CORNWALL INSIGHT

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Ofgem seeks views on Debt Relief Scheme Framework

Headline assessment	
Document:	Debt Strategy: Next steps
Consultation dates:	04/08/2025 – 29/08/2025
Impact classification:	High: Domestic Suppliers, Consumers
Action if desired:	Respond to the call for input

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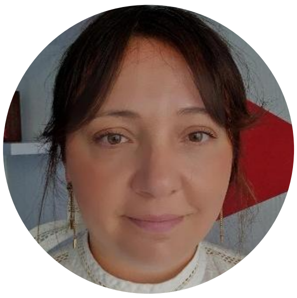

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1 Assessment and recommendation

On 4 August, Ofgem published a working paper setting out potential next steps in its debt strategy review, seeking stakeholders' views on reforms to debt-related cost recovery in the retail energy market. In this paper, Ofgem outlines the proposed structure for a two-phase Debt Relief Scheme (DRS) to tackle unsustainable debt accumulated during the energy crisis by offering targeted write-offs to financially vulnerable customers, especially those receiving means-tested benefits (MTB).

The working paper focuses on the longer-term framework for Phase One of the DRS, covering eligible debt types, supplier recovery processes, governance, and the method of cost recovery via network charges.

A statutory consultation on the DRS implementation is expected in September 2025, with Phase One delivery targeted for Q126, subject to legislation. Ofgem is now seeking stakeholder feedback on proposed eligibility criteria, engagement requirements, supplier reimbursement methodology, and funding approaches, with responses requested by 29 August 2025.

Phase Two, which encompasses broader reforms and an enduring affordability measure, will be implemented later in 2026.

Cornwall Insight comment: While the proposed DRS scheme is a positive step toward easing the burden on financially vulnerable households, it will be important for Ofgem to ensure that the cost recovery framework is robust and delivers timely reimbursement to suppliers. With implementation targeted for early 2026, the operational and administrative burden, particularly around customer identification, engagement, and systems readiness, could be significant. Careful attention will also be needed to ensure that suppliers are not left exposed to shortfalls between the value of written-off debt and the recovery received. Finally, while the scheme targets those most in need, consideration may be warranted for customers who fall just outside of the eligibility criteria but are still struggling with energy debt.

2 Background and strategic aims

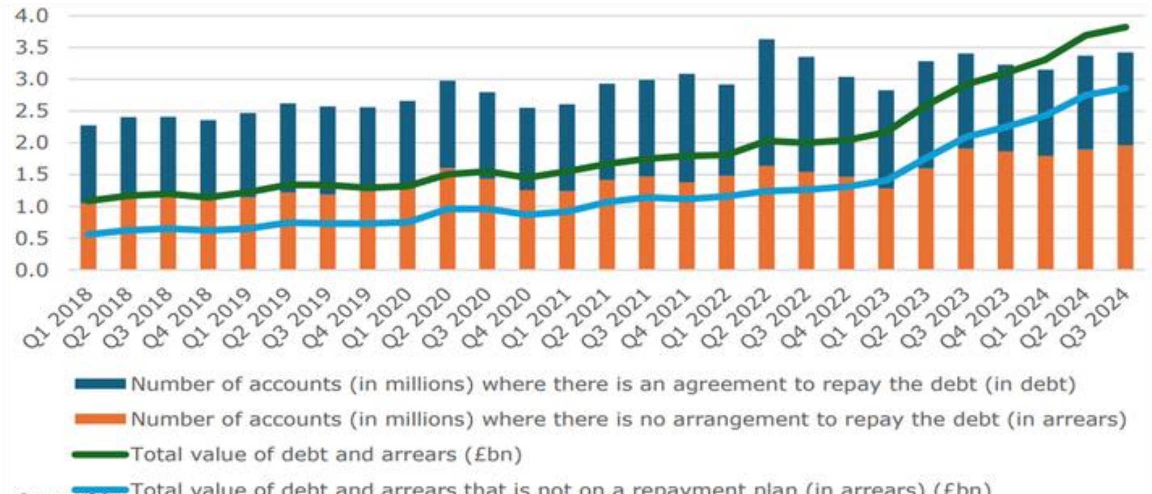
Ofgem's publication follows a December 2024 policy consultation, which outlined a commitment to deliver a debt write-off scheme targeting consumers most affected by debt build up during the energy crisis in 2021-2022. The regulator highlighted that energy debt reached concerning levels following the pandemic and the price cap shocks, as demonstrated in Figure 1.

Building on that, Ofgem confirmed the DRS will proceed in a two-phase implementation, with Phase One targeting customers most in need and aiming to establish fairer debt management practices in the long term.

The DRS forms part of Ofgem's broader strategic priorities to:

- Reduce unaffordable consumer debt in the energy sector
- Address structural barriers to debt management
- Incentivise earlier supplier-consumer engagement
- Establish fairer and more consistent provisioning approaches across suppliers

Figure 1: Total of domestic accounts in arrears/debt, total value of arrears and total value of debt between Q118 and Q324



Source: Ofgem

3 Phase One design

3.1 Customer eligibility

Ofgem proposes that to qualify for Phase One support, customers must:

- Be domestic account holders;
- Have accrued over £100 in debt between 1 April 2022 and 31 March 2024;
- Be receiving MTBs;
- Demonstrated engagement via repayment or other channels.

Eligibility will be determined using existing datasets such as Warm Home Discount and Department of Work and Pension (DWP) data. MTB status will serve as an income proxy for Phase One. Support will be capped at the level of eligible debt "accrued between 1 April 2022 and 31 March 2024", as assessed at the point of the statutory consultation, expected in Autumn 2025.

Question for Stakeholders:

1. **Whether Ofgem should cap available DRS support as at statutory consultation date?**

3.2 Engagement expectations

- **Engaged customers:** Customers who meet eligibility criteria and have demonstrated sustained engagement with their supplier, such as making repayment contributions, accepting a smart meter installation, participating in the Fuel Direct Scheme, or engaging via a third-party (e.g.) charities or consumer groups), will automatically qualify for DRS support if they meet eligibility criteria.
- **Disengaged customers**: Must re-engage through supplier contact, repayment discussion smart meter acceptance, Fuel Direct Scheme, or charity referrals.
- **Closed accounts**: Must show ongoing effort to repay for eligibility.

Suppliers are required to inform eligible customers of the scheme, provide accessible engagement options, and track and report re-engagement outcomes.

Questions for Stakeholders:

1. **Are there any alternative engagement pathways that customers could choose to demonstrate a commitment to resolving debt sustainably?**
2. **Do stakeholders agree with the conditions proposed for both engaged and currently disengaged customers, or do stakeholders believe that the threshold for accessing DRS should be lower or higher (and if so, please clarify how)?**
3. **Are there any improvements that could be made to existing processes or rules to make the scheme more effective – e.g. to the Fuel Direct Scheme**

4 Supplier readiness and operational expectations

Suppliers will be expected to demonstrate operational readiness before participating. This includes:

- Being ready by Q126 to identify eligible customers using current systems;
- Undergo a readiness assessment by Ofgem prior to accessing reimbursement (late 2025);
- Maintain consistent provisioning methodology;
- Submit regular reports and assurance documents;
- Develop and implement a customer communication strategy;
- Only suppliers who pass the readiness assessment, expected to be completed ahead of Phase One go-live in Q1 2026, will be able to claim reimbursement. Ofgem estimates that "approximately 195,000 MTB customers will be targeted in Phase 1, of whom 175,000 are already engaged and 50,000 customers who will need to receive further support". This highlights the necessity for suppliers to implement systems that can effectively identify and engage potentially eligibles customers on a large scale.

5 Reimbursement design and options

Ofgem proposes a reimbursement framework that accurately reflects the real value of written-off debt. According to Ofgem, this approach acknowledges that the face value often overstates the amounts that can actually be recovered.

5.1 Customer contributions

Ofgem has previously highlighted that customer repayments under debt relief schemes reduce overall scheme costs through two primary mechanisms: debt payment displacement and engagement benefit. The former happens when customers shift their repayments to non-eligible debts after some of their eligible debts have been forgiven, allowing suppliers to keep receiving payments for those debts. The latter highlights that customers who pay towards their eligible debts are more likely to develop positive repayment habits. Ofgem believes that this behaviour can reduce the risk of bad debt in the future and may also decrease the overall size of the debt relief scheme.

The modelling for the scheme assumes a 5% value for customer contributions and debt repayment displacement. To account for these contributions in supplier reimbursements, three options have been proposed as demonstrated in Table 1.

The outcomes of customer contributions on net supplier reimbursements vary across the different option models, highlighting how contributions can influence the financial aspects of the DRS.

Table 1 – Summary of customer contributions models proposed by Ofgem

Options	Summary
Option 1	• Suggests that a 5% contribution applies to all eligible customer accounts, thereby reducing the net supplier reimbursement based on the total eligible debt.
Option 2	• Restricts the 5% contributions to non-automatic route customers, recognising their engagement in contributions towards the debt.
Option 3	• States that no contributions are considered, which would lead to higher direct scheme costs.

Questions for Stakeholders:

1. **Which of the three options is preferred?**
2. **Whether 5% is a reasonable value for Customer Contributions (including debt displacement) or do stakeholders have an alternative methodology for assessing this value?**
3. **What data does Ofgem need to help inform this decision?**

5.2 Reimbursement models

The reimbursement strategy Ofgem proposed focuses specifically on Phase One of the DRS, with plans to explore alternatives in Phase Two. In the proposed framework, customer debt is recognised as an asset on supplier balance sheets, providing a means for suppliers to be reimbursed rather than collecting it directly.

While stakeholders have noted that some funding has already been secured, the task of establishing a fair and effective reimbursement method is anything but straightforward. To navigate this complexity, Ofgem presented three key options for calculating the realised value of historic debt: The Notional Supplier Model, the Supplier-by-Supplier Model and the Hybrid Model.

The Notional Supplier Model takes a broad view, offering reimbursement based on an average provisioning rate across the industry, which accounts for the diverse customer base and the various payment types involved. On the other hand, the Supplier-by-Supplier Model delves deeper, providing reimbursement that reflects the audited provisioning rates of each individual supplier. Meanwhile, the Hybrid Model combines elements from both approaches, implementing a minimum provisioning of debt at 56.7% to help adjust the values as needed.

For example, the Notional Supplier Model calculates average provisioning rates based on customer number and payment types, leading to approximately 20% reimbursement of eligible debt. While it acknowledges the complexity of supplier provisioning methodologies, it risks disadvantaging suppliers expecting higher future recoveries. In contrast, the Supplier-by-Supplier Model offers reimbursement aligned with individual supplier provision rates from audited accounts.

As part of Phase One, Ofgem recommends a hybrid model based on the provisioning data suppliers provide. It considers this is consistent with what suppliers have already written off and reflects and accommodates the fact different suppliers have different abilities to recover debt.

Questions for Stakeholders:

1. **Preferred methodology for calculating reimbursement rate?**
2. **Whether under a hybrid or supplier by supplier model Ofgem should set a single rate for each supplier, or a rate for each supplier by payment type.**

6 Funding and recovery mechanism

Ofgem proposes that funding for the DRS should be collected through network distribution charges, as this offers a cost-effective and administratively efficient solution. According to the regulator, this approach allows for differential payments to suppliers while simultaneously reducing administrative costs. A key feature of the scheme is the proposed "Pay When Paid" model for supplier claims. Under this mode:

- Suppliers will be paid only after networks have collected funds from customers.
- Payments are proposed to begin in May 2027, upon Ofgem claims approval.
- DNOs will set 2027-28 tariffs, including DRS costs, in December 2025.

The cost recovery mechanism will mirror aspects of the Supplier of Last Resort (SoLR) process:

- Electricity customers: via standing charges.
- Gas customers: via volume-based charges.
- Independent networks will incur higher "All The Way" charges from DNOs.
- IGT shipped customers will also be subject to a DRS-related network charge.

Ofgem noted that it will retain responsibility for ensuring networks can finance their operations under this model, and draft licence condition changes are proposed to support implementation.

While Ofgem considered a two-to-three-year recovery period, it prefers a one-year window due to the expected scale of the scheme and the additional financing costs associated with delaying supplier payments. The rationale is that the financial relief provided to customers and the potential improvement in supplier debt positions will have a lasting effect beyond the immediate payment year, helping to offset short-term recovery impacts.

Suppliers will assess the value of their eligible claims and submit them to Ofgem for review, supported by relevant evidence. Once approved, claims will be passed to the relevant network operators for reimbursement. The process will draw on lessons from SoLR cost recovery, though Ofgem expects a faster timeline for DRS payments given the narrower range of allowable expenses. Suppliers may submit multiple claims throughout the life of the scheme, with recovery potentially extending beyond 2027.

Ofgem is also exploring whether to enable Third Party Assignment rights within the DRS framework. This could allow suppliers to access approved payments before network funds are collected, providing earlier cash flow. Eligibility to submit claims will be limited to suppliers formally obligated under the DRS and who have passed the required readiness assessment. The same payment process is expected to apply across both Phase One and Phase Two of the scheme, although eligible cost categories may vary.

Finally, successful implementation will require code modifications in both the gas and electricity sectors. Ofgem encourages stakeholders to begin working on these changes and invites feedback on the suitability of the “Pay When Paid” model and the proposed reimbursement approach.

7 Next steps

Stakeholders are encouraged to engage with the ongoing development of the DRS and prepare for the upcoming implementation milestones, with responses to this call for input requested by 29 August 2025.

Ofgem is expected to publish the Phase One statutory consultation in autumn 2025, alongside formal communications to suppliers outlining their responsibilities under the scheme. Suppliers should begin preparing for the Readiness Assessment process, with submissions due in winter 2025.

Network operators and industry parties are advised to begin preparatory work on code modifications and system changes necessary to implement the scheme, including the proposed cost recovery mechanism via network charges. Legislative changes related to data sharing are anticipated by early 2026, with Standard Licence Conditions (SLCs) due to take effect from January 2026.

Phase One of the scheme is set to go live in Q1 2026, followed by Phase Two in summer 2026. Both phases will remain open to supplier claims until Q1 2027, after which a wind-down period will conclude the scheme.

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