

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

Email: [solrlevyteam@ofgem.gov.uk](mailto:solrlevyteam@ofgem.gov.uk)

20 October 2023

Dear Colleague

### **Last Resort Supply Payment Claim from British Gas Trading Limited**

On 7 September 2023, British Gas Trading Limited ("British Gas") gave notice to Ofgem of its claim for a Last Resort Supply Payment (LRSP) in relation to acting as Supplier of Last Resort (SoLR) to customers of the former Neon Reef Limited ("Neon Reef") and Social Energy Supply Limited ("Social 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 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 **£143,886.39**.

We are minded-to consent to British Gas making a claim for costs incurred in complying with a Last Resort Supply Direction<sup>1</sup> 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 Neon Reef and Social Energy;

During winter 2021/22 we introduced a number of temporary changes to the LRSP claim process, which were designed to ensure that the SoLR process continues to protect consumers in volatile 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. Our policy on

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<sup>1</sup> [Direction to Appoint British Gas Trading Limited as Electricity Supplier of Last Resort to Neon Reef Limited | Ofgem](#)  
[Direction to Appoint British Gas Trading Limited as Gas Supplier of Last Resort to Social Energy Supply Ltd | Ofgem](#)  
[Decision to appoint British Gas Trading Limited as Electricity Supplier of Last Resort to Social Energy Supply Ltd | Ofgem](#)

assessing further claims under this temporary multiple-claim process was published on 21 September 2022<sup>2</sup>. On 25 May 2023 we published a further consultation on whether to end or continue the temporary multiple-claim process. In the consultation decision, published on 24 August 2023, we set out our decision to maintain the temporary process until at least after winter 2023/24, at which point we would again review market conditions and consult on whether the temporary process should be ended.<sup>3</sup>

As part of that faster multiple-claim levy process, each of the SoLRs entered into a True-up Agreement with Ofgem. Under the True-up Agreement between British Gas and Ofgem, Subsequent Levy Claims and a final True-up claim may be made following the Initial Levy Claim. Clause 5 of the True-up Agreements sets out what is required for a final True-up claim.

Clause 2.2 of the True-up Agreements sets out that the agreement will terminate on the earlier of the following:

- (a) Where any Valid True-up Amount is an Excess, the date upon which the SoLR has repaid in full the total of any Excess resulting from the True-ups of all Last Resort Supply Directions covered by this Deed;*
- (b) Where any Valid True-up Amount is a Deficit, the date of the last of the Valid Final Levy Claim(s) covered by this Deed; and*
- (c) The date of termination specified in any notice of termination of this Deed issued by the Authority.”*

Following our assessment of this current claim, we consider that it meets the requirements of a True-up claim under clause 5 of the True-up Agreement. However, in the claim submission, British Gas notified us that this may not be the final claim under this True-up Agreement. Therefore, we are minded-to to treat it as a Subsequent claim under the terms of the True-up Agreement. As a result of this, under the terms of the True-up Agreement, we will require a final True-up claim to be submitted in a future year. In the meantime, we note that obligations under the True-up Agreement continue to apply and will remain in place until a final True-up claim has been finalised.

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 2023.

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<sup>2</sup> [Decision \(ofgem.gov.uk\)](https://www.ofgem.gov.uk)

<sup>3</sup> [Decision on ending the temporary Last Resort Supply Payment claim process | 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.

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 notice<sup>4</sup>.

### Failed Supplier event

On 21<sup>st</sup> November 2021, we appointed British Gas as the SoLR<sup>5</sup> for Neon Reef and Social Energy gas<sup>6</sup> and electricity<sup>7</sup> customers, following their announcements that they 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 22<sup>nd</sup> November 2022<sup>8</sup>.

## 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 LRSP from each Relevant Gas Transporter and Electricity Distribution 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.

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

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<sup>4</sup> 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).

<sup>5</sup> [Ofgem appoints British Gas to take on customers of Neon Reef Limited and Social Energy Supply Ltd | Ofgem](#)

<sup>6</sup> [Direction to Appoint British Gas Trading Limited as Gas Supplier of Last Resort to Social Energy Supply Ltd | Ofgem](#)

<sup>7</sup> [Direction to Appoint British Gas Trading Limited as Electricity Supplier of Last Resort to Neon Reef Limited | Ofgem](#)

[Decision to appoint British Gas Trading Limited as Electricity Supplier of Last Resort to Social Energy Supply Ltd | Ofgem](#)

<sup>8</sup> [Ofgem appoints British Gas to take on customers of Neon Reef Limited and Social Energy Supply Ltd | Ofgem](#)

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 true-up decision process and methodology**

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. These initial claims were therefore limited to the recovery of costs for energy delivered within 6 months of their SoLR appointment or up to the end of March 2022, whichever was earlier. SoLRs may then follow this claim with an additional claim (or claims) in accordance with SLC 9. We refer to these additional claims as either a Subsequent claim or a final True-up claim. SoLRs entered into a 'True-up Agreement' with Ofgem to support the faster process. The Initial, Subsequent and True-up claim consents are conditional on SoLRs meeting the requirements of the True-up Agreement. The true-up process is intended to reconcile suppliers' initial and subsequent claims with actual costs incurred and determine any additional payments or repayments that should be made.

Following consultation, on 21 September 2022<sup>9</sup> we published our policy decisions on our approach to these true-up claims. These policies have been applied in order to reach our position on subsequent and true-up claims.

In December 2022, Ofgem consented to SoLRs making Subsequent levy claims totalling £405m on the condition that these claims be treated as Subsequent levy claims under the True-up Agreements, and that the Agreements remain in place until a valid final True-up claim is made. As a result, SoLRs that submitted claims in 2022 under their True-up Agreements were still required to submit to Ofgem a final True-up claim for each Last Resort Supply Direction in respect of which they have a True-up Agreement.

In May 2023, we set out in an open letter our expectations for SoLRs' final True-up claims following the LRSP claims that were approved in December 2022 under the temporary multiple claim process.<sup>10</sup>

Under Supplier 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 SLC 9.3.

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<sup>9</sup> [Decision \(ofgem.gov.uk\)](https://www.ofgem.gov.uk)

<sup>10</sup> [Update on the last resort claim process for 2023 | Ofgem](#)

Our process to reach our minded-to position included:

- a. A quantitative check of British Gas 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. A true-up and cross check of any evidence that may result in a change to the initial claim or subsequent claim made by the SoLR;
  - c. Undertaking validation of some assumptions with other data sources, where appropriate; and
  - d. A qualitative and quantitative assessment of the claim for costs related to credit balances and wholesale costs in accordance with the relevant licence conditions and/or 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 claim

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

The initial claim(s) were consented to in December 2021,<sup>11</sup> and a subsequent claim was consented to on 20 December 2022.<sup>12</sup> Consistent with the terms of that consent and the True-up Agreement between the SoLR and Ofgem, we have taken those claims into consideration in reaching our minded-to position on this claim.

### **Summary of our minded-to decision**

Based on the information available and consideration of the circumstances in which the claims for LSRPs by British Gas were consented to, and in accordance with the True-up Agreement in relation to customers of the former Neon Reef and Social Energy, Ofgem is minded-to consent to British Gas claiming a LRSP of up to £143,886.39.

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<sup>11</sup> Our Notice of Reasons for granting consent to the initial claim was published on 23 June 2022: [Faster SoLR levy process: Notice of Reasons for Last Resort Supply Payment \(LRSP\) claims | Ofgem](#)

<sup>12</sup> [Decision on last resort levy true-up claims | Ofgem](#)

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 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 initial claim, true-up and minded-to position on final claim amounts.

<b>Item</b>	<b>Cost</b>	<b>Initial Claim Approved</b>	<b>Subsequent Claim Approved</b>	<b>True-up Claim Submitted</b>	<b>Minded-to position on True-up Claim</b>
1	Wholesale	£7,963,351.81	£7,378,794.20	£130,259.21	£128,832.73
2	Credit Balances	£0	£4,561,369.68	£15,053.66	£15,053.66
	Total			£145,312.87	£143,886.39.

## **Reasons for our minded-to decision**

### **Cost category: Wholesale**

#### *Retrospective backwardation*

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 incurred in cap period seven, 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, applied via an increase to the additional wholesale risk allowance component of the cap. In August 2022 a further allowance of £6 per customer was introduced, to be recovered in the year from 1 October 2022.

These allowances would be recovered from all customers, SoLR and non-SoLR. Given this, we considered that the revenues collected by suppliers under this allowance should be deducted from claims made by SoLRs in relation to the costs of hedging SoLR customers' demand subsequent to it taking on the customers of the failed supplier. In other words, the costs of purchasing wholesale energy for these customers should be reduced because suppliers were allowed to recover approximately £14 per customer through higher bills in later periods.

We calculated the relevant deduction for each supplier in our decision in the subsequent claim (our December 2022 decision), 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.

Given that the retrospective backwardation deductions included in the decision on the subsequent claim were based on our best view of information submitted by the supplier at the time, we provided SoLRs an opportunity to submit evidence in September 2023 to substantiate actual allowances received.

### Retrospective shaping

As shaping costs were included in British Gas' subsequent claim for Neon Reef and Social the price cap shaping allowance was rightly accounted for and removed in calculations by British Gas. However, we also noted that in February 2022<sup>13</sup> Ofgem introduced a retrospective allowance into the default tariff cap to allow suppliers to recover additional revenue in relation to electricity shaping and imbalance costs incurred in cap period seven, which had been materially higher in winter 2021/22 than the price cap had accounted for. An amount of £12 per electricity customer (at typical consumption) was included within the cap for the year starting 1 April 2022, applied via an increase to the additional wholesale risk allowance component of the cap.

This allowance would be recovered from all customers, SoLR and non-SoLR. Given this, we considered that the revenues collected under this allowance should be offset against any claims made by SoLRs in relation to the costs of shaping and imbalance.

To calculate the appropriate amount to deduct, we had, as with the backwardation allowance (and for similar reasons), used our best estimate of the remaining SoLR customer accounts as of the end of winter 2021/22, combined with an estimate of annualised demand for these customers, whilst adjusting the price to account for line losses.

Given that the retrospective shaping deductions included in the decision on the subsequent claim were based on our best view of information submitted by the supplier at the time, we provided SoLRs an opportunity to submit evidence in September 2023 to substantiate actual allowances received.

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

- Assess the actual retrospective backwardation allowances received by SoLRs from April 2022 to September 2023 based on actual demand (MWh) and updated allowance numbers (£/MWh), adjusted for actual UIG and line losses.
- Assess the claim value for retrospective backwardation by calculating the difference between the deduction amount published in the decision on the subsequent claim and the actual retrospective backwardation allowances received by SoLRs.
- Assess the actual retrospective shaping allowances received by SoLRs from April 2022 to March 2023 based on actual demand (MWh) and updated allowance numbers (£/MWh), adjusted for actual UIG and line losses.
- Assess the claim value for retrospective shaping by calculating the difference between the deduction amount published in the decision on the subsequent claim (including the amount already included by SoLRs in their claims) and the actual retrospective shaping allowances received by SoLRs.

### Decision

This claim from British Gas included £63,330.30 for retrospective backwardation and £66,928.90 for retrospective shaping. Following the above assessment process, we identified an error in the claim and notified British Gas who acknowledged this error. We are minded to consent to the following claims:

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<sup>13</sup> Ofgem (2022), Price Cap - Decision on the potential impact of increased wholesale volatility on the default tariff cap, <https://www.ofgem.gov.uk/publications/price-cap-decision-potential-impact-increased-wholesale-volatility-default-tariff-cap>

- A claim of £62,752.58 for retrospective backwardation, calculated as the difference between the amount by which the subsequent claim (submitted in 2022) was reduced for retrospective backwardation allowances £495,453.47 and the actual allowances of £432,700.89 received by British Gas between April 2022 and September 2023. The actual allowances were calculated by multiplying Seasonal Normal Demand values on a quarterly basis from Q2 2022 to Q3 2023 with the relevant £/MWh retrospective backwardation allowances for each quarter, adjusted for UIG and line losses.
- A claim of £66,080.15 for retrospective shaping, calculated as the difference between the amount by which the subsequent claim (submitted in 2022) was adjusted for retrospective shaping allowances £714,180.43 and the actual allowances of £648,100.28 received by British Gas between April 2022 and March 2023. The actual allowances were calculated by multiplying Seasonal Normal Demand values on a quarterly basis from Q2 2022 to Q1 2023 with the relevant £/MWh retrospective shaping allowances for each quarter, adjusted for UIG and line losses.

British Gas provided demand values adjusted for seasonal normal weather and consumption, which we are minded to allow based on previous decisions allowing seasonal normal demand for British Gas. As we told SoLRs they could submit August and September 2023 numbers as forecasts, during the minded-to consultation period we expect British Gas to confirm if the figures it submitted in its claim are final.

The proposed total claim is £128,832.73. When taking into account the amount approved for the wholesale claim in the decision on the subsequent claim, the total wholesale costs approved to date would be £15,470,978.74.

Table 2: Summary of claims and minded-to position for wholesale costs

Item	Cost	Initial Claim Approved	Subsequent Claim Approved	True-up Claim Submitted	Minded-to position on True-up Claim
1	Wholesale	£7,963,351.81	£7,378,794.20		
	Retrospective backwardation			£63,330.30	£62,752.58
	Retrospective shaping			£66,928.90	£66,080.90

### 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:

British Gas' claim includes £15,053.66 for credit balances repaid to date to former customers of Neon Reef.

We consider that the claimed amount is consistent with the definition of Customer Credit Balances in SLC 9.4(b) and we minded-to consent to the claim. We have set out our rationale for this position below.

Table 3: Summary of claims and minded-to position for credit balances

Item	Cost	Initial Claim Approved	Subsequent Claim Approved	True-up Claim Submitted	Minded-to position on True-up Claim
2	Credit Balances	£0	£4,561,369.68	£15,053.66	£15,053.66

Rationale for decision:

As part of our assessment of the closed account credit balances, our position is that costs incurred by SoLRs as a result of credit balance refunds being made by cheque should only be recovered by the supplier through the levy once that cheque is cashed. This is to avoid consumers bearing the cost of compensation for credit balances that yet to be received by customers of the failed supplier and to ensure the SoLR does not benefit from a situation where some cheques are never cashed. British Gas has submitted evidence as part of its claim demonstrating instances where previously disallowed uncashed cheques have since been cashed by the former customers of Neon Reef.

We are minded to allow this part of 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 Neon Reef, to which British Gas has, in accordance with the requirements of the LRSP process, submitted a subrogated creditor claim for the 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.

**Requirements for final True-up claim**

The True-up Agreements set out the requirements for final True-up claims, which provide that True-up claims must at a minimum contain certain things, including:

- a calculation with supporting evidence showing the total actual or committed additional costs incurred by the SoLR in complying with that Last Resort Supply Direction, including those costs already claimed for under the Valid Initial Levy Claim(s) and any Valid Subsequent Levy Claim(s) and showing whether those costs exceed or are less than the LRSP claims already made; and
- evidence for additional LRSPs not already claimed; and
- indication of any changes to circumstances relevant to previously approved claims, including changes to assumptions about wholesale costs; and
- evidence that all costs have been audited with due rigour and signed off by the company secretary or a director of the SoLR; and

- a declaration from the SoLR's board of directors or the financial director, where authorised by the SoLR's board of directors, that the information provided in the True-up is true, accurate and not misleading in any material respect.

In compliance with our published policy<sup>14</sup> British Gas undertook an independent internal audit to assess the accuracy of the true-up claims.

We are content that the claim meets all the requirements under the True-up Agreement for a final True-up claim, and that the internal audit and declaration provides sufficient assurance of the accuracy of the information provided to us to support British Gas' claim.

However, in the claim submission, British Gas notified us that this may not be the final claim under this True-up Agreement. Therefore, we are minded-to to treat it as a Subsequent claim under the True-up Agreement. This would mean that the final True-up claim would happen in a future year.

### **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 17 November 2023. Responses should be emailed<sup>15</sup> to [solrlevyteam@ofgem.gov.uk](mailto:solrlevyteam@ofgem.gov.uk).

We normally publish all responses on our website. However, if you do not wish 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 be placed easily on our website.

We will take into account all relevant information, including any representations we receive, and the results of our internal assurance of our assessment process in reaching our final decision on British Gas' claim. We expect to make our final decision in mid-December 2023.

Yours faithfully,

**Rohan Churm**  
**Director, Financial Resilience and Controls**

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<sup>14</sup> [Decision \(ofgem.gov.uk\)](#)

<sup>15</sup> Although we prefer responses in electronic format, responses can be posted to the address below.