

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

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Dear colleague,

### **Decision on Last Resort Supply Payment claim from Ovo Energy Limited**

On 13 December 2019, we<sup>1</sup> published our minded-to decision on a claim by Ovo Energy Limited ("Ovo") for a Last Resort Supply Payment ("LRSP")<sup>2</sup>. Ovo is seeking to claim for costs incurred by Ovo Gas Ltd and Ovo Electricity Ltd in acting as a Supplier of Last Resort ("SoLR") to customers of the former Spark Energy Supply Limited ("Spark").

We received one non-confidential response and one confidential response to our consultation, which did not raise any issues that have given us reason to change our minded-to position in this case. This letter confirms our decision to consent to Ovo claiming a LRSP of up to £12.4m<sup>3</sup>, a reduction of £708k from our minded-to letter. This reflects the actual amount paid by Ovo in respect of credit balances to former customers of Spark. We also explain additional factors we have taken into consideration in making our decision, including representations made to us by interested parties in response to our consultation.

Our decision will allow Ovo to recover the costs of protecting the credit balances owed by Spark to the customers Ovo acquired in line with commitments given at the time of appointment. In taking this decision, we have had due regard to Ofgem's principal objective of protecting the interests of current and future energy consumers<sup>4</sup> the relevant provisions of Ovo's gas and electricity supply licences<sup>5</sup> Ofgem's "Guidance on supplier of last resort and energy supply company administration orders" (our "**Guidance**")<sup>6</sup>, the terms of the LRSD and the particular circumstances of compliance with the LRSD<sup>7</sup>.

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<sup>1</sup> References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work. This decision is made by or on behalf of GEMA.

<sup>2</sup> <https://www.ofgem.gov.uk/publications-and-updates/consultation-last-resort-supplier-payment-claim-ovo-energy>

<sup>3</sup> Precisely £12,372,332.

<sup>4</sup> See section 3A of the Electricity Act 1989 and section 4A of the Gas Act 1986.

<sup>5</sup> See standard licence conditions 8 and 9 of Ovo's gas and electricity licences.

<sup>6</sup> <https://www.ofgem.gov.uk/publications-and-updates/supplier-last-resort-revised-guidance-2016>

<sup>7</sup> <https://www.ofgem.gov.uk/publications-and-updates/direction-appoint-ovo-gas-ltd-gas-supplier-last-resort> and <https://www.ofgem.gov.uk/publications-and-updates/direction-appoint-ovo-electricity-ltd-electricity-supplier-last-resort>

## 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 in light of supplier failure. When a supplier fails, we take action to ensure continuity of supply for its customers and to minimise wider negative impacts on the market. These wider effects stem from the fact that if an energy supplier fails, its customers will continue to be physically supplied with gas and / or electricity, but the supplier will not be able to meet the costs of providing this energy. In these circumstances, the costs of procuring the necessary electricity will be smeared across all suppliers and the costs of procuring gas will be incurred by the relevant shipper. There is also a real risk that if a supplier fails without urgent intervention, consumer trust and confidence in the energy market could be materially damaged.

Ofgem can ensure continuity of supply to the failed supplier's customers and minimise these wider negative effects by appointing a SoLR to supply the failed supplier's customers at very short notice<sup>8</sup>.

### Claim for Last Resort Supply Payment

As set out in the gas and electricity supply standard licence conditions, a supplier may make a claim for any additional costs it incurs in complying with a Last Resort Supply Direction ("LRSD")<sup>9</sup>.

In our guidance, we explain that we will decide on a case-by-case basis whether it might be appropriate for a SoLR to make a claim under these arrangements. We also explain that we would consider whether the amount of any claim or the reasons for any claim were reasonable. In that guidance, we note that, in certain circumstances, we may consider it appropriate to approve a claim for reimbursing customers who had a credit account balance with the failed supplier. Ovo indicated at the time of the SoLR appointment process that it would not waive its right to make a claim and would claim for the recovery of a percentage of credit balances. In keeping with that commitment Ovo's claim is for a percentage of the cost of credit balances owed to customers of Spark when the company ceased trading.

Ovo has not submitted a claim to recover any additional costs it incurred as a result of being the SoLR for these customers.

### LRSP claim

Ovo is claiming of £12.4m<sup>10</sup> towards the cost of refunding credit balances owed to customers of Spark when the company ceased trading. The LRSP claim is net of a contribution by Ovo to credit balances.

Cost Category associated with SoLR	Cost claimed (£)
Recovery of 59% of net customer credit balances	£12,372,332

<sup>8</sup> The obligation for a supplier to comply with a LRSD derives from standard licence condition 9 of each suppliers' 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). The duties of a SoLR are further described in our Guidance and the LRSD contains specific details of Ovo's obligations to supply Spark Energy Supply Limited's former customers.

<sup>9</sup> Standard condition 9 of the electricity and gas supply licences

<sup>10</sup> Precisely £12,372,332.

Ovo Energy is self-funding a portion (41%) of the credit balance liability which it assumed in its role as a SoLR.

## **Stakeholder feedback**

We received one confidential and one non-confidential response to our consultation<sup>11</sup>.

One respondent noted that our minded-to letter provides a clear rationale for the proposed outcome and approval of the claim but objected to our minded-to position. The respondent cited a number of issues on the wider circumstances of the appointment of Ovo in addition to requesting greater transparency on the SoLR process.

We appreciate the desire for greater transparency and we aim to share as much information as we can with stakeholders on the SoLR process and on LRSP claims. However, the requirement to preserve commercial confidentiality limits the information we can disclose without breaching confidentiality, or disclosing suppliers bidding strategies which could undermine the effectiveness of the SoLR process. In our consultation we confirmed that Ovo's claim is in line with the commitments made at the time of the SoLR appointment.

Another respondent considered that our minded-to position is premature because Ovo, as a creditor, may receive monies from the liquidation of Spark. As we note below under the heading 'Our decision', while we are not required to make a decision in advance of the conclusion of the Spark liquidation process, we consider that to delay making a decision would increase uncertainty for SoLRs and ultimately increase the costs faced by consumers. Our decision is therefore to allow the recovery of the cost, minus any payment that Ovo receives from the Spark liquidation process.

Ovo has provided an updated (lower) figure of the cost incurred to repay credit balances and the amount we consent to has been reduced to reflect this lower figure.

## **Our decision**

On balance, taking into consideration all information available to us and the specific circumstances of this case, we have decided to consent Ovo to receive a Last Resort Supply Payment of up to £12.4m<sup>12</sup>. This sum reflects the actual amount paid by Ovo in respect of credit balances owned to former customers of Spark, which is less than the estimate OVO originally submitted. This figure will be reduced by any payment that Ovo receives from the Spark liquidation process.

We are minded to make this decision in light of the broader market considerations and our wider statutory duties to protect both existing and future consumers. Our position will enable Ovo to recover up to this amount from relevant distribution network licensees. This is subject to any costs recovered from the Spark Energy liquidation process.

For the avoidance of any doubt, we consider on a case-by-case basis whether it may be appropriate for any SoLR to make a claim for a LRSP. We have set out below our reasons for our decision in 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.

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<sup>11</sup> <https://www.ofgem.gov.uk/publications-and-updates/consultation-last-resort-supplier-payment-claim-ovo-energy>

<sup>12</sup> Precisely £12,372,332.

## Reasons for our decision

In our minded to letter, we noted that our published guidance<sup>13</sup> states that we may in certain circumstances approve a claim associated with costs incurred in repaying credit balances to customers who had a positive credit balance with a failed supplier. We also noted that the claim is consistent with the commitments made by Ovo at the time of its appointment.

We are satisfied in this case that Ovo's claim is consistent with:

1. The approach we set out in our guidance; and
2. The commitments made by Ovo to claim only for the cost of credit balances and to make a financial contribution to offset the cost of credit balances.

As part of our decision, we have considered whether the costs Ovo is seeking to claim are otherwise unrecoverable. We have concluded that the costs are unrecoverable, except to the extent that Ovo recovers any of the costs through the Spark administration process. As set out above, our decision is that if this situation occurs, the LRSP will be reduced accordingly.

## Recovery of LRSP

Ovo will be paid<sup>14</sup> the amount specified in our Direction by relevant gas and electricity distribution networks<sup>15</sup>. This will be recovered by the relevant gas and electricity distribution networks allocated in proportion to the total number of nationwide gas and electricity supply points. We consider this apportionment to best enable broad socialisation of the claim costs in line with the intent of the SoLR regime to protect all consumers in the market, for example, through limiting the extent of unpaid industry bills of a failing supplier.

As per the supply standard licence conditions regarding LRSP claims<sup>16</sup>, Ovo will be able to submit a claim to each relevant distribution network, based on the amounts we have consented to and each network's share of the total premises served by the relevant networks, in each fuel respectively. We expect Ovo to do this on the basis of the data on customer numbers contained within the network companies' regulatory reporting packs. This has the advantage of being a data source that is transparent and consistent between gas and electricity

**Yours faithfully,**

**Philippa Pickford**  
**Director, Future Retail Markets, Consumers and Markets**

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<sup>13</sup> <https://www.ofgem.gov.uk/publications-and-updates/supplier-last-resort-revised-guidance-2016>

<sup>14</sup> Our decision should enable relevant Gas Distribution Network (GDN) companies to make payment of the relevant share of the LRSP claim in charging year 2020/21, assuming a valid claim is made by the SoLR in time. Relevant Electricity Distribution Network Operators (DNOs) are required to begin payment no later than 3 months after being presented with a valid LRSP claim and to complete payment within a further period of 12 months.

<sup>15</sup> The relevant distributors according to standard licence condition 9 of the electricity and gas supply licences are distributors in whose distribution areas there were premises supplied under the Last Resort Supply Direction, excluding independent distribution network operators and independent gas transporters.

<sup>16</sup> Standard supply licence condition 9.