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14 December 2023

Dear Colleague

Last Resort Supply Payment Claim from Octopus Energy

On 7 September 2023, Octopus Energy Limited ("Octopus Energy") 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 UK Energy Incubator Hub Limited ("UKEIH").

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 Octopus Energy included its calculation of the claim amount and information to support the calculation (outlined in Table 1).

On 20 October 2023 Ofgem published a minded-to position in relation to that claim.¹ Summaries of the responses to the minded-to position consultation, including any relevant general representations made in response to the consultations on other SoLR claims, can be found within this document.

In addition, we undertook further 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 14 December 2023 Ofgem consented to Octopus Energy making a LRSP claim of up to £1,391,001.57.

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

- Additional wholesale costs incurred as a result of commitments to supply energy to customers of UKEIH;
- other costs reasonably incurred as a result of becoming a SOLR.

¹ [Last Resort Supply Payment claims minded-to positions 2023 | Ofgem](#)

We have assessed this LRSP claim in accordance with our policy published 21 September 2022,² and consistent with our published *Guidance on supplier of last resort and energy supply company administration orders*.³ In addition, in making this decision, we have had regard to Ofgem's principal objective of protecting the interests of current and future energy consumers⁴, the public sector equality duty⁵ relevant licence provisions, and the particular circumstances of the case.

As part of the temporary multiple-claim levy process introduced in December 2021, Octopus Energy entered into a True-up Agreement with Ofgem. Under the True-up Agreement between Octopus Energy and Ofgem, Subsequent Levy Claims may be made following the Initial Levy Claim and before a final True-up claim.

We set out in the consultation in relation to this claim that we were minded to consider this claim to be a Subsequent Levy Claim under the True-up Agreement. Following this consultation, we consider that this remains a reasonable approach. Accordingly, Ofgem has made its consent to this LRSP claim conditional on confirmation by Octopus Energy 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 will enable Octopus Energy to submit additional LRSP claims with supporting evidence for costs that have not yet been approved by Ofgem. As a result of this decision, the final True-up Claim required under the True-up Agreement will be made next year or later.

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 Octopus Energy'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.

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.⁶

² <https://www.ofgem.gov.uk/publications/decision-last-resort-levy-claims-true-process>

³ https://www.ofgem.gov.uk/system/files/docs/2016/10/solr_revised_guidance_final_21-10-2016.pdf

⁴ s4AA Gas Act 1986 and s3A Electricity Act 1989

⁵ *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)

⁶ 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).

Failed Supplier event

On 9 July 2022, we appointed Octopus Energy as the SoLR for UKEIH gas⁷ and electricity⁸ customers. This followed an appointment process aimed at getting the best deal for consumers. We outlined the material factors behind our decision to appoint Octopus Energy as the SoLR to those customers in our decision letter published on 1 December 2022⁹.

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 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 incurred in serving SoLR customers (typically wholesale commodity costs) in the period immediately after appointment. 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

⁷ <https://www.ofgem.gov.uk/publications/appointment-octopus-energy-limited-gas-supplier-last-resort-uk-energy-incubator-hub-ltd>

⁸ <https://www.ofgem.gov.uk/publications/appointment-octopus-energy-limited-electricity-supplier-last-resort-uk-energy-incubator-hub-ltd>

⁹ <https://www.ofgem.gov.uk/publications/appointment-octopus-energy-limited-supplier-last-resort-uk-energy-incubator-hub-limited>

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 2022¹⁰ we published our policy on our approach to these claims. In December 2022, Ofgem consented to SoLRs making LRSP 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.

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.¹¹

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 Octopus Energy, 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. Octopus Energy 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 Octopus Energy 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 Octopus Energy methodology for each cost item claimed. This included determining how each total cost item was calculated based on data sent to us by Octopus Energy and ensuring these costs were in line with commitments Octopus Energy 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;
- d. Review and audit 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 and other costs in accordance with our criteria and methodology, set out below.

¹⁰ <https://www.ofgem.gov.uk/sites/default/files/2022-09/Decision%20on%20the%20last%20resort%20levy%20claims%20true-up%20process.pdf>

¹¹ [Update on the last resort claim process for 2023 | Ofgem](#)

- **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.

Octopus Energy's claim

Octopus Energy indicated at the time of our SoLR appointment process that it would not waive its right to make a claim for a LRSP for additional costs incurred as a result of acting as the SoLR for customers of UKEIH.

The initial claim was consented to on 20 December 2022.¹² Consistent with the terms of the LRSP consents and the True-up Agreement between the SoLR and Ofgem, we have taken that claim into consideration in reaching our decision on this claim.

In our minded-to-position published on 20 October 2023, we stated that based on the information available and consideration of the circumstances in which the claims for a LRSP by Octopus Energy was consented to, and in accordance with the True-up Agreement in relation to customers of the former UKEIH, Ofgem was minded-to not grant consent to Octopus Energy claiming a LRSP for wholesale costs and other costs.

For wholesale costs, we were minded-not to allow any wholesale costs, as Octopus Energy had not submitted an audit for this claim, either by the submission deadline or during the assessment period, that would give us the assurance we required in relation to the evidence provided to support this claim. In our minded-to consultation we incorrectly stated that the required declaration also remaining outstanding. This had in fact been satisfactorily received.

For other costs, Octopus Energy had not provided any further evidence which indicated the costs have been incurred.

Following the end of our assessment of claims for the minded-to-positions, we did belatedly receive an audit, along with a revised data for their claim. Despite the compressed timescales, we have been able to progress the wholesale assessment.

¹² <https://www.ofgem.gov.uk/publications/decision-last-resort-levy-true-claims>

Summary of decision

Ofgem has consented to Octopus Energy claiming a LRSP of up to **£1,391,001.57**.

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 of initial claim, subsequent claim, true-up claim minded-to position and final decision on deductions and amounts.

Item	Cost	Initial Claim Approved	This claim	Minded-to position	Decision on this claim
1	Wholesale	£0	£4,009,171.09	£0	£1,391,001.57
2	Other costs - Administrator withheld funds	N/A	£350,000	£0	£0
Total:			£4,359,171.09	£0	£1,391,001.57

Responses to consultation

We received two responses to our minded-to consultation, one from a supplier and one confidential response that was not specifically related to our minded-to positions.

The supplier supported the minded-to positions on its claims and flagged that updated data had been submitted as requested in our minded-to positions. The supplier also queried how we will treat claims for customer credit balances refunded to customers by cheques that remain unpresented - for example, cheques that have not been cashed after five years from issue.

In response to this query, we note that further LRSP claims (subsequent claims and true-up claims) can continue to be made by a SoLR as long as the True-up Agreement remains open, which may be beyond the default five-year limitation period in SLC 9.3. Where customer credit balance cheques remain uncashed, we encourage SoLRs to be proactive in following up with customers where appropriate.

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. We recognise 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.

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. We consider it to

be in the interest of current and future consumers to allow this claim to ensure that the 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.

Cost category: Wholesale

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

- Assess whether costs being claimed are consistent with our criteria (set out earlier in this letter) and the policy we published in September 2022²;
- 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;
- 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

Octopus initially claimed £4,009,171.09 for wholesale costs in relation to UK Energy Innovation Hub (UKEIH). In the audited claim it subsequently provided (on 13 October 2023) it reduced this claim to £2,634,015.08. The subsequent deductions we have made and our final decision is based on the revised and audited claim.

Following the above assessments, we consider that the claimed amount is not fully consistent with our criteria and, as a result, have decided to consent to Octopus making a claim of up to £1,391,001.57¹³ for wholesale costs.

This reflects the following adjustments to the audited claim:

- A deduction of £840,513.08 to adjust for the time period claimed. Octopus' claim covered the period 9 July 2022 to 31 March 2023. This exceeds the 6-month SoLR direction period that we would usually allow costs to be recovered for, as set out in our September 2022 policy position.
- A deduction of £194,206.85 which reflects a change to the price comparator used in the claim.
- A deduction of £167,790.56 to adjust for the backwardation allowance introduced in the wholesale element of the price cap from cap period 9a onwards.
- A deduction of £40,503.03 for the retrospective backwardation allowances introduced during February 2022 and August 2022 to compensate suppliers for high costs incurred during cap period 7. These allowances were to be recovered

¹³ There is a small difference between the total amount consented to, and the total claimed minus adjustments made. This is due to rounding.

by suppliers between April 2022 and September 2023. We have calculated a deduction amount for Octopus only from July 2022 onwards.

Table 2: Summary of claims and decision on wholesale costs

Item	Cost	This Claim as Submitted	Deduction Category	Deduction amount (minded-to, subject to audit)	Deduction amount (final decision)	Minded-to position on This Claim	Decision on this claim
1	Wholesale	£4,009,171.09	Audited Claim Adjustment	N/A	£1,375,156.01		
			Claim Period Adjustment	£810,470.47	£840,513.08		
			Price Comparator Adjustment	£217,352.21	£194,206.85		
			Backwardation	£143,420.38	£167,790.56		
			Retrospective Backwardation	£50,979.02	£40,503.03		
	Total					£0 ¹⁴	£1,391,001.57

Summary of minded-to position

Octopus had not submitted an audit on this claim by the time we reached our minded-to position. As a result, we did not have the level of assurance required to consent to this claim. In the absence of a satisfactory audit of the claim we were minded-to not consent to Octopus claiming a LRSP. Despite the lack of audit, we carried out an assessment of Octopus' wholesale claim. Based on that assessment, we were minded-to allow Octopus to make a claim of up to £1,355,458.33 for wholesale costs if a satisfactory audit was provided (subject to consideration of other consultation responses).

On 13 October 2023, Octopus submitted a revised claim along with an audit. This audited claim had a number of changes from Octopus' initial submission on 8 September 2023, as well as their first resubmission on 18 September which are outlined in further detail below.

Our decision is based on an assessment of the audited claim submitted by Octopus on 13 October 2023.

Audited Claim Adjustment

Reasons for decision

Octopus first submitted its claim on 8 September 2023, without the required audit. On 18 September 2023, it re-submitted the claim, also without the required audit. Despite this, we carried out an assessment on the claim. The minded-to position on that claim was to award £0 for wholesale costs. However, we considered that if an audit was

¹⁴ Despite the lack of audit, we carried out an assessment of Octopus' wholesale claim. Based on that assessment, we were minded-to allow Octopus to make a claim of up to £1,355,458.33 for wholesale costs if a satisfactory audit was provided (subject to consideration of other consultation responses).

received, we would be minded to allow a claim of £1,355,458.33 for wholesale costs (subject to consideration of consultation responses).

On 13 October 2023, Octopus submitted a revised claim along with an audit. This claim includes several changes from the initial submissions in September:

- The volumes being claimed for wholesale electricity are higher in the audited claim than in the initial submission and the first resubmission. This results in an increase to the value of the claim.
- The volumes being claimed for wholesale gas are lower than in the initial submission and the first resubmission. This results in a decrease to the value of the claim.
- The price used in the trade data for electricity to be delivered in July 2022 has increased. This increases the value of the claim.
- Some of the price comparators used have changed. This has a mixed effect. The price comparator for wholesale electricity to be delivered in P9a increased, which results in a lower claim. For electricity to be delivered in P9b, the price comparator decreased, which results in a higher claim.

All of these changes resulted in a total wholesale claim of £2,634,015.08. This is £1,375,156.01 lower than the initial claim.

Gas Volume Adjustment

Summary of minded-to position

Through our analysis of Octopus' claim, we identified an inconsistency between the volume of gas that Octopus had claimed for, and the traded volumes and demand forecast it had provided for gas. The volume of gas that Octopus had claimed for was significantly higher than the traded gas volumes.

Following our findings, we engaged with Octopus and during this process Octopus were able to confirm that this inconsistency was an error in their submitted data. Octopus resubmitted their claim with corrected gas volumes. We used these corrected volumes in our analysis to reach our minded-to position. The resubmitted gas volumes would have resulted in a deduction of £1,431,490.68 to Octopus' original claim submission if a satisfactory audit had been provided. We were however minded to not award any wholesale claim to Octopus without the submission of an audit.

Summary of consultation responses

We did not receive any specific comments on our minded-to position on the gas volume adjustment, in relation to this wholesale claim.

Reasons for decision

As noted previously, Octopus submitted an audited claim part-way through the assessment process. The audited claim includes updated volumes of gas. We have taken the volumes of gas as they appear in the audited claim, hence making the gas volume adjustment of £1,431,490.68 irrelevant.

Electricity Volume Adjustment

Summary of minded-to position

During our assessment we identified that, in its first resubmission to correct the gas volumes, Octopus had adjusted its electricity volume claimed and electricity demand forecast upwards.

Octopus did not provide a supporting narrative to explain this change when it resubmitted its claim. Since Octopus did not provide a justification for this change, we decided to proceed with the electricity volume included in its original submission. This would make the claim £40,285.66 lower than if we used the electricity volumes in the first resubmission. Hence the remaining minded-to deductions were based on the resubmitted gas claim value but the original electricity claim value, amounting to a total of £2,577,680.41.

Summary of consultation responses

We did not receive any specific comments on our minded-to position on the electricity adjustment, in relation to this wholesale claim.

Reasons for decision

As noted previously, Octopus submitted an audited claim part-way through the assessment process. The audited claim includes updated volumes of electricity, and we have used those volumes to reach our final decision, hence making the electricity volume adjustment irrelevant.

Claim Period Adjustment

Summary of minded-to position

Our view is that Standard Licence Condition 9.4 requires SoLRs to show that a contractual liability for costs has arisen during the period of its SoLR Direction (six months) and that the energy (to which those costs relate) has been/will be delivered to SoLR customers' premises during the period of that Direction.

Octopus submitted a claim which covered wholesale energy costs for a nine-month period from 9 July 2022 to 31 March 2023.

Octopus provided a supporting narrative for its extended claim, which argued that it experienced unique and unavoidable costs due to when it was appointed SoLR. Octopus stated that when it was appointed SoLR the observation window for cap period 9b (which is January to March 2023) had already commenced. The price cap methodology assumes that suppliers can gradually hedge during this observation window. Octopus argued that as it was appointed after this window had already started, it was not able to match the price cap methodology for this cap period. Octopus' extended claim covers cap period 9b.

We considered that Octopus is not unique in being appointed as a SoLR part-way through an observation period. We envisaged such a scenario when we assessed the options for our policy on the time period of claims in developing our September 2022

policy³, and decided that on balance it would be in consumers' interest to limit the claim period to six months after appointment. We also considered that, more broadly, after the end of the six-month SoLR direction, it is reasonable for the customers that remain with the supplier to be treated as 'normal' customers.

We therefore did not consider that Octopus had submitted sufficient evidence to warrant an exception to the six-month time period for wholesale costs. Allowing Octopus to claim for an extended time period would increase the costs to be recovered from consumers and could therefore have an adverse impact on current and future consumers.

We therefore considered that limiting recovery to costs incurred for energy delivered until the end of the six-month direction period, to be the most appropriate approach, balancing the case for SoLRs to recover costs for an extended period against the needs of existing and future consumers.

This would result in a deduction of £810,470.47 to the claim.

We were however minded to not award any wholesale claim to Octopus without the submission of an audit.

Summary of consultation responses

We did not receive any specific comments on our minded-to position on the claim period adjustment, in relation to this wholesale claim.

Reasons for decision

On 13 October 2023 Octopus resubmitted their claim with an audit which is what we have taken into consideration when calculating the claim period deduction amount.

The position we have taken for the final decision remains the same as our minded-to position. During our further assurance of the claim, we noticed an error in the cut-off date we had used for the 6-month period. For the minded-to assessment, we used a cut-off date of 9 January 2023. For the final decision, we have changed this to 8 January 2023. This more accurately reflects a 6-month period, and is consistent with other SoLR claims we have assessed in the past. Calculating the deduction on the audited claim results in a deduction of £840,513.08. The final deduction differs from the number we calculated during the minded-to analysis because we have calculated it using the new audited claim, and additionally made an adjustment to the cut-off date used.

Price Comparator Adjustment

Summary of minded-to position

When assessing claims for wholesale costs, we use a price cap comparator to determine the amount of revenue that a supplier is expected to reclaim from customers through the wholesale portion of the price cap. The difference between the wholesale costs submitted by the supplier and the price cap comparator is the amount we consider is 'otherwise unrecoverable', which is one part of the test we apply to assess what costs are reasonable for suppliers to claim for under the SoLR Levy.

Octopus used its own methodology to calculate the price comparator in its claim. Octopus' methodology used a weighted average of wholesale prices through the

observation window period for price cap period 9a (P9a) and price cap period 9b (P9b) only up until the date it was appointed as SoLR for UKEIH (9 July 2022). For price cap period 8, it had taken the weighted average of wholesale prices across the entire observation window.

This methodology produced a price comparator that was significantly lower than the relevant wholesale portion of the price cap for price cap periods 9a and 9b. This inflated Octopus' claim substantially compared to the price cap comparator that we typically use based on the core direct fuel allowance.

We considered that since the price comparator is used to establish what a supplier has actually been able to recover through customer bills within a given period, the relevant allowance within the price cap should be used. We replaced the price comparator that Octopus used with the core direct fuel allowance amount for cap periods 8, 9a and 9b, as published in Annex 2⁴. This reduced its claim and resulted in a deduction of £217,352.21 to the claim.

We have taken a consistent approach in how we use price cap comparators in our assessments across SoLRs. We do not consider that Octopus justified its use of an alternative comparator.

We were however minded to not award any wholesale claim to Octopus without the submission of an audit.

Summary of consultation responses

We did not receive any specific comments on our minded-to position on the price comparator adjustment, in relation to this wholesale claim.

Reasons for decision

On 13 October 2023 Octopus resubmitted its claim with an audit which is what we have taken into consideration when calculating the price comparator deduction amount. Assessing this deduction against the audited claim results in a deduction amount of £194,206.85. The final deduction differs from the number we calculated during the minded-to analysis because we have calculated it using the new audited claim. This does not represent a difference in policy or methodology.

As part of our engagement with Octopus, it disagreed with our approach to this deduction. Octopus argued that the adjusted price comparator more accurately reflected the cost of wholesale energy that it would have incurred if it had been able to purchase gas and electricity throughout the observation windows for P9a and P9b. We have taken this argument into account and considered its theoretical basis, but have decided to proceed with our minded-to position to use the core direct fuel allowance as the price comparator. Using the core direct fuel allowance has been done to more accurately reflect what Octopus would receive from customers as revenue for the delivery of gas and electricity. This is consistent with our approach in other claims and is consistent with Ofgem's policy that costs should be 'otherwise unrecoverable'.

During our engagement, Octopus stated that if we proceed with our minded-to policy decision, it would revise its claim to include 100% of the volumes of wholesale gas and electricity hedged for P9a and P9b, rather than just the volumes hedged on the date of the SoLR appointment (Octopus' claim includes only volumes that it hedged on 9 July

2022, covering the volumes for P9a and P9b that it should have been hedged for up until that point in time).

Since this is not Octopus' final true-up claim in respect of UKEIH, the true-up process will remain open. Any future claims will be assessed on their individual merit.

Backwardation Adjustment

Summary of minded-to position

Backwardation costs are a result of the difference between the index used to set the cap level and the way suppliers are able to purchase energy for their cap customers. When the market is in backwardation, the forward prices in the later nine months are lower than in the first three (the actual cap period). It brings the cap level below the cost to suppliers of purchasing that energy for customers (for that cap period).

In our decision published on 4 August 2022⁴ on changes to the wholesale methodology in the price cap, we decided to update the wholesale methodology to include ex-ante modelled backwardation costs, which would be calculated quarterly at each cap update. This approach provides suppliers with certainty on the allowance compared to an ex-post approach.

These backwardation costs would be recovered over a six-month period with costs spread over six months relative to the gas and electricity demand in each quarter. We also decided to set a £9 deadband (£4 for electricity and £5 for gas £/customer/year) to ensure the wholesale methodology does not capture backwardation costs when the market is broadly stable.

As Octopus' claim covers cap periods 9a and 9b, we added a £/MWh backwardation allowance amount to the core direct fuel allowance price comparator value for the relevant quarters. This is because in addition to earning revenue from customers through the direct fuel cost component, Octopus would also recover backwardation allowances from their SoLR customers through the wholesale element of the price cap. The £/MWh backwardation allowance amount has been calculated post-deadband and post six-month recovery.

This would result in a deduction of £143,420.38 to the claim.

We were however minded to not award any wholesale claim to Octopus without the submission of an audit.

Summary of consultation responses

We did not receive any specific comments on our minded-to position on the backwardation deduction, in relation to this wholesale claim.

Reasons for decision

On 13 October 2023 Octopus resubmitted their claim with an audit which is what we have taken into consideration when calculating the backwardation deduction amount. Assessing this deduction against the audited claim results in a deduction amount of £167,790.56. The final deduction differs from the number we calculated during the

mind-to analysis because we have calculated it using the new audited claim. This does not represent a difference in policy or methodology.

Retrospective Backwardation Adjustment

Summary of mind-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 costs 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 have been 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 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 price cap periods.

Given the timing of Octopus' claim period, Octopus would have recovered a portion of these retrospective backwardation allowances from customers from July 2022 to September 2023. We calculated the deduction based on (a) the monthly demand forecasts provided by Octopus for July 2022 to September 2023 for gas and electricity and (b) the relevant £/MWh allowances, adjusted for UIG and line losses.

We calculated the relevant deduction based on our best view (given the information submitted by Octopus as part of its claim) of (a) the number of SoLR customers that remained with that supplier and (b) the annualised demand of those customers. We have used the same approach this year for our mind-to position.

This would result in a deduction of £50,979.02 to the claim.

Summary of consultation responses

We did not receive any specific comments on our mind-to position on retrospective backwardation, in relation to this wholesale claim.

Reasons for decision

During the mind-to consultation, we requested further updated data from Octopus to reflect the actual retrospective backwardation allowances received by Octopus from July 2022 to September 2023.

For the final decision, we revisited the calculations made for the mind-to position using the same methodology but with this updated data. For Octopus, this results in a deduction amount of £40,503.03. Our decision differs from our mind-to position as we have used the updated data. This does not represent a difference in policy or methodology.

Cost category: "Other costs"

We understand that other costs may have been incurred when undertaking activities as part of becoming a SOLR (for example, legal fees). We have used the criteria set out in our published decision on the last resort levy claims true-up process to assess whether it is appropriate for these costs to be recovered through a LRSP. The other costs that Octopus Energy has claimed are detailed below.

Decision

Octopus Energy's claim includes £350,000 for other costs when acting as SoLR for former customers of UKEIH. We consider that the claimed amount is not consistent with our assessment criteria and we do not consent to the claim. We have set out our rationale for this below.

Table 3: Summary of claim for other costs

Item	Cost	Initial Claim Approved	This Claim as Submitted	Minded-to position on claim	Decision on this claim
2	Administrator withheld funds	N/A	£350,000	£0	£0

Administrator withheld funds

Summary of minded-to position

Octopus Energy requested our permission to £350,000 for costs that are anticipated in relation to acting as SoLR for former customers of UKEIH but have yet to be incurred. We consider that since the claimed amount is for costs that have not been incurred, it cannot be included in a claim for LRSP under SLC 9.4(a). We were minded-to not grant consent to this part of the claim.

Summary of consultation responses

Octopus Energy have not provided a formal written consultation response to our minded-to position, however in bilateral meetings during the consultation period they responded to our minded-to position acknowledging that it was disallowed due the cost not being incurred.

Rationale for decision

Octopus Energy has not provided any further evidence which indicates the costs have been incurred. As stated above, this cost cannot be included in a LRSP claim under SLC 9.4(a). Therefore, based on the information submitted as part of the claim and within the particular circumstances of this case, we do not consider it reasonable to allow Octopus Energy to recover these costs and we have not approved the amount claimed.

Recovery of LRSP Claim

Octopus Energy 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,

Rohan Churm
Director, Financial Resilience and Controls