

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 Ovo Energy Ltd**

On 6 February 2020, we<sup>1</sup> published our consultation setting out our minded-to position on SSE's claim for a Last Resort Supply Payment (LRSP) for additional costs incurred by Southern Electric Gas Limited<sup>2</sup> and SSE Electricity Limited<sup>3</sup> in acting as a Supplier of Last Resort (SoLR)<sup>4</sup> to customers of the former Brilliant Energy Supply Limited ('Brilliant Energy').<sup>5</sup>

SSE's licenced gas and electricity domestic supply businesses have been bought by Ovo Energy Ltd and the claim for the LRSP is now in respect of Ovo (S) Gas Limited and Ovo (S) Electricity Limited.

We received two non-confidential responses to our consultation both of which are published on our website.<sup>6</sup> This letter confirms our decision to consent to Ovo claiming for a LRSP of up to £711k.<sup>7</sup> We also explain the reasons for our decision.

Our decision will allow Ovo to recover the costs of protecting the credit balances owed by Brilliant Energy to the customers acquired by Ovo at the time of the appointment, and certain other costs incurred by Ovo in complying with Ofgem's Last Resort Supply Direction ('LRSD').<sup>8</sup>

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>9</sup>, the relevant provisions of Ovo's gas

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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> The company name of Southern Electric Gas Limited changed to Ovo (S) Gas Limited on 16 January 2020.

<sup>3</sup> The company name of SSE Electricity Limited changed to Ovo (S) Electricity Limited on 16 January 2020.

<sup>4</sup> <https://www.ofgem.gov.uk/publications-and-updates/consultation-last-resort-supplier-payment-claim-sse>

<sup>5</sup> The claim is in respect of costs incurred in complying with the terms of the relevant Last Resort Supply Direction.

<sup>6</sup> <https://www.ofgem.gov.uk/publications-and-updates/consultation-last-resort-supplier-payment-claim-sse>

<sup>7</sup> Exactly £711,346.

<sup>8</sup> <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>

<sup>9</sup> See section 3A of the Electricity Act 1989 and section 4A of the Gas Act 1986.

and electricity licenses<sup>10</sup>, Ofgem’s “Guidance on supplier of last resort and energy company administration orders” (our “Guidance”)<sup>11</sup>, the terms of the LRSD and the particular circumstances of compliance with the LRSD.

## 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 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>12</sup>

### The LRSP process

Once appointed a SoLR may make a claim for a LRSP for relevant licensed distribution networks where we have given our consent to the amount claimed. On 29 August 2019, Ovo notified us of its intention to claim for a LRSP of £825k<sup>13</sup> consisting of the following elements.

**Table 1: Ovo Energy LRSP claim**

Item	Cost Category associated with SoLR	Cost claimed by Ovo (£)
1	Recovery of customer credit balances	755,790
2	IT and Operational costs	498,687

<sup>10</sup> Standard condition 9 of the gas and electricity supply licences.

<sup>11</sup> <https://www.ofgem.gov.uk/publications-and-updates/supplier-last-resort-revised-guidance-2016>

<sup>12</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). The duties of a SoLR are further described in our Guidance and the LRSD contains specific details of Ovo’s obligations to supply Brilliant Energy’s former customers.

<sup>13</sup> £825,329

3	Blocked customers	113,983
4	Administrator costs	84,250
5	Communication costs	23,184
	<b>Total costs</b>	<b>1,475,894</b>
	<b>Supplier Contribution</b>	<b>-650,565</b>
	<b>LRSP Claim</b>	<b>825,329</b>

In our consultation we said that we are minded-to consent to Ovo claiming an LRSP of up to £711k, that is the total claim as set out above less the element claimed for “blocked customers”.

**Table 2: Initial minded to position on Ovo’s LRSP claim**

<b>Item</b>	<b>Cost Category associated with SoLR</b>	<b>(£)</b>
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
	<b>Total costs</b>	<b>1,361,911</b>
	<b>Supplier Contribution</b>	<b>-650,565</b>
	<b>LRSP Claim</b>	<b>711,346</b>

### **Our decision**

We received no representations from stakeholders that have led us to revise our approach to assessing the LRSP claim submitted by Ovo. We are satisfied that the claim represents no more than the total costs incurred by Ovo in complying with the LRSD, minus the total amounts recovered by Ovo from Brilliant’s former customers.<sup>14</sup>

On balance, taking into consideration all information available to us and the specific circumstances of this case, we consent to Ovo claiming a LRSP of up to £711k.<sup>15</sup> We 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.

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 and whether the costs it has incurred in discharging the duties under an LRSP are efficient. 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

<sup>14</sup> This is the test set out in Ovo’s gas and electricity supply licences.

<sup>15</sup> £711,346.

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.

## **Stakeholder responses**

We received two responses to our consultation. Both were broadly supportive of our minded-to position in relation to the claim for costs incurred by Ovo in refunding credit balances to former customers of Brilliant Energy. One respondent welcomed the detail included on the costs claimed, while another respondent emphasised the need for greater transparency on the SoLR process as a whole (including the information provided to the supplier before bidding), so as to allow a meaningful assessment of the costs claimed by SoLRs.

We understand the desire for greater transparency in the SoLR process. In explaining the reasons for our decision on LRSP claims we aim to provide stakeholders with as much information as we can. However, the obligation on us not to breach commercial confidentiality limits the extent to which we can share information. The disclosure of information on commercial arrangements and bidding strategies could also undermine suppliers' interest in bidding for future SoLR appointments. This would not be in consumers' interests.

## **Reasons for our decision**

### Cost item 1: Credit balances

Ovo's claim of £756k for this item is 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 that the claimed amount is consistent with the relevant criteria and, in particular, with Ovo's commitment in its SoLR bid.

Our decision is subject to the outcome of the Brilliant Energy liquidation process. At that point, the final amount Ovo can claim for credit balances will be adjusted to remove any sums recovered by Ovo through the liquidation process.

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

In our consultation we noted that Ovo's claim for IT and Operational costs is higher than the estimate given in its bid and set out Ovo's explanation for the higher than estimated costs.

Our decision to consent to the recovery of this item reflects the reasoning set out in our consultation letter: we accept that these costs were difficult to estimate at the time of bid and note that Ovo specified in its bid that these costs were an estimate. We consider that the evidence provided by Ovo shows that they experienced particularly complex data issues which required investigation and at times manual intervention. We are further satisfied that the approach taken by Ovo was proportionate and delivered benefit to the customers they were onboarding.

### Cost item 3: Blocked customers (£0k)

When Ovo tried to onboard Brilliant Energy's ex-customers into their internal systems 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, Ovo remained the registered supplier. However, due to these customers having elected to switch, Ovo was unable to source information through the CoS process to set up accounts and bill these customers for the period that Ovo was the registered supplier. Ovo informed us that they undertook significant effort to try to obtain the necessary customer data from alternative sources. Ovo 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 Ovo as their supplier, Ovo were concerned about the collectability of these accounts.

A group of 500 customers for whom Ovo had the most complete set of customer data were billed. Ovo 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. Ovo'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.

In our consultation we explained our view that this risk should be priced into a supplier's bid for a SoLR appointment. One respondent supported this position. We advise customers of a failed supplier not to switch until their transfer to the SoLR is complete. However, customers are free to switch and we consider that a supplier should take into account the risk that some customer will switch when bidding for a SoLR appointment.

### Cost item 4: Administrator costs (£84k)

This item of the claim is made up of two elements: (i) the cost of access to the billing and CRM system used by Brilliant Energy and specific data requests made by Ovo to the administrator, and (ii) the cost to develop and use a cloud based 'bill finder' app. In consenting to the recovery of this item we accept that this work was a reasonable approach to assist in the prompt and effective management of queries from the former customers of Brilliant Energy.

### 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 related web landing pages and FAQ information to support customers through the transition.

Our decision to consent to the recovery of this item reflects the importance of effective communications to customers of a failed supplier, so that they understand clearly what the SoLR process means for them and are confident that arrangements have been made to protect the continuity of their supply.

## **Recovery of claim**

Ovo will be paid the amounts specified in the gas and electricity consents published alongside this decision, by the relevant licenced gas and electricity network companies. 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 standard conditions of the gas and electricity supply licence regarding LRSP claims, Ovo will be able to submit a claim to each relevant distribution network operator, based on the amount 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 customer numbers contained within the network companies' regulatory reporting packs. This has the advantage of being a data source that is transparent and consistent as between gas and electricity.

The LRSP claim we have consented to will be recovered from relevant licenced gas and electricity distribution network operators. Electricity distribution network companies have three months from receipt of a valid LRSP claim to begin to make payments to Ovo and a further period of 12 months to complete making payment. Gas distribution network operators will make payments to Ovo in the charging year 2021/2022.

Yours faithfully,

**Lesley Nugent**

**Deputy Director, Licensing Frameworks**