

Gas and Electricity Suppliers,
Electricity Distribution Network
Operators,
Gas Transporters and all other
interested parties

Email: solrlevyteam@ofgem.gov.uk

4 November 2022

Dear Colleague

Last Resort Supply Payment Claim from British Gas

On 19 July 2022, British Gas Trading Limited (“British Gas”) gave notice to Ofgem of its intention to make a claim for a Last Resort Supply Payment (LRSP). British Gas is seeking to recover additional, otherwise unrecoverable costs incurred in acting as Supplier of Last Resort (SoLR) to customers of the former Simplicity Energy Limited (“Simplicity Energy”).

Under Standard Licence Condition (SLC) 9.1 of the Supply Licence, SoLRs are entitled, provided Ofgem consents, to make a claim for a LRSP from each Relevant Gas Transporter and Electricity Distribution Network Operator. The claim from British Gas included its calculation of the claim amount and information to support the calculation (outlined in Table 1).

This letter sets out the reasons why we are minded to consent to British Gas claiming a LRSP of up to £3,024,176.70.

We are minded to allow British Gas to claim for costs incurred in complying with a Last Resort Supply Direction¹ relating to protecting the credit balances owed to former customers of Simplicity Energy.

The purpose of this consultation letter is to provide interested parties with an opportunity to make any representations to us, ahead of us making our final decision. We will take such representations into account in our final decision-making and may make changes to our minded to position in response to such representations, if we consider it appropriate to do so.

In addition, before we make our final decision we will conduct an additional assurance process in respect of the calculations contained in our minded to position, the results of which may also be reflected in our final decision.

We expect to make our final decision in mid-December 2022.

¹ [Direction to appoint British Gas Trading Limited as Electricity Supplier of Last Resort | Ofgem](#) and [Direction to appoint British Gas Trading Limited as Gas Supplier of Last Resort | Ofgem](#)

Background

The SoLR process

Electricity and gas supply is a competitive activity in Great Britain. While competition has the potential to bring many benefits to consumers, in a competitive market, companies that are not operating efficiently may fail. This applies as much in relation to the gas and electricity supply markets as it does to other markets.

It is Ofgem's statutory duty to protect customers' interests when suppliers fail. When a supplier fails, our focus is to ensure continuity of supply for its customers and to minimise wider negative impacts on the market. These wider effects stem from the fact that if an energy supplier fails, its customers will continue to be physically supplied with gas and/or electricity, but the supplier will not be able to meet the costs of providing this energy. In these circumstances, the costs of procuring the necessary energy will be spread across all domestic suppliers and the costs of procuring gas will fall to the relevant shipper. There is also the real risk that if a supplier fails without urgent intervention, consumer trust and confidence in the energy market would be materially damaged.

Ofgem can ensure continuity of supply to the failed supplier's customers and minimise these wider negative effects by appointing a SoLR, which is issued with a Last Resort Supply Direction requiring it to supply the failed supplier's customers at very short notice².

Simplicity Energy SoLR event

On 29 January 2021, we appointed British Gas as the SoLR for Simplicity Energy's gas³ and electricity⁴ customers, following its announcement that it had ceased trading. This followed an appointment process aimed at getting the best deal for consumers. We outlined the material factors behind our decision to appoint British Gas as the SoLR to those customers in our decision letter published on 3 March 2021⁵.

Claim for Last Resort Supply Payment

Under SLC 9.1 of the Supply Licence, SoLRs are entitled, with Ofgem's consent, to make a claim for a Last Resort Supply Payment ("LRSP") from each Relevant Gas Transporter and Electricity Distribution Network Operator.

SLC 9.4 provides that the total amount of the LRSP must not exceed the amount by which the total costs (including interest on working capital) reasonably incurred by the SoLR in supplying customers under the Last Resort Supply Direction and a reasonable profit plus any sums paid or debts assumed by the SoLR to compensate customers in respect of any customer credit balances plus any additional (actual or anticipated) interest and finance costs associated with a financing arrangement approved under SLC 9.7C are greater than the total amounts recovered by the SoLR through charges for that supply.

² The obligation for a supplier to comply with a LRSD derives from standard licence condition 8 of each supplier's gas and electricity supply licences and is intended to ensure a universal service for Great British energy consumers (for further information on this universal service, see Articles 3(3) of the EU Directives 2009/72/EC and 2009/73/EC).

³ <https://www.ofgem.gov.uk/publications/direction-appoint-british-gas-trading-limited-gas-supplier-last-resort-0>

⁴ <https://www.ofgem.gov.uk/publications/direction-appoint-british-gas-trading-limited-electricity-supplier-last-resort-0>

⁵ <https://www.ofgem.gov.uk/publications/appointment-british-gas-trading-limited-supplier-last-resort-0>

SLC 9.6 makes clear that Ofgem may determine that an amount other than the one calculated by the SoLR is a more accurate calculation of the relevant amount and, in such cases, the amount specified by Ofgem must be treated as the relevant amount when the licensee submits its claim to each relevant electricity or gas network licensee in accordance with SLC 9.8.

LRSPs are paid for by the relevant gas and electricity network operators, who then recover the cost through charges to suppliers. SLC 38B of the Electricity Distribution Licence and Standard Special Condition A48 of the Gas Transportation Licence set out the details of this.

Our decision process and methodology

Under SLC 9.5, Ofgem must decide whether it is appropriate in all the circumstances of the case for the SoLR to make the claim notified to it in accordance with Standard Licence Condition 9.3.

Our process to reach our minded-to position included:

- a. A quantitative check of British Gas's methodology for each cost item claimed. This included determining how each total cost item was calculated based on data sent to us by British Gas and ensuring these costs were in line with commitments British Gas made at the time of its SoLR appointment;
 - b. Undertaking validation of some assumptions with other data sources, where appropriate; and
 - c. A qualitative and quantitative assessment of the claim for costs related to credit balances in accordance with our criteria and methodology, set out below.
- **Additional:** whether the costs claimed are additional to the costs to the SoLR of existing customers. In addition, we consider whether these costs would have been expected at the time of the SoLR's bid and whether any commitments were given in relation to these costs in their competitive SoLR bid.
 - **Directly incurred as part of the SoLR role:** whether the costs were incurred as a result of taking on customers in an emergency situation as opposed to normal customer acquisition routes.
 - **Otherwise unrecoverable:** 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 – or reasonably be expected to recover – through the administration process or customer charges, for example.
 - **Economic:** whether the SoLR had made all reasonable efforts to avoid the cost in the first instance or absorb the cost.

British Gas's claim

British Gas indicated at the time of its SoLR appointment that it would not waive its right to make a claim for a LRSP and that it would claim for the cost of credit balance costs. It also

indicated that it was willing to absorb some of the costs of honouring customer credit balances.

Summary of our minded-to decision

British Gas submitted a claim for the costs of honouring the credit balances of open and closed accounts of Together Energy customers. Taking into account the costs that British Gas agreed to absorb, its final LRSP claim is for £3,051,383.74. Based on the specific circumstances of this levy claim case and the information provided to us by British Gas to support its claim, Ofgem is minded to consent to British Gas claiming a LRSP of up to £3,024,176.70.

Under the supplier SLCs we are required to consider on a case-by-case basis whether in the circumstances it is appropriate for a SoLR to make a claim for a LRSP. We have set out below our reasons for our minded-to position for this case. This should not be taken as setting a precedent for any future claims, which would also be considered on their merits and on a case-by-case basis, taking into account all relevant circumstances of the particular case.

Table 1: Summary table of submitted claim and minded-to position on final claim amounts.

Item	Cost	Cost Claimed (£)	Deductions (£)	Minded-to position on claim (£)
1	Credit balances	3,051,383.74	27,207.04	3,024,176.70
	Total	3,051,383.74	27,207.04	3,024,176.70

Reasons for our minded-to decision

Cost category: Credit balances

Our published guidance sets out that we may in certain circumstances consider it appropriate to approve a claim associated with costs incurred in repaying credit balances to customers who had a positive credit balance with a failed supplier.

Decision:

The British Gas LRSP claim of £3,051,383.74 includes:

- The cost of honouring the credit balances of the customers transferred to it through the SoLR process ('open accounts')
- The cost of honouring the credit balances that were owed to former customers of Simplicity Energy ('closed accounts'). This includes £27,207.04 for credit balances refunded by cheque that have not been cashed by the customer.
- A deduction to account for British Gas' commitment to absorb a set amount of credit balances.

We are minded to remove the costs for uncashed refund cheques from the claim and allow the other claimed credit balances. This results in a reduction to the claim of £27,207.04.

Rationale for decision:

Under Supplier SLC 9.4(b) a SoLR may claim any sums paid or debts assumed to compensate customers of the failed supplier respect of any customer credit balances. British Gas has requested our consent to recover £3,051,383.74 through a LRSP for the cost of refunding credit balances to customers and former customers of Simplicity Energy above the amount they agreed to absorb from their own revenues on their appointment as SoLR. We are satisfied in this case that the claimed amount for open account credit balances is consistent with the relevant criteria outlined above.

As part of our assessment of the closed account credit balances, our position is that amounts of credit balance refunds made by cheque should only be recovered by the supplier through the levy once that cheque is cashed. We do not consider that it would be appropriate to allow SoLRs to claim for closed account credit balance cheques until the point that they are actually cashed for the following reasons:

- To avoid consumers bearing the cost of compensation for credit balances never in fact received by customers of the failed supplier.
- To ensure that the SoLR does not profit from a situation where some credit balance cheques are never presented; and
- Noting that a future LRSP claim can be made so that British Gas can recover the cost of any credit balance cheques presented after the cut off point for the current claim.

Following the minded to deduction for uncashed cheques of £27,207.04, we consider that the claim is consistent with British Gas's commitment at the time of its appointment as SoLR for customers of Simplicity Energy. British Gas confirmed in its submitted claim that the claimed amount is consistent with the SLC 9.10 definition of credit, including that no incentive or reward payments, Warm Home Discount payments or compensation payments are included in the credit balance costs of either open or closed accounts. Additionally, where customer payments have been recovered from the administrator these have been accounted for and deducted from the claimed amount as appropriate.

British Gas provided evidence of its credit balance claim which included customer-level data for all open and closed accounts in addition to an explanation of how final credit balances were determined with the administrator. Our assessment of the claim included verifying the calculations that British Gas made and ensuring that any deductions were applied appropriately. Based upon the evidence provided to us, we consider that the claimed amount for honouring the credit balances of open accounts is consistent with our criteria for a valid LRSP claim and we are minded to consent to the claim.

We have considered whether the costs British Gas is seeking to claim for credit balances are otherwise unrecoverable; it may still be the case that British Gas is able to recover some of this claimed amount through the ongoing administration process for Simplicity, to which British Gas has, in accordance with the requirements of the LRSP process, submitted a subrogated creditor claim for the sums paid to compensate customers for costs incurred in repaying credit balances. We propose to make our final decision on British Gas's claim ahead of the conclusion of the liquidation process, the timescale of which is uncertain. Given this, we are minded to approve this element of the claim, subject to the outcome of the Simplicity liquidation process.

At this point, the final amount British Gas can claim would be adjusted to include costs recovered through the liquidation process.

Based upon our assessment of all the evidence provided we are minded to approve a LRSP claim for up to £3,024,176.70.

Next steps

The purpose of this letter is to provide the SoLR and interested parties with an opportunity to make any representations to us, ahead of us making our final decision on this LRSP claim. We invite any representations by **30 November 2022**. Responses should be emailed⁶ to solrlevyteam@ofgem.gov.uk.

We normally publish all responses on our website. However, if you do not wish for your response to be made public then please clearly mark it as not for publication. We prefer to receive responses in an electronic form so that they can easily be placed on our website.

We will take into account all relevant information, including any representations we receive, and the results of our internal audit of our assessment process in reaching our final decision on British Gas's claim. We expect to make our final decision in mid-December 2022.

Yours faithfully,

Neil Lawrence
Director, Retail Directorate

⁶ Although we prefer responses in electronic format, responses can be posted to the address below.