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

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Dear colleague,

Last Resort Supply Payment claim from SSE Energy Limited

On 29 August 2019, SSE Energy Limited ('SSE') gave notice to Ofgem of their intention to submit a claim for a Last Resort Supply Payment ('LRSP'). SSE is seeking to claim for costs incurred by Southern Electric Gas Limited and SSE Electricity Limited in acting as Supplier of Last Resort ('SoLR') to customers of the former Brilliant Energy Supply Limited ('Brilliant Energy')[1].

As per Supply Licence Condition 9, a Supplier of Last Resort (SoLR) may make a claim for a LRSP from relevant distribution networks where we have given our consent to the amount claimed[2]. This letter sets out that we are minded to consent to a claim from SSE for a LRSP of up to £711k[3].

The purpose of this consultation letter is to provide interested parties with an opportunity to make any representations to us, ahead of making our final decision. We currently expect to make our final decision in March 2020.

Background

The SoLR process

Electricity and gas supply is a competitive activity in Great Britain. Competition has the potential to bring many benefits to consumers but 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, our focus is to ensure continuity of supply for its customers and to minimise wider negative impacts on the market. These wider effects stem from the fact that if an energy supplier fails, its customers will continue to be physically supplied with gas and / or electricity, but the supplier will not be able to meet the costs of providing this energy. In these circumstances, the costs of procuring the necessary electricity will be smeared across all suppliers and the costs of procuring gas will fall to the relevant shipper. There is also a real risk that if a supplier fails without urgent intervention, consumer trust

[1] The claim is in respect of costs incurred by Southern Electric Gas Limited and SSE Electricity Limited in complying with the terms of the relevant Last Resort Supply Direction (see footnote 5).
[2] In accordance with Standard Condition 9 of the electricity and gas supply licences.
[3] Exactly £711,346.

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.[4]

Brilliant Energy SoLR event

In March 2019, Brilliant Energy confirmed to us that it was in severe financial difficulties, at which point we prepared to commence the SoLR process, to ensure consumers were protected. Following our standard process and published SoLR guidance on 14 March 2019, we announced our decision[5] to appoint SSE as the SoLR for Brilliant's gas and electricity customers. This followed a competitive process aimed at getting the best deal for consumers, in line with our principal objective to protect the interests of existing and future consumers and our published guidance.

At the time of Brilliant Energy's failure, we received a number of submissions from suppliers, setting out the terms they would offer to customers if they were to be appointed as the SoLR. We outlined the material factors behind our decision to appoint SSE as the SoLR in our decision letter published on 2 May 2019[6].

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)[7].

As part of their competitive bid to become a SoLR, a supplier will include whether they expect to make a claim for a LRSP, or whether it will waive this right, in whole or in part. As stated in our published guidance, our preference is for the SoLR not to make any claim, and we expect efficient SoLRs to be able to minimise their exposure to otherwise unrecoverable costs to reduce the costs smeared across the rest of the market through a LRSP.

In our guidance[8], 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 where it relates to costs associated with the protection of customers who held a credit balance with the failed supplier.

SSE indicated at the time of our SoLR appointment process that it would not waive its right to make a claim. It stated that it would make a claim for the cost of credit balances and other costs incurred in acting as a SoLR. SSE committed to make a per customer contribution towards the costs incurred, to offset a levy claim. The claim from SSE includes its calculation of the claim amount and information to support the claim as outlined in Table 1 below.

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[4] 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). The duties of a SoLR are further described in our Guidance and the LRSD contains specific details of SSE's obligations to supply Brilliant Energy's former customers.
[5] https://www.ofgem.gov.uk/publications-and-updates/southern-electric-gas-limited-gas-supplier-last-resort and https://www.ofgem.gov.uk/publications-and-updates/sse-electricity-limited-electricity-supplier-last-resort
[6] https://www.ofgem.gov.uk/system/files/docs/2019/05/decision_letter_sse_final.pdf
[7] Standard condition 9 of the electricity and gas supply licences.
[8] https://www.ofgem.gov.uk/publications-and-updates/supplier-last-resort-revised-guidance-2016

Table 1: SSE LRSP claim

Item	Cost Category associated with SoLR	Cost claimed by SSE (£)
1	Recovery of customer credit balances	755,790
2	IT and Operational costs	498,687
3	Blocked customers	113,983
4	Administrator costs	84,250
5	Communication costs	23,184
	Total costs	**1,475,894**
	SSE Contribution	-650,565
	LRSP Claim	**825,329**

Our decision process and methodology

Our process to reach our minded-to position consisted of:

- A quantitative check of the methodology for each cost item claimed. This includes determining how each total cost item was calculated based on data sent to us.
- Ensuring costs are in line with commitments made at the time of the SoLR appointment.
- Validation of assumptions with other data sources, where appropriate.
- A qualitative assessment of each claim item against our methodology criteria.

Our methodology criteria for SoLR levy claims are as follows:

- **Additional**: whether the costs claimed are additional to the costs to the SoLR of serving 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. Although the SoLR is generally expected to know or predict the costs they will incur in serving a new customer base and take these into account in their competitive bid, there may be cases where this is not possible.

- **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. It would not be appropriate for us to allow the SoLR to claim for costs they would have incurred through a normal acquisition route.

- **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 through the administration process or customer charges, for example.

- **Unavoidable**: whether the SoLR had made all reasonable efforts to avoid the cost in the first instance or absorb the cost.

- **Efficient**: whether the SoLR has taken all reasonable steps to reduce the magnitude of any unavoidable and unrecoverable costs incurred, and therefore the total amount claimed.

SSE's claim

SSE seeks consent to recover £825k[9] in additional costs incurred in its SoLR role. This letter sets out the reasons why we are minded to consent to SSE claiming a LRSP of up to £711k[10].

Supplier contribution

In keeping with the commitment made when appointed as the SoLR, SSE has contributed £651k to offsetting the claim for costs from the industry levy.

Our minded-to position

We are minded to allow SSE to claim for the costs of protecting credit balances owed to former customers of Brilliant and certain other costs incurred by SSE in carrying out the SoLR role. As explained below, SSE has made a claim for £114K for costs in relation to customers who switched to an alternative supplier before SSE could bill them. Our initial view is that the risk should have been priced into SSE's bid. We welcome views from stakeholders on our minded-to position as a whole and in particular on our view on this aspect of SSE's claim.

Table 2: Initial view of SSE LRSP claim

Item	Cost Category associated with SoLR	(£)
1	Recovery of customer credit balances	755,790
2	IT and Operational costs	498,687
3	Blocked customers	0
4	Administrator costs	84,250
5	Communication costs	23,184
	Total costs	**1,361,911**
	SSE Contribution	-650,565
	LRSP Claim	**711,346**

Our reasons for our minded to decision

On balance, taking into consideration all information available to us and the specific circumstances of this case, we are minded to consent to SSE claiming a Last Resort Supply Payment of up to £711k[11]. 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. This is subject to any costs recovered from the Brilliant Energy liquidation process.

[9] Exactly £825,329
[10] Exactly £711,346
[11] Exactly £711,346.

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 minded-to position for this case. This should not be taken as setting a precedent for any future claims, which would also be considered on their merits and on a case-by-case basis, taking into account all relevant circumstances of the particular case.

Cost item 1: Credit balances

SSE is claiming £756k for the cost of open and closed customer credit balances.

Our published guidance 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 are satisfied in this case (subject to the points discussed below) that the claimed amount is consistent with the relevant criteria and in particular, is consistent with SSE's commitment in its SoLR bid.

We have considered whether the costs SSE is seeking to claim for credit balances are otherwise unrecoverable; it may still be the case that SSE is able to recover some of this claimed amount through the ongoing administration process for Brilliant Energy. The current licence provisions related to LRSPs do not require us to make our decision on SSE's claim ahead of the conclusion of the liquidation process. However, in our view delaying a decision until the conclusion of the liquidation process would introduce a disproportionate degree of uncertainty around the timing of any approved LRSP claim, and ultimately increase the future costs liable to by paid by energy suppliers and consumers. Given this, we are minded to approve the claim, subject to the outcome of the Brilliant liquidation process. At that point, the final amount SSE can claim for credit balances would be adjusted to remove any sums recovered by SSE through the liquidation process.

Cost item 2: IT and Operational costs (£499k)

SSE's claim for IT and Operational costs is higher than the estimate given in its bid. These costs relate to the building of processes and IT solutions to automate the onboarding of ex-customers of Brilliant Energy. SSE explained that the bulk of the costs relate to the IT and manual work to receive the customer file, validate data and automatically load the information on to SSE's systems to trigger the industry change of supply process and initiate the initial and welcome communications to customers.

SSE stated that the costs of manipulating and verifying the data to ensure all impacted customer accounts were managed appropriately and loaded into its systems proved to be very challenging. SSE has explained that the increase in estimated IT costs was driven by the need to utilise more senior IT resources at short notice to deliver technical solutions to challenges which they had underestimated due to quality of the information available when they bid for the SoLR appointment. SSE consider that a number of these challenges could not have reasonably been anticipated when the bid was made based on the information available.

We are minded-to approve these costs on the basis that these costs were difficult to estimate at the time of bid and that the bid specified that the costs provided for this category were estimated. We consider that the evidence provided by SSE shows that they experienced particularly complex data issues which required investigation and at times manual intervention. For example, SSE has stated that the data quality issues during the onboarding process generated a level of exceptions being generated at a level that was three times higher than they had expected when compared to business as usual operations. We are further satisfied that the approach taken by SSE was proportionate, efficient and delivered benefit to the customers they were onboarding.

We are therefore minded to accept this element of the claim.

Cost item 3: Blocked customers (£114k)

When SSE tried to onboard Brilliant Energy's ex-customers using the Change of Supplier (CoS) process they identified that approximately 2,800 customers had already chosen an alternative supplier. Until the switching process was completed, SSE remained the registered supplier. However, due to these customers having elected to switch, SSE was unable to source information through the CoS process to set up accounts and bill these customers for the period that SSE was the registered supplier. SSE undertook significant effort to try to obtain the necessary customer date from alternative sources. SSE explained that, over approximately 2 months, it collected information from various sources and ad-hoc data requests including to Brilliant Energy's Data Collector/Data Aggregator and Xoserve. However, due to the time taken to do this and the fact that customers were unlikely to recognise SSE as their supplier, SSE were concerned about the collectability of these accounts.

A group of 500 customers for whom SSE had the most complete set of customer data were billed. SSE managed to collect just under half of the amount billed to these customers but do not believe they can collect further debt from this group – or from the wider group - due to the lapsed time and poor quality of these accounts. SSE's levy claim for these customers therefore equates to the uncollected billed debt from the sample group plus the estimated unbilled revenue for the remaining customers - in total, £114k.

We advise customers of a failed supplier not to switch to another energy supplier until a new one has been appointed and that the new supplier will contact them in the following weeks. However, customers are free to switch supplier if they choose to and so there is a risk that some customers will switch supplier during this period. We consider that the loss of customers who switch is a risk that a supplier should be aware of and take into account when bidding for a SoLR appointment.

Our initial view is that this risk should have been priced into SSE's bid. We welcome views from stakeholders on this item.

Cost item 4: Administrator costs (£85k)

SSE has submitted a claim for £85k for costs relating to charges levied by Brilliant Energy's administrator. This item of the claim is made up of two elements: (i) the cost of access to the Gentrak billing and CRM system used by Brilliant Energy and specific data requests made by SSE to the administrator, and (ii) the cost to develop and use a cloud based 'bill finder' app to assist with the prompt and effective management of customer queries.

The cost of the development of the cloud based "Bill Finder App" tool to assist with customer query management was split equally with the administrator. The administrator's collections agent has stated that they expect to continue to follow-up unpaid final balances for a period of 9-12 months after the SoLR date[12]. This means that SSE will continue to receive bill disputes and potential credit balance adjustments beyond the date of the claim being submitted, until January 2020. SSE has stated that it will absorb these costs.

We are minded to approve the recovery of this cost.

Cost item 5: Customer communication costs (£23k)

These costs relate to the communications with Brilliant Energy's customers about the SoLR process to validate their account information, and include online enhancements made to help these customers to understand the SoLR process. This includes all digital changes, specifically Brilliant Energy and Northumbria Energy web landing pages and FAQ information to support customers through the transition. To minimise costs, SSE explained

[12] 14 March 2019

that messaging was adapted from existing customer communications specifically for the SoLR event.

It is vital that customers of a failed supplier are able to understand what the SoLR process means for them and are reassured that arrangements have been made to protect the continuity of their supply and that they can, if they need to, contact the SoLR supplier for more information.

We are therefore minded to approve the recovery of this cost.

Next steps

The purpose of this letter is to provide interested parties with an opportunity to make any representations to us, ahead of us making our final decision. We invite any representations by **5 March 2020**.

Responses should be emailed to supplier@ofgem.gov.uk.[13] 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, in reaching our final decisions.

Yours faithfully,

Philippa Pickford
Director, Future Retail Markets, Consumers and Markets

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