounts that have been included within the claim, but which have been disputed by the administrator
Financing Costs	The supplier is only claiming for financing costs that have been incurred by the time the claim is made, ie for money the supplier has already had to pay out. Evidence must be provided to demonstrate it has fully considered the commercial options available to it and has chosen the option that represents the best value for money for consumers. A claim cannot be made for forecasted financing costs.
Other	The supplier is only claiming for costs that have been reasonably incurred and it has provided evidence to demonstrate that the cost meets our criteria.

4.7. Unless otherwise advised, the completed AUP reports (in PDF format, word-searchable and not a scanned image) should be submitted alongside the true-up claim to the secure location set up for the purpose of the submission. AUP reports are to be received no later than the final claims submission deadline, ie October 2022 for SoLRs appointed at the end of 2021.

4.8. We are asking stakeholders if they agree with our minded-to position (numbered 6) outlined above.

Temporary mitigation measures

Section summary

During winter 2021/22 we introduced a number of changes to the levy process which were designed to ensure that the SoLR process continues to protect consumers in the current market conditions. This included the temporary introduction of a faster, multiple-claim levy process which was intended to reduce the time taken for suppliers to submit claims and for us to make decisions on those claims.

Minded-To Position 6: The temporary, multiple-claim, levy process will come to an end as early as possible after winter 2022/23 in order to reduce the risk of overpayment and lessen the short-term impact of levy claims on energy bills.

Question 6: Do stakeholders agree with our minded-to position 6?

Context

5.1. During winter 2021/22 we introduced a number of changes to the levy process which were designed to ensure that the SoLR process continues to protect consumers in the current market conditions. The changes included:

- The temporary introduction of a faster, multiple-claims levy process.²²
- Modifications of licences to allow for third-party financing of SoLR levies.²³

5.2. The temporary multiple-claim levy process is intended to reduce the time taken for suppliers to submit claims and for us to make decisions, and involves SoLRs submitting two claims per SoLR: an initial claim followed later by a true-up. The initial claim includes costs

²² [Decision letter on supplier of last resort levy claims | Ofgem](#)

²³ [Decision on modifications regarding Last Resort Supply Payment Claims \(LRSPs\) for electricity supply, gas supply, electricity distribution and gas transportation licence conditions](#)

that a SoLR incurs (and can be fully evidenced) in the period immediately after appointment, primarily commodity costs.

5.3. The second true-up claim (or a declaration that no such claim is required) must be made at a later stage. This may include request for consent to claim other costs, in addition to any further wholesale costs incurred that had not been included in the initial claim. What costs can be included in the true-up claim is the subject of this consultation.

5.4. The introduction of the multiple-claim levy process was intended to be a temporary measure to cover SoLR events that occurred during winter 2021/2022. However, given the ongoing volatility in the gas market, exacerbated by recent geopolitical events, we intend to continue with the multiple-claim levy process until at least the end of 2022. This means that where SoLRs were appointed during 2022 they will continue to be able to make use of the multiple claim process.

Analysis

5.5. In order to provide longer-term certainty, it is important that we consider what the status-quo will look like when the current crisis subsides. We have set out a number of possible scenarios below, and welcome views from stakeholders on what our approach should be in future.

Scenario 1 – return to the previous status-quo

5.6. Scenario 1 would see a return to the previous levy application process when we are satisfied that the previous arrangements can provide value for money and secure continuity of supply to customers of failed suppliers.

5.7. The multiple-claim process was introduced in response to wholesale market volatility and is designed to ensure we can continue to act quickly to appoint a SoLR to supply all affected customers when a supplier exits the market, and to protect domestic customers' credit balances. When the market volatility subsides, and SoLRs do not seek to recover wholesale costs, we anticipate that the multiple-claim process will no longer be necessary.

5.8. While the multiple-claim process is likely to reduce the overall cost of levy claims (as suppliers' costs are recovered more quickly), this is offset by the risk of overpayment at the first claim stage and a more immediate impact on consumer bills. Ending the multiple-claim

levy process as early as possible after winter 2022/23 will reduce the risk of overpayment and lessen the short-term impact of levy claims on energy bills.

5.9. Ending the multiple-claim process would need to be considered alongside the need to act quickly to appoint a SoLR to supply all affected customers should further suppliers exit the market after winter 2022/23. As set out under scenario 3, below, it is possible that there are elements of the temporary process that could be retained, even if the overall process reverts to the single-claim process.

Scenario 2 – continue with the changes

5.10. We were clear in our December 2021 decision document that the change to the levy claim process was a temporary measure. It is possible that if market volatility continues beyond winter 2022/23, we would need to extend the process further. As we stated in the decision document, we are aware of the potential impacts on consumer bills, and a further extension would only occur if we determined that the measures continued to be needed to facilitate the SoLR process. Any decision to extend the process would need to take into account the broader market conditions.

Scenario 3 – hybrid approach

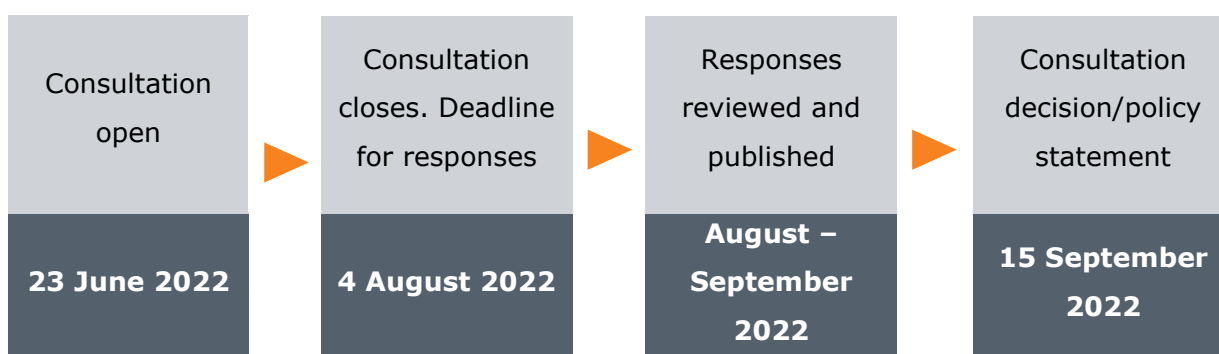
5.11. A further possible approach is that, in the longer-term, elements of both the previous arrangements and the temporary mitigations could be in place. This could involve, for example, retaining the option for split claims but only under very specific circumstances.

5.12. We welcome comments from stakeholders on what the approach should be in the longer-term, and whether there are aspects of the temporary measures that would be beneficial to maintain.

Next Steps and Timelines

Consultation timeline

6.1. This consultation on our approach to the SoLR levy true-up methodology is open for six weeks, from 23 June 2022 to 4 August 2022. Responses to the consultation should be sent to supplier@ofgem.gov.uk and must be received on or before 4 August 2022. The consultation process is summarised below.



6.2. During the consultation period, we intend to engage closely with industry, consumer groups and other interested parties. This will give stakeholders an opportunity to discuss, and ask questions about, the proposals we have put forward. If there are particular areas that stakeholders feel it would be useful to cover, please do get in touch. We will share details of planned engagement with stakeholders in due course.

6.3. Once the consultation is closed, we will analyse the responses we have received. All responses will be considered as part of the consultation process. Responses will also be published on our website, except where a respondent has requested that their response is kept confidential.

6.4. We intend to issue a policy statement and final decision in September 2022, ahead of the deadline for suppliers to submit their second claims on 7 October 2022. Our policy statement will summarise the responses we received and will set out our final position on whether, and how, we intend to take forward the proposals presented in the consultation.

Wholesale claim templates and methodology

6.5. We are currently working to finalise the design of our wholesale methodology against which true-up claims will be assessed, which includes determining what information and data

we will require from suppliers. We are also putting together standardised submission templates which will allow suppliers to submit the necessary data.

6.6. Establishing the wholesale methodology and finalising the submission templates is a key focus during June and July, and as part of this work we may seek to engage with suppliers directly. We are aiming to finalise submission templates by early August, and, if possible, may share draft versions with suppliers in advance.

Submitting true-up claims

6.7. Suppliers will be required to submit their true-up claim this autumn. We will confirm the specific deadline for suppliers alongside our decision document in September, but it is likely to be early October. We strongly recommend that suppliers engage with us ahead of submitting their claims and submit draft documentation to us if appropriate.

6.8. During the true-up process we will publish, for each claim submitted, consultations setting out our minded-to position on whether to consent to the claim. The purpose of these consultations is to provide interested parties with an opportunity to make any representations to us, ahead of us making our final decision.

6.9. We are aiming for final decisions on claims to be made in early to mid-December 2022, ahead of the deadline for suppliers to apply to the networks for their claims on 31 December 2022.

Appendices

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3	Appendix 3 – Privacy notice on consultations	57

Appendix 1: Analysis of wholesale costs impact

Summary of approach

6.10. We have analysed a set of wholesale cost components in order to understand where suppliers may have incurred incremental costs above price cap allowances, the materiality of any potential differences and the justification for these costs being included within any levy claims. Table 4 below sets out these key components and summarises which could seek to be claimed under each of the options we have considered.

Table 4: Cost components that a SoLR could seek to claim for under each option

Cost component	Option 1	Option 2	Option 3	Option 4
CP7 Hedging / Direct Fuel Costs	Conditional: energy must be <i>delivered</i> 6 months from appointment	Eligible to claim	Conditional: energy must be <i>procured</i> within 6 months from appointment	Eligible to claim
CP7 Shaping and Imbalance Cost	Conditional: energy must be <i>delivered</i> 6 months from appointment	Eligible to claim	Conditional: energy must be <i>procured</i> within 6 months from appointment	Eligible to claim
CP8 Hedging / Direct Fuel Costs	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>procured</i> within 6 months from appointment	Eligible to claim
CP8 Shaping and Imbalance Costs	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>procured</i> within 6 months from appointment	Eligible to claim
Other costs related to CP8 ²⁴	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>delivered</i> 6 months from appointment	Conditional: energy must be <i>procured</i> within 6 months from appointment	Eligible to claim

6.11. We have estimated the levels of these potential incremental costs in each of these components to provide a view of the overall impact on levy claims of each of the

²⁴ Price cap period 9 related to Winter 22.

options we have considered. There are a range of hedging and purchasing strategies which suppliers might have utilised which we will not have sight of until final claims are received.

6.12. Where there is uncertainty around the total final claims, our analysis includes ranges to reflect this incomplete information. Detail on these estimates is set out in the sections below. For all costs other than CP7²⁵ hedging/direct fuel costs we have estimated high, medium and low scenarios:

- **High scenarios:** Generally assume that all suppliers have a justified claim and will seek to claim the relevant costs, or that these costs are based on higher (yet viable) cost strategies employed by suppliers for the relevant cost component.
- **Medium scenarios:** Generally assume that all suppliers have a justified claim and will seek to claim the relevant costs, but that these costs are based on more efficient (cheaper) strategies for the relevant cost component.
- **Low scenarios:** Generally assume that only a limited number of suppliers who have indicated they intend to claim do so, or that the costs for the relevant component is based on strategies which lead to the lowest potential incremental costs incurred.

6.13. Where available, we have used actual data submitted by suppliers to inform our analysis.²⁶ Where we have limited or no data, we have used formed best estimates of the potential costs borne by suppliers using assumptions from the price cap on the products that SoLRs would have used to hedge and the prevailing market prices at the assumed point of purchase.²⁷

²⁵ We have not estimated high, medium and low scenarios for CP7 hedging/direct fuel costs as the majority of the costs in this category are based on actual data from December 2021 initial levy claims.

²⁶ Applicable to CP7 hedging and direct fuel costs.

²⁷ Applicable to CP7 shaping and imbalance costs and all CP8 costs.

Estimating CP7 hedging/direct fuel costs

Table 5: Estimated Cap Period 7 Hedging / Direct Fuel Costs

Cost component	Option	Estimate
Price Cap Period 7 Hedging / Direct Fuel Costs	Option 1 – baseline: Limit recovery to the cost of energy delivered within six months of being appointed. ²⁸	£ 1,694m
	Option 2 – minded-to position: Limit recovery to the cost of energy delivered by the 31 st March 2022 or within six months of being appointed, whichever is later.	£ 1,742m
	Option 3: Limit recovery to the cost of energy procured within six months of being appointed and which will be delivered by the end of September 2022.	£ 1,742m
	Option 4: Limit recovery to the cost of energy that will be delivered by the end of September 2022.	£ 1,742m

6.14. We compared the expected costs that SoLRs faced in direct fuel provision to their SoLR customers over CP7 to the allowances for the period that could be recovered via the price cap. As expected, SoLRs faced a material wholesale differential in supplying energy to SoLR customers throughout CP7 due to the allowances under the cap being below market prices. An estimate of these costs and how they differ by options is outlined in table 5, above.

6.15. The majority of the costs estimated in option 1 have already been claimed through the initial claims received in December 2021. The amount claimed in December was based on SoLRs estimated demand and prevailing costs at the time. During the true-up later this year we will seek to understand how outturn demand for SoLR customers and prices differed and expect SoLRs to offset any revenue received as a result of these differences in their final claim.

6.16. The increased costs of options 2-4 is attributable to SoLRs who were appointed in September 2021 being able to claim for all of their CP7 direct fuel allowance costs past their 6 month direction out until the Summer 22 price cap adjustment as opposed to being limited to claiming for only energy delivered within six months of being appointed.

²⁸ This would mean taking the same approach to our assessment of final claims that we took in our assessment of initial claims.

Estimating CP7 shaping and imbalance costs

Table 6: Estimated Cap Period 7 Shaping and Imbalance Costs

Cost component	Option	Low	Medium	High
CP7 Shaping & Imbalance Costs	Option 1	£ 19m	£ 101m	£ 183m
	Option 2	£ 19m	£ 104m	£ 189m
	Option 3	£ 19m	£ 101m	£ 183m
	Option 4	£ 19m	£ 104m	£ 189m

6.17. We estimated the expected costs that SoLRs faced relating to shaping and imbalance over CP7 and compared these to the allowances for the period that could be recovered via the price cap. These costs relate to:

- **Shaping:** refining positions on energy purchased for consumers by suppliers as they convert from bulkier forward contracts to more granular closer to delivery,
- **Imbalance:** the costs of matching their final traded electricity and gas contractual positions against their final expected demand.

6.18. Our analysis indicates that SoLR could have incurred additional CP7 shaping and imbalance costs for their SoLR customers, above that of the price cap allowances at this time for the duration of the period. However, as of yet we have seen limited evidence or claims for these additional costs, with only a small number of SoLRs providing estimates for any of these costs within the initial claims. This poor quality of data on the validity and materiality of costs for shaping and imbalance has resulted in a large estimated range for these costs, set out in table 6.

6.19. Our different options lead to differences in the timeframes for which shaping and imbalance costs can be claimed. Options 1 and 3 limit potential claims to only those shaping and imbalance costs incurred within the 6-month direction period after SoLR acquisition. Options 2 and 4 allow for suppliers to claim for costs incurred over a longer period, including for some suppliers the whole of CP7 up until the end of March 2022.

6.20. The actual costs attributable to this cost component will be highly dependent on the approach and strategies used by SoLR,²⁹ the size of their SoLR acquisition relative to their market size, and the timing of when they took on their SoLR customers. We expect that suppliers will only seek to claim these types of wholesale costs if they are able to justify and provide evidence that they have faced additional costs for shaping and imbalance.

6.21. However, suppliers are already receiving back payments³⁰ throughout CP8 and CP9 to recoup the additional shaping and imbalance costs faced during CP7.³¹ To avoid overcompensating SoLRs through the levy, any SoLRs seeking to claim for further incremental shaping and imbalance costs must demonstrate that the amount it seeks to claim are incremental to the revised CP7 cost levels which are already being back paid.

6.22. We want to hear stakeholders' views on the drivers of the additional claims for CP7 shaping and imbalance costs for their SoLR customers. We are seeking additional information on two key factors where suppliers claim for shaping and imbalance within CP7, specifically:

- Evidence that shows suppliers incurred additional shaping and imbalance costs as a result of a SoLR acquisition (not driven higher through wider volatility within energy prices) relative to CP7 allowances. This could include comparisons to their wider costs of shaping and imbalance within CP7 for non-SoLR customers; and
- If applicable, supplier estimates on the (incremental) shaping and imbalance costs above the revised CP7 price cap shaping and imbalance allowances which are accounting for the additional costs driven by volatility.

CP7 other costs

6.23. We see limited evidence of any other efficiently incurred costs in CP7 driven by SoLR participation. We only expect costs for other elements of incremental wholesale costs to

²⁹ Such as the ability of each supplier to include the additional demand from new SoLR customers into the ongoing shaping and imbalance procedures being taken across their wider customer book.

³⁰ [Price Cap - Decision on the potential impact of increased wholesale volatility on the default tariff cap](#)

³¹ In the increased shaping and imbalance costs faced over and above what could be recovered from the allowances in place at the time due to the increased energy price volatility during CP7.

be claimed where there is substantial evidence on material costs being incurred above allowances within the price cap for this period.

Estimating CP8 hedging/direct fuel costs

Table 7: Price Cap Period 8 Hedging / Direct Fuel Costs

Costs	Option	Low	Medium	High
Cap Period 8 Hedging / Direct Fuel Costs	Option 1	£ 3m	£ 6m	£ 9m
	Option 2	£ 3m	£ 6m	£ 9m
	Option 3	£ 39m	£ 80m	£ 121m
	Option 4	£ 39m	£ 80m	£ 121m

6.24. We compared the expected costs that SoLRs faced in direct fuel provision to their SoLR customers over CP8 to the allowances for the period that could be recovered via the price cap. Our analysis indicates that suppliers may have potentially have incurred additional CP8 hedging / direct fuel allowance in relation to customers acquired through a SoLR. This is because the wholesale allowance observation window for CP8 began on the 1 August 2021 and ended on the 31 January 2022. The price cap methodology assumes that suppliers gradually hedge for expected demand for CP8 over this observation window, and are fully hedged by 31 January 2022. Where suppliers take on a SoLR after this window has begun, it is not possible for them to match the price cap hedging methodology, and their approach is limited to hedging against the remaining portion of the observation window remaining for their required volumes.

6.25. We have estimated incremental costs above allowances for which suppliers might have borne above the price cap allowance for CP8 hedging costs, based on two different hedging methodologies.³² Our analysis shows that SoLRs have potentially incurred direct fuel hedging costs which were higher than allowances for the CP8, due to the steady rise in forward prices for CP8 over the observation window.

³² Methodology 1 assumes that suppliers hedge equally on a daily basis for the remainder of the observation period to fulfil their required demand. Methodology 2 assumes that suppliers initially hedge the required volumes equal to the proportion of the observation period which has passed, hedging the remaining volumes equally until period end.

6.26. However, this is also true for 'SVT drift' customers (where suppliers have not adequately adjusted their hedging strategies) – ie existing customers who have drifted on to standard variable tariffs at the end of a fixed deal, who prior to the market volatility the supplier had assumed would churn away and therefore did not hedge for. We introduced a number of other additional flows to suppliers to mitigate the impact of this.

6.27. As noted in our December 2021 decision document, the direction to act as a SoLR applies for 6 months from appointment. When the direction expires it is therefore reasonable for the customers that remain with the supplier to be treated as standard customers, rather than SoLR customers, and as such for any additional costs the supplier faces due to market volatility to be mitigated through broader measures introduced, rather than through the levy. We consider this to be a proportionate approach which balances the impact of these costs on existing consumers' bills with the risk of adverse impacts and costs to future consumers.

Price Cap Period 8 Shaping and Imbalance Costs

6.28. We see no evidence for there being an increase in the efficiently incurred shaping and imbalance costs above those of price cap allowances for CP8 driven by SoLR. All SoLR acquisitions as part of this process were completed by 4 December 2021. All suppliers would have had adequate time to fully hedge for customer demand (albeit at increased costs) prior to beginning of the CP8, and subsequently prepare for the required shaping and imbalance costs to supply these customers. Therefore, shaping and imbalance costs in CP8 should be covered by the price cap allowance for serving their customers.

Appendix 2: Impact Assessment

Overarching approach to the draft impact assessment

6.29. This draft impact assessment aims to identify and assess the effects and impacts of the SoLR Levy True-Up on consumers, industry participants, government and Ofgem, and the environment. We present our analysis of the impact of a set of options we have considered. This analysis has informed our policy decisions relating to the fair approach to reflecting the costs suppliers faced in providing energy to customers after being appointed as a SoLR between September 2021 and December 2021

6.30. A final impact assessment will be included alongside our final decision later this year. This impact assessment has been conducted in accordance with the Ofgem Impact Assessment Guidance. In developing the impact assessment we have also drawn on HM Treasury Green Book, BEIS and Regulatory Policy Committee (RPC) guidance.

Table 8: Estimated cost of claims within baseline scenario (option 1)

Metric	Metric	Low	Medium	High
Additional cost of claims already expected within baseline scenario	Total Levy Claim	£3m	£88m	£174m
	Impact on 2023/24 bills	£0.10	£3.10	£6.20

6.31. We have assessed the relative impact of our options against the baseline position that cost recovery is limited to the cost of energy delivered within six months of being appointed as SoLR (option 1 in our analysis above). We estimate that £88m of wholesale costs remained to be claimed through the true-up process in relation to this baseline position. This is the minimum estimated cost of reconciling in the true-up the initial wholesale costs SoLRs claimed for in December 2021 with the final wholesale costs faced.

6.32. As such, for the purpose of this impact assessment, when assessing the impact of the alternatives considered we focus only on the additional impact of the options compared to this baseline.

6.33. Our core analysis covers monetised and non-monetised impacts over the period of the impact wholesale period, from September 2021 until October 2022.

Impact on consumers

6.34. The temporary multi-claim levy process applies to all suppliers who were appointed as a SoLR between 1 September and 6 December 2021. Under these procedures, claims submitted by 6 December 2021 were reviewed by Ofgem/GEMA by 17 December 2021. SoLRs were then able to begin the process of recovering the amounts we consented to from 1 April 2022, via network companies, who increased their network charges to cover these costs, also from 1 April 2022.

6.35. As part of the true-up process, we expect that any approved additional claims will be added to the winter 2022 claims process, with claims flowing through to bills as from the 1 April 2023 to 31 March 2024. Any increased in claims that follow the recovery route outlined above will impact network charges, and therefore domestic consumer bills from April 2023 – March 2024.³³

6.36. An estimate of the total incremental levy claims, and their potential impact on bills for consumers between April 2023 – March 2024 is outlined below for our four options.

Table 9: Estimated Impact of Options on Consumer Bills

Costs	Option	Metric	Low	Medium	High
Options Impact on Consumers	Option 1 (Baseline)	Total Levy Claim	£0m	£0m	£0m
		Impact on 2023/24 bills	£0.0	£0.0	£0.0
	Option 2	Total Levy Claim	£48m	£51m	£53m
		Impact on 2023/24 bills	£1.70	£1.80³⁴	£1.90
	Option 3	Total Levy Claim	£81m	£119m	£157m
		Impact on 2023/24 bills	£2.90	£4.20	£5.50
	Option 4	Total Levy Claim	£84m	£125m	£166m
		Impact on 2023/24 bills	£3.00	£4.40	£5.90

³³ The licence modifications we introduced in early 2022 to allow for third-party financing of levy claims may help mitigate the immediate impact on consumer bills. If suppliers take up the option of third-party financing of SoLR levy claims, the impact of some of the costs on consumer bills may be spread over a longer period.

³⁴ Impact estimated based on expected total levy claim, apportioned to UK electricity network accounts as a proxy for households. Total impact apportioned across April 2023 to March 2024.

6.37. The direct financial impact of Option 2 is estimated to increase in wholesale element of the levy claim by £51m (or £1.80 per customer bill), compared to our baseline scenario of the claims we have already received (and expect to receive within the true-up process for this policy option) – ie option 1, limiting all wholesale cost recover to the duration of the 6-month SoLR direction.

6.38. We consider that allowing SoLRs to claim until the Summer 22 price cap adjustment is the appropriate course of action given the circumstances of the case, as outlined within Table 9. While it would result in some additional costs for consumers compared to limiting the claim strictly to 6-months from appointment, it is more consistent with our stated broad principle of no-gain/no-detriment through acting as SoLR during the crisis.

6.39. We consider that allowing SoLRs to claim for additional, unrecoverable costs up to the point of the price cap adjustment is in line with broad principle at the time of SoLR appointments that suppliers should be subject to no-gain/no-detriment if acting as a SoLR during the energy crisis, and on balance should represent a fair balance between the risk of adverse impacts on current consumers by allowing a longer recovery period in relation to which suppliers can claim costs and the risk of adverse impact and costs to future consumers.

6.40. We consider it to provide a measured and a proportionate approach to balancing the cost to current consumers of allowing a longer recovery period against the risk of adverse impact and costs to future consumers if our approach acts as a disincentive on suppliers to act as SoLR. It will also mitigate against the risk of overcompensating SoLRs, who are also being compensated through the broader measures introduced for all suppliers to recover costs faced during Winter 21 (outlined in chapter 1).

6.41. In addition, we have considered the potential for other secondary impacts on customers driven by these options. We do not expect there to be any other unintended risks to consumers from the implementation of this policy not already considered. Given we do not expect there be any material detriment to suppliers, we do not foresee any impacts on service quality provided by suppliers, or impacts on quality due to changes in competition.

Impact on suppliers

6.42. The key direct impacts of this policy on suppliers will involve the additional transfer of allowances to suppliers from the levy compared to what would occur under the baseline scenario. As part of our analysis, we have analysed the supplier level transfers for our options to each of the relevant suppliers who took on one of the 22 SoLR claims which were submitted within December 2021. For each supplier, we analysed the financial impact at an individual supplier level. The net aggregate flows to suppliers as part of the levy impacts are outlined below.

Table 10: Estimated Impact of Options on Suppliers (Levy flows to suppliers)

Costs	Option	Metric	Low	Medium	High
Options Impact on Consumers	Option 1	Levy Flows to Suppliers	£0m	£0m	£0m
	Option 2	Levy Flows to Suppliers	£48m	£51m	£53m
	Option 3	Levy Flows to Suppliers	£81m	£119m	£157m
	Option 4	Levy Flows to Suppliers	£84m	£125m	£166m

6.43. Suppliers will have incurred a set of incremental costs driven solely by their participation within SoLR. Our preferred option (option 2) will enable the costs directly attributable to delivering energy during the period of time a supplier has been directed to act as a SoLR to be claimed via the levy. Therefore, overall, we do not believe that suppliers will be left materially “out of pocket” because of their participation within the SoLR regime.

Other impacts

6.44. The SoLR Levy process is expected to lead to a direct transfer to suppliers, and an increase in energy bills for consumers within all options analysed, this could impact energy demanded and carbon emissions. We assume within this impact assessment, all other things being equal, that any increase in price could be expected to lead to a decrease in energy usage for these customers, and subsequently of emissions.

6.45. Given the small increase in bill levels (compared to overall energy bills) within the options we have analysed, we expect these increases to be immaterial. We subsequently expect there to be a limited environmental impact of this policy proposal. We also do not expect any potential for other impacts from this policy proposal on government or other industry participants.

6.46. Given that any bill impacts or impacts on supplier finances which we might expect are only a small proportion of overall energy bills expected for 2023/24, we do not expect a material impact on competition. The last resort levy claims true-up policy will only impact a limited number of suppliers who participated within the December 2021 claims process. We believe our proposed policy position fairly compensates these suppliers for participation within the SoLR process. We consider any risk of unintended impacts from our position that could impact the competitiveness (positively or negatively) of suppliers involved to be unlikely.

Appendix 3: Privacy notice on consultations

Personal data

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

1. The identity of the controller and contact details of our Data Protection Officer

The Gas and Electricity Markets Authority is the controller, (for ease of reference, "Ofgem"). The Data Protection Officer can be contacted at dpo@ofgem.gov.uk

2. Why we are collecting your personal data

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. ie a consultation.

4. With whom we will be sharing your personal data

We may share consultation responses with BEIS and HMT, where appropriate.

5. For how long we will keep your personal data, or criteria used to determine the retention period.

Your personal data will be held for six months after the project, including subsequent projects or legal proceedings regarding a decision based on this consultation, is closed.

6. Your rights

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data
- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it

- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3rd parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

7. Your personal data will not be sent overseas.

8. Your personal data will not be used for any automated decision making.

9. Your personal data will be stored in a secure government IT system.

10. More information: For more information on how Ofgem processes your data, click on the link to our "[Ofgem privacy promise](#)".