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20 December 2022

Dear Colleague

Last Resort Supply Payment Claim from ScottishPower Energy Retail Limited

On 7 October 2022, ScottishPower Energy Retail Limited ("ScottishPower") submitted a claim for a Last Resort Supply Payment (LRSP) for Ofgem's consent under Supply Licence Standard Licence Condition (SLC) 9. ScottishPower is seeking to recover additional costs incurred in complying with a Last Resort Supply Direction¹ to act as Supplier of Last Resort (SoLR) to customers of the former Entice Energy Supply Limited ("Entice").

On 4 November 2022 Ofgem published a minded to position in relation to that claim for consultation.² Responses to this consultation and consultations on other SoLR claims can be found within this document.

In addition, we conducted internal assurance of our minded to position.

Decision to consent

After taking into consideration the consultation responses and the results of our internal assurance process, on 20 December 2022 Ofgem consented to ScottishPower making a LRSP claim of up to £468,417.87.

This letter is the notice of reasons for Ofgem's decision to consent to ScottishPower making a LRSP claim from relevant network operators. Our decision will allow ScottishPower to claim for costs relating to:

- Additional wholesale costs incurred as a result of commitments to supply energy to SoLR customers;
- protecting the credit balances owed to former customers of Entice; and
- financing costs incurred on becoming a SoLR.

¹ [Direction to Appoint ScottishPower Energy Retail Limited as Electricity Supplier of Last Resort to Simply Your Energy Limited | Ofgem](#) (Simply Your Energy Limited traded as Entice Energy Supply Limited) and [Decision to Appoint ScottishPower Energy Retail Limited as Gas Supplier of Last Resort to Entice Energy Supply Limited | Ofgem](#)

² [Last resort levy True-up claim minded-to position | Ofgem](#)

We have assessed this LRSP claim in accordance with our policy decision on the True-up process, published 21 September 2022³, and consistent with our published *Guidance on supplier of last resort and energy supply company administration orders*.⁴ In addition, in making this decision, we have had regard to Ofgem's principal objective of protecting the interests of current and future energy consumers⁵, the public sector equality duty⁶, relevant licence provisions, and the particular circumstances of the case.

Nothing in this decision should 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.

An overview of ScottishPower's LRSP claim together with the reasons for decision with respect to this claim are set out below.

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. The failure of a supplier may affect a range of groups including its consumers, the wider market and other consumers. Ofgem has discretionary powers that enable it to address these consequences.

It is Ofgem's statutory duty to protect customers' interests when suppliers fail including their interests in the security of energy supply to them⁷. Under Supplier SLC 8 Ofgem can issue a Last Resort Supply Direction to direct any gas or electricity supplier to take over responsibility for a failed supplier's customers.

Generally, suppliers are open to taking on the role of SoLR because they acquire a large number of new customers who may remain with them over the longer-term and allow the supplier to increase its margins. As a result, suppliers may compete to be appointed.

In considering which supplier to appoint as SoLR, Ofgem must be satisfied that the SoLR can supply additional customers while continuing to supply its existing customers and to fulfil its contractual obligations for the supply of gas or electricity⁸.

Ofgem's criteria for the selection of a SoLR are set out in its "Guidance on supplier of last resort and energy supply company administration orders"⁹ and our stated policy preference is to appoint a SoLR that has volunteered for the role. To understand the terms on which suppliers are willing to volunteer as SoLR, Ofgem requires potential SoLRs to provide information about a number of issues, including customer service, how the supplier would meet SoLR obligations, whether it would make any LRSP claim and, if so, for what categories of costs and with what upper limit. This is done by way of a Request for Information (RFI).

³ <https://www.ofgem.gov.uk/publications/decision-last-resort-levy-claims-true-process>

⁴ https://www.ofgem.gov.uk/system/files/docs/2016/10/solr_revised_guidance_final_21-10-2016.pdf

⁵ s4AA Gas Act 1986 and s3A Electricity Act 1989

⁶ Equality Act 2010 Part 11 Sections 149 to 157 [Equality Act 2010 \(legislation.gov.uk\)](https://www.legislation.gov.uk/ukpga/2010/154/part_11)

⁷ See section 4AA (1A) (b) Gas Act 1986 and section 3A (1A) (b) of the Electricity Act 1989

⁸ See Supplier SLC 8(1)(b)

⁹ [Supplier of Last Resort: Revised Guidance 2016 | Ofgem](#)

Once a Last Resort Supply Direction has been issued, the responses to the RFI become supplier commitments, which under Supplier SLC 8.3 the SoLR must take all reasonable steps to honour. Under Supplier SLC 8 a supplier must comply with a Last Resort Supply Direction, whether or not it volunteered for the SoLR role.

As part of its regulatory responsibilities Ofgem has discretion under Supplier SLC 9¹⁰ to determine the amount of compensation that a SoLR can recover for additional costs incurred as a result of complying with a Last Resort Supply Direction¹¹. Ofgem's subsequent exercise of that discretion cannot be limited by any response that a supplier makes to an RFI before a Last Resort Supply Direction is issued. SLC 9 makes clear that in deciding whether or not to approve a SoLR levy claim, Ofgem must consider what it considers to be '*appropriate in all the circumstances of the case*'. In making that decision, Ofgem's principal objective is to protect the interests of existing and future consumers and we are very mindful that all amounts consented under SoLR levy claims are paid for by customers.

It is well understood by suppliers that Ofgem must make complex regulatory choices about the allocation of risks and when a supplier has failed. It must do so having regard to the future operation of the market. In particular, Ofgem must balance the need to ensure that its approach to claims for a LRSP ensures that suppliers are not disincentivised from volunteering to become SoLRs while not creating a moral hazard by encouraging suppliers to make commitments on the basis that any losses subsequently incurred could be recovered by way of a LRSP. This is a complex balancing assessment carried out by Ofgem as regulator, having regard to its principal objective to protect consumers.

Entice Energy SoLR event

On 30 November 2021, we appointed ScottishPower as the SoLR for Entice gas¹² and electricity¹³ 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 ScottishPower as the SoLR to those customers in our decision letter published on 18 March 2022¹⁴.

Last Resort Supply Payment

Under SLC 9.1, 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 Operator ("network operators").

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

¹⁰ See in particular Supplier SLC 9.5 and 9.6

¹¹ A consent given by Ofgem under SLC 9 may be varied, amended or remade and may be made subject to conditions – see Supplier SLC 2.7.

¹² [Ofgem appoints ScottishPower to take on customers of Entice Energy and Orbit Energy | Ofgem](#)

¹³ [Direction to Appoint ScottishPower Energy Retail Limited as Electricity Supplier of Last Resort to Simply Your Energy Limited | Ofgem](#) (Simply Your Energy Limited traded as Entice Energy Supply Limited)

¹⁴ [Appointment of ScottishPower Energy Retail Ltd as Supplier of Last Resort for Entice Energy Supply Ltd and Simply Your Energy Ltd | Ofgem](#)

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.

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 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.

Multi-stage claims

During winter 2021/22 we introduced a number of changes to the process for making LRSP claims, 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 process whereby SoLRs are able to submit more than one claim in relation to each Last Resort Supply Direction.

This involves SoLRs submitting an 'initial claim' for costs faced in serving SoLR customers (typically wholesale commodity costs) in the period immediately after appointment. SoLRs may then follow this claim with a subsequent claim (or claims) for any additional and otherwise unrecoverable costs reasonably incurred under their SoLR Direction. We refer to these additional claims as 'True-up' claims for additional costs reasonably incurred during the relevant period. SoLRs entered into a 'True-up Agreement' with Ofgem to support the faster process. Initial claim consents, subsequent claims and True-up claims are conditional on SoLRs complying with the True-up Agreement. The True-up process is intended to reconcile suppliers' initial claims with actual costs incurred and determine any additional payments or repayments that should be made.

In line with our faster, multiple claims process, by December 2021 we had consented to SoLRs making initial levy claims totalling £1.83 billion. At the time, we set out that we would give further due consideration to a number of issues and consult with stakeholders before assessing any subsequent claims by SoLRs who submitted initial claims.

On 23 June 2022, we issued a consultation seeking views 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 SoLR between September 2021 and December 2021. A decision document was published on the 21 September 2022¹⁵ that set out our policy decisions on the approaches SoLRs should take with regards to these True-up claims. We applied these policies in order to reach our minded-to position on this claim, which we published for consultation on 4 November 2022.

¹⁵ [Decision on the last resort levy claims True-up process](#)

Decision-making process

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. In making this decision Ofgem has considered evidence provided by ScottishPower, its own knowledge of the energy markets, and responses to consultation on the minded-to position on this claim.

In exercising this decision-making function Ofgem has had regard to the interests of current and future consumers of gas and electricity and has considered the public sector equality duty.

Ofgem published a minded-to position on this claim and invited consultation responses. ScottishPower was offered the opportunity to meet with us to clarify aspects of the minded-to position during the consultation period. In reaching its decision Ofgem has taken into consideration any additional evidence provided by ScottishPower during the consultation period and any consultation responses received in relation to the published minded-to position.

In reaching its decision Ofgem carried out:

- a. A quantitative check of ScottishPower methodology for each cost item claimed. This included determining how each total cost item was calculated based on data sent to us by ScottishPower and ensuring these costs were in line with commitments ScottishPower made at the time of its SoLR appointment;
 - b. A True-up and cross check of any evidence that may result in a change to the initial claim made by the SoLR;
 - c. Undertaking validation of some assumptions with other data sources, where appropriate;
 - d. Review and assurance of the calculations made in the published minded-to position; and
 - e. A qualitative and quantitative assessment of the claim for costs related to wholesale costs, credit balances and financing costs 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.

Overview of ScottishPower's claim

ScottishPower indicated at the time of our SoLR appointment process that it would waive its right to make a claim for a LRSP for certain other costs but that it would claim for the cost of wholesale, credit balances and working capital costs.

The initial claim(s) were consented to on 17 December 2021¹⁶. Consistent with the terms of that consent and the True-up Agreement between the SoLR and Ofgem, we have taken that claim into consideration in reaching our decision on this claim.

Summary of decision

Ofgem has consented to ScottishPower claiming a LRSP of up to £468,417.87 conditional on ScottishPower confirming that this claim is a Subsequent Levy Claim for the purposes of the True-up Agreement and that the terms of the True-up Agreement continue to apply to this and subsequent claims in respect of the Last Resort Supply Direction.

The reasons for the decision are set out below. This decision 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.

Table 1: Summary table

Item	Cost	Initial Claim Approved	True-Up claim (this claim)	Minded-to deductions on this claim	Decision on deductions for this claim	Amount approved for this claim
1	Wholesale	£2,377,284.47	£183,419.36	£98,344.44	£98,336.66	£85,082.70
2	Credit balances	£0.00	£359,847.56	£28,468.83	£28,468.83	£331,378.73
3	Working capital	£0.00	£51,956.44	£0.00	£0.00	£51,956.44
Total:						£468,417.87

General points raised in consultation

Summary

We received eight responses to our minded-to positions, with seven responses from SoLRs and one from a consumer group. We received wide-ranging support and recognition for working efficiently throughout the assessment period to ensure each LRSP claim was given due consideration whilst maintaining engagement stakeholders. We note several general points made by suppliers on the wider SoLR levy process, including the potential for further claims, and concerns regarding the policy decision to limit the additional, otherwise unrecoverable, wholesale costs that SoLRs can claim to

¹⁶ [Faster SoLR levy process: consents to Last Resort Supply Payments | Ofgem](#)

the cost of energy delivered by the end of March 2022, or within six months of being appointed, whichever is later, the latter of which we have responded to in the wholesale section of this document. We have expanded below upon each general issue raised in consultation responses to the minded to position.

Changes in approach during consultation

Several suppliers claimed in their consultation responses that we had changed our approach during the process, including one supplier who believed that Ofgem had disallowed sums previously agreed in principle. Ofgem made it clear throughout the entirety of the claims process that we would assess each claim on a case-by-case basis, considering the evidence and circumstances of each case before making a decision. Ofgem could not have made a decision on claims before considering all the information provided by SoLRs and any responses to our consultation on our minded-to positions. This was clear from our minded-to positions, which explained that the purpose of the consultation letter was to provide interested parties with an opportunity to make any representations to us, ahead of us making our final decision and that we would take such representations into account when reaching our final decision, making changes to our minded to position if considered appropriate. We also made it clear that our decision might reflect changes resulting from an additional assurance process.

This applies to all LRSP claims made by SoLRs. Ofgem has exercised its statutory discretion to ensure all decisions are fair and reasonable, taking into account the statutory framework, the relevant licence conditions, all the relevant circumstances and no irrelevant factors. The reasons for our decisions with respect to this claim are set out in subsequent sections of this letter. 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 the relevant circumstances of the particular case.

Volunteering to be SoLR in the future

Several suppliers noted that, due to our positions on certain elements of their claims, they may be less willing to volunteer as SoLR in the future. We note suppliers' concerns. However, Ofgem must make complex regulatory choices about the allocation of risks and costs in the event that a supplier has failed and must do so having regard to the future operation of the market¹⁷.

'In particular, Ofgem must balance the need to ensure that its approach to claims for a LRSP ensures that suppliers are not disincentivised from responding to the SoLR RFI to become SoLRs, whilst not creating a moral hazard, namely, circumstances where suppliers do not respond appropriately or take excessive risks when responding, knowing that any losses subsequently incurred could be recovered by way of a LRSP. This is a complex balancing assessment carried out by Ofgem as regulator, having regard to its principal objective to protect consumers¹⁸.'

We are confident that the process we have undertaken for assessment of these claims has been appropriate, in particular to protect consumers during the current cost of living

¹⁷ see *R (on the application of Scottish Power Energy Management Ltd v Gas and Electricity Markets Authority)* [2005] EWHC 2324 (Admin) paragraph 97.

¹⁸ see *R (on the application of Scottish Power Energy Management Ltd v Gas and Electricity Markets Authority)* [2005] EWHC 2324 (Admin) paragraph 97.

crisis. In exercising its statutory discretion Ofgem has ensured all decisions are fair and reasonable, taking into account the statutory framework, the relevant licence conditions, and to be reasonable in all the circumstances.

Lack of sufficient evidence

One supplier noted that they were surprised by Ofgem's statements regarding a lack of sufficient evidence being provided to support claims. Where we have identified insufficient evidence, teams have worked to engage with SoLRs throughout the process to raise issues and request further information where appropriate to ensure that sufficient evidence is provided for us to consider. We are grateful for all SoLRs continuing engagement in this regard. As noted in the policy decision we published in September 2022, the consultation provided interested parties with an opportunity to make representations to us, ahead of us making our final decision. During the consultation period we engaged with SoLRs that had not submitted enough evidence initially, giving them an opportunity to provide more and better evidence for Ofgem to consider. Ofgem has carefully scrutinised the evidence provided by SoLRs in relation to each claim and where it considers the evidence provided to be insufficient, has only allowed claims if additional evidence has been provided which justifies that the costs claimed (or an element of those costs) should be approved. We believe that this was a reasonable approach to balancing the need for rigorous and robust evidence, whilst recognising the need for suppliers to be compensated for costs meeting our criteria described above as a result of acting as a SoLR.

External Assurance

The consumer group restated the view, previously put in their response to our September policy consultation, that external assurance of all LRSP claim is required. Due to the scale of the LRSP claims, they do not believe that an internal audit is sufficient. We have decided to apply the policy decision published in September and not to require external auditing of these LRSP claims. This is because we consider that adding a requirement for external audit at this stage would be unreasonable. We will, however, consider this point ahead of any future LRSP claims.

Further claims

Several suppliers voiced their view that further LRSP claims should be permitted, generally to allow further reconciliation of wholesale costs incurred. The possibility of further claims was echoed by the consumer group, which considered that further claims may be required to ensure that SoLRs are not overcompensated. However, the consumer group also pointed to the clear commercial incentive SoLRs have to use any further claims to argue that they have been undercompensated.

As part of that faster multiple-claim levy process, each of the SoLRs entered into a true-up deed with us. Under the True-up Agreement between ScottishPower and Ofgem, Subsequent Levy Claims may be made following the Initial Levy Claim and before a final True-up claim. As set out in the consultation for this claim, we were minded to consider this claim to be a Subsequent Levy Claim for the purposes of the True-up Agreement.

Following the consultation on this claim, we consider that this remains a reasonable approach. Accordingly, Ofgem has made its consent to this LRSP claim conditional on confirmation by ScottishPower that this claim is a Subsequent Levy Claim for the

purposes of the True-up Agreement and that the terms of the True-up Agreement continue to apply. This includes an obligation to submit true-up information as requested and to refund any amounts by which ScottishPower has been overcompensated by a LRSP.

This would mean that the final True-up claim under the True-up Agreement will be made next year or later. This will allow additional time for suppliers to provide additional supporting evidence for the limited instances where we have specified that our decision on certain costs is not final. In addition, this will allow additional time to make the final True-Up decision to ensure that the benefit of any monies recovered from the administrators of the failed suppliers can be utilised for consumers' benefit.

For the avoidance of doubt, unless we have specified otherwise in respect of certain costs suppliers are seeking to claim, our decision on each Subsequent Levy Claim is a final decision, and we do not expect suppliers to seek to revisit those final decisions.

We have made clear in this decision where we consider that we have not yet made a final decision on a particular element of this subsequent claim; and/or where we expect to make a revision to the amounts approved here under the True-Up Deed (or amended or otherwise varied consent), especially should additional evidence be forthcoming or once additional validations have taken place.

Status of SoLR RFI responses

We note that when suppliers respond to an RFI to become a SoLR, they may include certain requests in their response to the RFI and ask us to consider them, for example the recovery of costs over a longer period. However, while we use the information provided in responses to the information request issued at the time of the SoLR appointment to inform our decision on which supplier to appoint, this should not be seen as an endorsement of any particular requests that a supplier included in their RFI response. The supply licences provide that the SoLR would be able to make a claim to recover its reasonable incremental costs incurred in taking on the new customers where those costs are additional to the total amounts recovered from the customers for the supply where it has not waived its right to do so. We cannot give assurance, prior to the appointment of the SoLR, as to what costs can be claimed for, or over what period. The onus is on the SoLR to submit a claim that is supported by evidence and demonstrates why the amounts claimed meet the criteria for SoLR levy claims and should be allowed. Ofgem will then take all relevant information into account in deciding on whether to consent to any claim, or not, given all the circumstances of the case.

Reasons for decision

General

Ofgem's general preference is for a SoLR not to make a claim for a LRSP for costs it has incurred carrying out its role. However, we do recognise that circumstances may exist which would justify a departure from this general rule and that the costs of this claim will ultimately be paid by consumers. In our assessment of the claim, consideration has been given to the interests of current and future consumers, particularly those in more vulnerable circumstances.

Historically, some SoLRs have waived their right to make that claim through the SoLR processes. Recent SoLRs have not waived those rights as the recent costs associated with becoming a Supplier of Last Resort have been significant. In the particular

circumstances of this claim, and in line with the relevant licence conditions, we consider it appropriate to allow for the additional and otherwise unrecoverable costs summarised in Table 1 to be recovered via a LRSP.

In granting consent for this claim, the net costs incurred by the supplier acting as a SoLR in an emergency situation will be spread across all consumers, rather than borne solely by the SoLR and its customers. We consider it to be in the interest of current and future consumers to allow this claim to ensure that the consumer safety net provided by the SoLR process remains viable into the future, and the stability of the retail energy market is not further undermined to the detriment of all consumers.

Condition

Ofgem has made its consent to this LRSP claim conditional on confirmation by ScottishPower that this claim is Subsequent Levy Claim for the purposes of the True-up Agreement between ScottishPower and Ofgem and that the terms of the True-up Agreement continue to apply to this and subsequent claims in respect of the Last Resort Supply Direction. We have made this decision because it has the effect of allowing additional time to finalise claims for LRSPs following multiple Last Resort Supply Directions in difficult market conditions. We consider that it will enable suppliers to provide additional supporting evidence for costs that have not yet been approved by Ofgem, as well as allowing Ofgem to ensure the benefit of any monies recovered from the administrators of the failed suppliers can be utilised for consumers' benefit.

Cost category: Wholesale

In our published decision on the claims True-up process¹⁹ we explained that all SoLRs appointed in the period from September – December 2021 should be able to recover additional and otherwise unrecoverable wholesale costs reasonably incurred as part of the SoLR role relating to energy delivered up until 31 March 2022 or until the end of their 6-month SoLR direction, whichever is later. This has been necessary largely as a result of a period of extreme wholesale energy price volatility and record high prices seen, resulting in wholesale direct fuel costs often far exceeding those assumed in the default tariff price cap over the period. The bulk of these costs were considered in the December 2021 initial claim, by which time most initial wholesale energy purchases had taken place.

In this assessment we have analysed the information provided by suppliers, to:

- Assess whether costs being claimed for are consistent with the criteria set out earlier in this letter and our September 2022 Decision on the True-up process
- Assess the reasonableness of assumptions made and decisions taken, including for example demand forecasting and hedging strategies, against the criteria we consider in assessing claims
- Assess the specifics of the reported wholesale market trades, including trade date, contract type, price, and volume. Specifically, we have considered whether trade prices are consistent with market benchmarks and price assessments
- Assess cost per MWh and cost per customer to facilitate comparisons between claims

¹⁹ [Decision on last resort levy claims True-up process | Ofgem](#)

- Assess the amounts deemed to have been recovered from customer charges, including the applicability of various price cap allowances, and hence offset against the wholesale costs incurred

Decision

The ScottishPower True-up claim for Entice submitted on 7 October 2022 includes £183,419.36 in wholesale costs. Following the above assessments, and having considered the responses received to our minded to position consultation, as well as carrying out further assurance of our own calculations we consider that the claimed amount is not fully consistent with our criteria, and we have decided to consent to the claim with the following deductions:

- A deduction of £56,004.86 has been made for ScottishPower as part of our final decision for the revenue received from SoLR customers in respect of the Backwardation allowances in the price cap. Our final decision is unchanged from our minded to position, other than a small adjustment to reflect rounding.
- A deduction of £42,331.80 has been made for ScottishPower as part of our final decision for the revenue received from SoLR customers in respect of the Contracts for Difference (CfD) Interim Levy Rate (ILR) allowance in the price cap in cap period 7. Our final decision is unchanged from our minded to position, other than a small adjustment to reflect rounding.

The final total deduction for ScottishPower is £98,336.66, which is £7.78 lower than the proposed deduction of £98,344.44 in the minded-to decision. This results in a net wholesale True-up claim of £85,082.70, as opposed to £85,074.92 set out in the minded-to decision. When accounting for the initial claims made in December 2021, the total wholesale costs approved are £2,462,367.17, as opposed to £2,462,359.39 set out in the minded-to decision.

Table 2: Summary of wholesale costs

Item	Cost	Initial Claim	True-up claim	Deduction category	Deduction amount (minded -to)	Deduction amount (final decision)	Minded-to position on claim	Final position on claim
1	Wholesale	£2,377,284.47	£183,419.36	Backwardation	£56,039.32	£56,004.86		
				Contracts for Difference	£42,305.12	£42,331.80		
							£85,074.92	£85,082.70

Note: We are unable to calculate the proportion of the wholesale claim made up of backwardation and CfD. As such, we have shown the deductions above in relation to the overall wholesale claim.

Backwardation

Summary of minded-to position

In February 2022 Ofgem introduced a retrospective allowance into the default tariff cap to allow suppliers to recover the systematic and unrecoverable backwardation cost for suppliers, beyond the normal basis risk inherent in the cap. An amount of £8 per customer (at typical consumption) was included within the cap for the year starting 1 April 2022, and a further allowance of £6 per customer was introduced in August 2022, to be recovered in the year from 1 October 2022.

In our minded-to decision, the relevant backwardation deduction for each supplier was based on our best view (given the information submitted by the supplier as part of its claim) of:

- a. the number of SoLR customers that remained with that supplier as of the end of winter 2021/22 and
- b. the annualised demand of those customers.

We noted that we preferred this to an approach based on suppliers' own forecasts of their SoLR customers' demand in the period from 1 April 2022, because the latter approach would result in deductions that are dependent on suppliers' forecasts of future customer numbers which have proved to be highly uncertain and prone to error in this unprecedented time for the market (as seen by previous 'unexpected SVT demand' allowances). We preferred it to an approach based on the number of SoLR customers at the time of appointment, because that approach would not account for the fact that some SoLR customers may have since switched to fixed tariffs or other suppliers which did not take on any SoLR customers in winter 2021/22.

Summary of consultation responses

In relation to the standardised backwardation deduction, three suppliers that responded to our consultation confirmed that they understood and did not oppose the rationale for making this deduction in principle. Some respondents raised challenges regarding the specific demand-base used, suggesting that this would overstate the revenue that would be recovered under the backwardation allowance. One supplier questioned whether the deduction was consistent with Ofgem's decision not to allow claims for costs relating to supply after the six-month direction period.

Specifically in relation to this claim, ScottishPower told us that it understood the thinking behind the proposed backwardation deduction, but that it did not consider the decision to make this deduction to be reasonable because it was inconsistent with Ofgem's position to not allow claims for wholesale costs relating to energy delivered after the six-month direction period.

It also noted that Ofgem's calculations do not account for customer churn and, given this, it is very likely the deduction will be overstated. Therefore, if Ofgem maintains its minded-to position, ScottishPower would expect to submit a further True-up claim.

Reasons for decision

We have decided to deduct an amount from ScottishPower's claim to reflect the backwardation allowances in the cap, for the reasons set out in our minded-to position.

We do not agree with ScottishPower's submission that deducting an amount to reflect the backwardation allowance is inconsistent because it will be recovered (in part) after the direction period. This is because what matters when preparing claims is not the date on which the payment was made or received by the supplier (subject to this taking place within five years of the end of the direction period), but instead the supply period to which the amount relates. The backwardation allowance was specifically designated to allow suppliers to recover costs incurred in relation to energy delivered to SoLR customers in winter 2021/22, and so *within* the six-month direction period that is the subject of the claim. Therefore, it is correct that we should include an equivalent amount to the revenue expected to be received under the retrospective backwardation allowance when considering what part of the total amount recovered through charges for the supply of gas and electricity to SoLR customers under the last resort supply direction it is relevant to deduct from the costs presented in suppliers' claims. Failing to deduct this amount from claims would cause the same costs to be recovered twice – first via the price cap allowance, second via the SoLR claim.

We have decided that it will be open to SoLRs to submit a further claim in 2023 in relation to the backwardation deduction if they consider that new evidence exists to support such a claim. We note that an important consideration in assessing any such claim will be the extent to which it is appropriate to base the amount to be deducted on outturn demand, rather than seasonally normal demand (given the potential inconsistency with how costs for winter 2021/22 have been treated).

Finally, we note that, in calculating the backwardation deduction for the minded-to decision, Ofgem relied on inputs which were rounded to different numbers of decimal places. For consistency, we have for our final decision used unrounded inputs, as they appear in the relevant workbook submitted by suppliers alongside their claim, or annex to the default tariff cap. This results in small adjustments to backwardation deductions for all claims.

Contracts for Difference

Summary of minded-to position

The default tariff cap relating to electricity customers includes an allowance for costs incurred in relation to the CfD scheme, which is a government scheme aimed at supporting low carbon electricity generation. The charges that suppliers face under the CfD scheme depend on wholesale electricity prices, with higher prices resulting in lower costs for suppliers (all else equal). The allowance included in the cap is based on Low Carbon Contract Company (LCCC) forecasts of the relevant charges as they exist prior to

the cap being set,²⁰ which are in turn based on forward prices observed at that time of the forecast.

The increases in wholesale prices which followed the cap for winter 2021/22 being set in August 2021 led to SoLRs paying prices for wholesale electricity for the customers of the failed suppliers which were well in excess of the direct fuel allowances included in the cap. However, increases in wholesale electricity prices also resulted in CfD costs for those customers that were significantly lower than the relevant allowance in the cap.

As we set out in our February 2022 price cap decision on the potential impact of increased wholesale volatility on the default tariff cap, for non-SoLR customers, this benefit was not realised in most cases, as suppliers had hedged their CfD risk earlier in 2021, when wholesale prices were lower. However, we consider that this is unlikely to apply to SoLR customers. This is because, where a supplier hedged their CfD exposure for SoLR customers, this would have been at much higher wholesale prices given the timing of the SoLRs, locking in a lower CfD cost than included in the cap. And where a supplier did not hedge, they would have realised the outturn CfD cost – which given high Day Ahead wholesale prices would have been a net payment back to the SoLR in question through the CfD scheme.

To avoid SoLRs over-recovering in relation to wholesale costs of their SoLR customers, we were therefore minded to deduct an amount from claims equivalent to the demand-weighted interim levy rate component of the default tariff cap for period 7 multiplied by the volume of electricity being claimed for, on the basis that the revenue generated under the CfD allowance would have offset the wholesale costs incurred by suppliers.

Summary of consultation responses

In relation to the standardised CfD deduction, three suppliers that responded to our consultation confirmed that they understood and did not oppose the rationale for making this deduction, and one supplier did not comment on this deduction. Some respondents raised challenges at the demand-base used. One supplier questioned if the CfD deduction was consistent with the rest of the price cap, and that Ofgem were being selective about deductions made when some elements of the price cap may adversely affect suppliers.

Specifically in relation to this claim, ScottishPower did not comment on the CfD deductions.

Reasons for decision

Our decision to disallow an amount from the ScottishPower claim to reflect the CfD allowance in the price cap remains unchanged from our minded-to position.

Finally, we note that in calculating the CfD deduction for the minded-to decision, Ofgem relied on inputs which were rounded to different numbers of decimal places. For consistency and greater accuracy, we have for our final decision used unrounded inputs, as they appear in the relevant annex to the default tariff cap. This results in small adjustments to the CfD deductions for all claims.

²⁰ [August 2021, Default tariff cap, Annex 4](#)

Claims for costs relating to supply beyond the six-month direction period

Summary of minded-to position

In our decision on the last resort levy claims True-up process published on 21 September 2022,²¹ we set out our position that - where appropriate - SoLRs appointed during the period September – December 2021 would be allowed to apply to recover additional and otherwise unrecoverable wholesale costs incurred relating to energy delivered up until 31 March 2022, or within six months of being appointed, whichever was later. We said²² that it would not be proportionate to allow a blanket extension to allow SoLRs to recover costs via the levy throughout summer 2022 (i.e. beyond the six-month direction period), recognising that while some SoLRs may consider there is still a portion of costs they should be able to claim that are unrecoverable, we did not consider these costs to be directly related to their role as SoLR, and other suppliers would face similar costs as a result of higher than anticipated volumes of customers remaining on the standard variable tariff. We explained that while this would be our broad approach when assessing claims - because we considered that it best balanced the interests of consumers and fairness between suppliers - we would also consider whether the circumstances of any specific claim warranted exceptional treatment.

In the September 2022 decision, we also noted that when we initiate a competition for the appointment of a SoLR, we issue a RFI to suppliers. In their responses, suppliers may include certain requests and ask us to consider them, for example the recovery of costs over a longer period. However, while we use the information provided in responses to the information request issued at the time of the SoLR appointment to inform our decision on which supplier to appoint, this should not be seen as an endorsement of any particular requests that a supplier included in their RFI response. The supply licences provide that the SoLR would be able to make a claim to recover its reasonable incremental costs incurred in taking on the new customers where those costs are additional to the total amounts recovered from the customers for the supply where it has not waived its right to do so. We cannot give assurance, prior to the appointment of the SoLR, as to what costs can be claimed for, or over what period. The onus is on the SoLR to submit a claim that is supported by evidence and demonstrates why the amounts claimed meet the criteria for SoLR levy claims and should be allowed. Ofgem will then take all relevant information into account in deciding on whether to consent to any claim, or not, given all the circumstances of the case.

As described in our minded-to letter, ScottishPower has submitted two claims, one covering wholesale energy costs to the end of May 2022, in line with our September policy decision, and the other covering wholesale costs to end the September 2022. In that letter we set out our view that the evidence provided by ScottishPower was not sufficient for us to change our September policy position to allow them to exceptionally claim costs up to the end of September 2022. Were additional evidence to be provided to justify a claim over a longer period, we would be open to considering it as part of the True-up process.

²¹ [Decision on the last resort levy claims True-up process](#)

²² Ibid paragraph 3.8

Summary of consultation responses

In its response to our consultation, ScottishPower reiterated its view that the costs relating to hedging customers' demand for summer 2022 aligned with Ofgem's criteria. It stated that Ofgem's approach (not to allow costs for the full summer period) would discourage suppliers from entering future SoLR processes, and was discriminatory, favouring suppliers which were appointed as SoLRs earlier. It also argued that it had set out in its response to our SoLR RFI its intention to claim for the summer as well as the winter period, and highlighted that it absorbed certain operational costs on the basis that it would be able to recover valid wholesale costs via the levy claim.

Reasons for decision

We have decided not to allow ScottishPower to claim for wholesale costs relating to the supply of energy to SoLR customers which took place subsequent to the six-month direction period. This decision is in line with the policy position published in September 2022. The evidence presented and arguments raised by ScottishPower do not, in our view, demonstrate that ScottishPower claim was exceptional, or should be treated differently to the claims of other suppliers for the same period. Rather they relate to the impact of high wholesale prices; the mechanics of the price cap methodology; and/or the fact that their appointment as SoLR took place after the observation window for summer 2022 opened – factors which were common to all SoLRs appointed in winter 2021/22. Given this, we consider it to be in consumers' interests to limit the claim to the six-month direction period set out in the licence condition, for the reasons set out in our September decision.

Cost category: Credit balances

Under SLC 9.4(b) a SoLR can claim 'any sums paid or debts assumed by the licensee to compensate any Customer in respect of any Customer Credit Balances'.

Decision

ScottishPower claimed £359,847.56 in compensation to former customers of Entice for their credit balances. We consider that the claimed amount is consistent with our criteria. We have consented to ScottishPower claiming £331,378.73 for sums paid to compensate customers for credit balances, with a deduction of £28,468.83 for uncashed cheques.

Table 3: Summary of claims and decision for credit balances

Item	Cost	Initial Claim	This claim	Minded-to deductions	Decision on deductions	Decision on this claim
2	Credit Balances	£0.00	£359,847.56	£28,468.83	£28,468.83	£331,378.73

Summary of minded-to position

ScottishPower requested our consent to claim £359,847.56 through the LRSP for the cost of refunding credit balances of customers and former customers held at the time the Entice direction was issued and stated it would reduce its claim to reflect any uncashed element.

In our minded-to position, we noted that SoLR could claim sums paid or debts assumed to compensate customers of the failed supplier in respect of customer credit balances.

We were minded to not allow claims for the value of uncashed cheques where the SoLR had compensated customers for credit balances by sending cheques. In our minded-to position, we explained that this was because we did 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 ScottishPower can recover the cost of any credit balance cheques presented after the cut off point for the current claim.

In our minded-to position, we considered whether the amount ScottishPower is seeking to claim for credit balances is otherwise unrecoverable; it may still be the case that ScottishPower is able to recover some of this claimed amount through the ongoing administration process for Entice to which ScottishPower has, in accordance with the requirements of the LRSP process, submitted a subrogated creditor claim for the sums paid to compensate customers for credit balances. In our minded-to position, we noted that, as we propose to make our decision on the claim ahead of the conclusion of the liquidation process, the timescale of which is uncertain, we were minded to approve this element of the claim, subject to the outcome of the Entice liquidation process.

Summary of consultation responses

We received one stakeholder response from British Gas to our minded-to position on credit balances. British Gas stated that it supported our stance of allowing all credit balances refunded to customers to be reclaimed via the levy. It also stated that it supported the pragmatic approach for uncashed cheques that will allow it to claim any issued cheques that are cashed by customers in the future.

Reasons for decision

ScottishPower requested our consent to recover £359,847.56 for the cost of refunding credit balances to some former customers of Entice and stated it would reduce its claim to reflect any uncashed element. In our minded-to position, Ofgem stated that, in principle, we were minded to allow the claim, with deduction for the value uncashed cheques. We have considered the consultation responses, noting that no objections were raised to the approach proposed on uncashed cheques, and one supplier noted their support for this approach. We are satisfied that the claim is consistent with our criteria

and have decided to consent to a LRSP claim of £331,378.73 for sums paid to compensate customers for credit balances, with a deduction of £28,468.83 for uncashed cheques consistent with ScottishPower's position.

Cost category: Working capital

The policy decision on last resort levy claims True-up process²³ explained what would be required for SoLRs to claim for financing or working capital costs incurred. The policy decision also set out the requirement for suppliers to demonstrate, with evidence, that their financing cost claim delivers value for money for consumers and is the best possible rate they could achieve given their individual circumstances.

Decision

ScottishPower claimed £57,676.73 for the cost of working capital, followed by a revised claim totalling £51,956.44. The calculation includes costs incurred to reflect actual costs incurred and the timescale for the recovery of those costs as set out in our published policy decision.

We consider that the revised claim amount is consistent with our criteria. We have consented to ScottishPower claiming that amount as part of an LRSP.

Table 4: Summary of claims and decision for working capital

Item	Cost	Initial Claim	True-up claim	Revised True-up	Minded-to deductions	Decision on deductions	Decision on this claim
3	Working capital	£0.00	£57,676.73	£51,956.44	£0.00	£0.00	£51,956.44

Summary of minded-to position

ScottishPower submitted a claim for the cost of working capital amounting to £57,676.73. It submitted evidence that detailed its expenditure relevant to its claim for working capital costs, as well as justification for why it had applied the interest rate that it had. Based upon our assessment of the submitted evidence against our overall criteria, which included reviewing commitments made when ScottishPower was appointed as SoLR and comparing the rate against all other claims submitted to Ofgem on 7 October 2022, we stated in our minded-to letter that we were satisfied that ScottishPower has provided adequate evidence to demonstrate the rate of interest they faced in respect of working capital costs is reasonable. We further stated that we believe that ScottishPower's proposed rate is reasonable when compared against the range of rates secured for initial claims and the overall market movements since the submission of initial claims. Our decision on the reasonableness of the rate applied by ScottishPower applies in this case, and for this purpose only, and means that we may take a different view as to what is a reasonable rate, or approach to, financing for other purposes or in other cases.

²³ [Decision on the last resort levy claims True-up process](#)

Resubmission of claim for working capital

In our minded-to letter we stated that working capital may only be claimed on costs that meet our criteria for assessing claims²⁴. In light of our minded-to position to make deductions to other cost categories and/or to make deductions where further evidence is not forthcoming, the total amount of working capital claimed for of £57,676.73 was subject to ScottishPower resubmitting a revised working capital claim taking into account the deductions in our minded-to position. In order to fully assess the working capital aspect of the claim, we therefore required ScottishPower to recalculate the working capital element of their claim using, as costs incurred, the amounts we stated we were minded to consent to in our minded-to letter.

In our minded-to letter we also stated our expectation that ScottishPower should follow the same methodology, and apply the same rate, as their 7 October submission, and to clearly set out which costs have been reduced or removed. We also asked that ScottishPower submitted their full calculations to allow us to undertake these calculations on working capital unilaterally for our decision, so that we can work out what their working capital allowance should be, without having to revert to ScottishPower. While we noted that, based on the evidence submitted to us, the claim appeared consistent with our criteria, in order to arrive at a decision on working capital costs we required that suppliers submit to us their calculations that we could unilaterally validate and replicate and amend for final decision, without having to revert to the supplier. In the minded-to Position process, we had been unable to replicate what suppliers had done on working capital, and could not deduct the disallowances made through the minded-to position.

In our minded-to letters we requested that the SoLRs provide further evidence which would allow us to effectively assess the costs claimed against our criteria. With the exception of one supplier, all SoLRs provided the evidence required from them in order to support their working capital claims. We thank suppliers for being so engaged with Ofgem during the consultation period.

Summary of consultation responses

Ofgem thanks suppliers and consumer groups for responding to our consultation, and for their active engagement with the consultation process, and Ofgem, during this period. We did not receive any specific comments on our minded-to position on working capital costs from ScottishPower in relation to this claim.

Reasons for decision

As noted above, ScottishPower submitted a revised working capital claim totalling £51,956.44, taking into account the deductions in our minded-to position. The re-submitted calculations were sufficiently clear to allow us to unilaterally undertake additional recalculations to account for adjustments to the deductions set out in our minded-to letter. No additional evidence was required from ScottishPower.

²⁴ [Last resort levy true-up claim minded-to position | Ofgem](#)

Based upon our assessment of the evidence provided, the submitted re-calculation of the claim, and the relevant consultation responses received, we consider that the rate at which working capital has been calculated, and the methodology followed, is consistent with our criteria and reasonable in this case, and for these purposes only. Our decision on the reasonableness of the rate applied by ScottishPower applies in this case, and for this purpose only, and means that we may take a different view as to what is a reasonable rate, or approach to, financing for other purposes or in other cases.

In arriving at our decision on whether the rate submitted by ScottishPower demonstrated that their financing cost claim delivered value for money for consumers, and considering the evidence submitted to us as part of the consultation process, we have undertaken the following approach. For companies that secured financing through intra-group company arrangements, we have looked at whether the rate secured through these arrangements could have been improved had the supplier gone to market. In order to undertake this assessment, we looked at the range of rates approved in the initial claims, and the market movements since the initial claims decision. For companies that have gone to market for their financing, we looked at the rate that they have claimed for, and whether that rate is consistent with the range of rates approved in the initial claims, and the market movements since the initial claims decision.

Therefore, we are proceeding with the decision that we proposed in our minded-to position, to approve a LRSP claim of £51,956.44 for working capital. Our decision is, therefore, to consent to the recovery of these costs.

Cost category: “Other costs”

ScottishPower chose not to claim for costs associated with the migration of former customers of Entice and absorbed these amounts. Through their consultation response they noted that they consider that ScottishPower has absorbed greater levels of operational costs relating to its appointment than many other appointed SoLRs. ScottishPower maintain that they absorbed these operational costs as their response to the RFI in relation to appointment of a SoLR for Entice was based on them being able to claim wholesale costs for the full summer 2022 period. ScottishPower have set out that they may seek to recover additional costs if they consider they are under-compensated for wholesale costs.

ScottishPower submitted a claim for summer 2022 wholesale costs which, in our minded-to position, we considered provided insufficient evidence that the policy published in September should not be applied but that we were open to considering additional evidence to justify a claim as part of the True-up process.

While ScottishPower agreed as part of their SoLR RFI to absorb other costs associated with migrating customers of Entice, other suppliers have chosen to take different approaches to their SoLR RFIs as it is up to each supplier to decide on how they respond. ScottishPower, in their SoLR RFI response undertook to cover the costs of customer migration, which they have done. But they also noted that they would make an LRSP claim if there were unexpected costs associated with customer migration, which they have not subsequently claimed for.

As ScottishPower is aware, suppliers are obliged under Supplier SLC 8.3 to take all reasonable steps to honour any commitment made to Ofgem before their Last Resort Supply Direction was issued. Claims for LRSP for costs incurred carrying out the SoLR role must be decided by Ofgem in accordance with the statutory framework, taking into

consideration all the available evidence and the particular circumstances of the case. If ScottishPower do have unexpected costs associated with the migration of Entice customers then they can seek to make a claim for an additional LRSP with supporting evidence, as other suppliers have done.

Recovery of LRSP claim

ScottishPower will be paid the amounts specified in the Ofgem's consent documents, published alongside this letter, by the relevant licensed gas and electricity network operators. This will be recovered by the network operators in proportion to the total number of nationwide gas and electricity supply points.

Yours faithfully,

Neil Lawrence
Director of Retail