



Making a positive difference  
for energy consumers

Gwneud gwahaniaeth gwirioneddol  
i ddefnyddwyr ynni

Direct Dial: 020 7901 3877  
Email: [CSS@ofgem.gov.uk](mailto:CSS@ofgem.gov.uk)

Date: 18 December 2014

Dear Colleague

### **Modification of gas supply and electricity supply and generation Licences**

Please find enclosed a modification decision for Standard Licence Condition (SLC) 19A of the gas and electricity supply licences and SLC 16B of the electricity generation licence. We are making these modifications to provide greater transparency of energy company profitability. The modifications will apply for the 2014 Consolidated Segmental Statements (CSS).

We gave notice on 14 November 2014 that we proposed to make modifications to condition 19A of the gas and electricity supply licences and SLC 16B of the electricity generation licence by requiring any representations to the modification to be made on or before 12 December 2014.

The effect of the licence modification is to ensure that the information in the CSS more robust, useful and accessible for consumers, potential new entrants to the market and all other users. Relevant licensees are now required to subject their CSS to a full external audit, including tighter scrutiny of transfer pricing practices, and to publish within four months of the end of their financial year. Relevant licensees will also be required to provide a more detailed cost breakdown and include non-financial information that we consider helps to improve transparency on company costs and operation.

### **Responses to the statutory consultation**

We received 9 responses to the November consultation. We have published non-confidential responses on the Ofgem website. The majority of respondents supported the intent of the proposed licence modifications and had no substantive comments, with the exception of the correction of a few typographical errors and minor suggested amendments to wording. We have made these changes where we consider they improve the clarity of the wording in the licence conditions and better reflect our policy intent.

Two respondents questioned the necessity of modifications to tighten scrutiny of transfer pricing practices, whereas one respondent suggested the new obligation did not go far enough. We have chosen to amend the wording of the licence conditions to ensure that transfer pricing methodologies are appropriate and up-to-date and for auditors to check that they are applied in practice.

One respondent suggested that the requirement of an external audit duplicated some of the original obligations. We have not made any further amendments in response to this suggestion as we consider that they would not deliver the necessary improvements required to improve confidence in the transparency of the statements.

As part of our consultation, we proposed to amend the 'relevant licensee' definition to ensure it only applied to vertically integrated groups of companies. One respondent asked for clarification on whether the definition caught non-active supply licence holders. In response to this, we have made a further minor amendment to the definition so that (non-active) suppliers, who have affiliates that jointly supply over the threshold, no longer fall within the definition. For the avoidance of doubt, we consider that non-active suppliers are not 'relevant licensees'.

Amendments to the current drafting of the licence conditions are double underlined for additions and struck through for deletions. Any further amendments made to the drafting since the proposed drafting in the statutory consultation are highlighted in yellow.

### **Guideline amendments**

In addition to the statutory consultation on the licence modifications in November we also asked for respondents' views on the addition of a line in Appendix 1 of the guidelines that requires relevant licensees to include the supply volume as purchased from the wholesale market (ie without adjusting for losses). The purpose of this proposal was to address the issue that the Weighted Average Cost of Electricity/Gas (WACO E/G) calculation currently assumes losses within the numerator but not within the denominator.

While the majority of respondents had no comments regarding this, one stakeholder strongly objected to the inclusion of purchased volumes in the CSS on the grounds of competition concerns. We consider that we will need more time to assess the implications of making this information publically available and propose to retract this addition from Appendix 1 of the guidelines for now. Nevertheless, we are keen to acquire this information and propose to write to companies separately to ask for purchased volumes on a confidential basis. We would also welcome further views on whether disclosure of this information could have a detrimental impact on competition.

In the October and November consultation we proposed the inclusion of an additional line in Appendix 1 to report exceptional items. We have received mixed responses on the best way to account for exceptional items within Appendix 1. Companies need certainty now on how to prepare their 2014 statements, therefore we have chosen to revert to the original guidelines for the 2014 statements. We reiterate the importance of companies providing a full and clear explanation of their treatment of exceptional items if included. We will revisit the inclusion of exceptional items within the table for the 2015 statements.

We have also made minor amendments to the guidelines to address a number of clarification points raised by respondents. All final modifications to the current guidelines are in red text. Further amendments to the draft guidance issued as part of the statutory consultation in November are highlighted in yellow.

**Next steps**

In accordance with the powers contained in 11A (2) and 23(2) of the Act the Authority has decided to modify Standard Licence Condition (SLC) 19A of the gas and electricity supply licences and SLC 16B of the electricity generation licence. This decision will take effect on and from 13 February 2015 in time for the 2014 CSS.

If you have any queries regarding the information contained within this letter, please contact Robyn Daniell on 0207 901 3877 or by email [CSS@ofgem.gov.uk](mailto:CSS@ofgem.gov.uk)

Yours faithfully

**Neil Barnes**  
**Associate Partner, Retail Markets**  
**For and on behalf of the Gas and Electricity Markets Authority**