

To: All holders of a domestic gas supply licence

Email: [retailpriceregulation@ofgem.gov.uk](mailto:retailpriceregulation@ofgem.gov.uk)

Date: 19 November 2021

## **Domestic Gas and Electricity (Tariff Cap) Act 2018**

### **Notice of statutory consultation on a proposal to modify the standard conditions of all gas supply licences**

1. The Gas and Electricity Markets Authority ('the Authority')<sup>1</sup> proposes to modify the standard conditions of all gas supply licences granted or treated as granted under section 7A(1) of the Gas Act, pursuant to section 1 of the Domestic Gas and Electricity (Tariff Cap) Act 2018 ('the Act'). These proposed modifications are set out in Appendix 1.
2. We are proposing to modify the standard supply conditions, incorporated in supply licences by virtue of section 8 of the Gas Act 1986, namely the conditions which impose a cap on all standard variable and default rates that may be charged by the holders of supply licences for the supply of gas under domestic supply contracts ('the tariff cap conditions'), subject to section 3 of the Act (exemptions from the tariff cap).
3. The Competition and Markets Authority (CMA) designed and introduced the Prepayment Charge Restriction (PPM cap) to protect energy consumers with prepayment meters (PPM customers) from weak competition and barriers to engagement. In August 2020, Ofgem announced that the default tariff cap would protect PPM customers after 31 December 2020, the date the CMA PPM Cap expired.<sup>2</sup>
4. In August 2019, the industry modification XRN 4665 led to the creation of new End User Categories (EUCs), resulting in changes to how industry reports and accounts for gas Annual Load Profiles (ALPs), Unidentified Gas (UIG) and Peak Load Factors (PLFs) for different categories of consumers.<sup>3</sup> In particular, the modification introduced unique EUCs for domestic gas PPM customers, which more accurately reflect their consumption behaviour.
5. In our statutory consultation on reflecting prepayment EUCs in the default tariff cap, we propose to amend the wholesale and network cost methodologies in the price cap to account for the new prepayment EUCs. Currently, the Wholesale Cost Allowance and Network Cost Allowance in Standard Licence Condition (SLC) 28AD of the gas standard supply licence conditions are not calculated for specific payment methods.

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<sup>1</sup> The terms "the Authority", "we" and "us" are used interchangeably in this document.

<sup>2</sup> Ofgem (2020), Protecting energy consumers with prepayment meters: August 2020 decision. [https://www.ofgem.gov.uk/sites/default/files/docs/2020/08/protecting\\_energy\\_consumers\\_with\\_prepayment\\_meters\\_-\\_august\\_2020\\_decision.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2020/08/protecting_energy_consumers_with_prepayment_meters_-_august_2020_decision.pdf)

<sup>3</sup> Xoserve (2019), Creation of new End User Categories. <https://www.xoserve.com/change/change-proposals/xrn-4665-creation-of-new-end-user-categories/>

6. We are proposing to introduce modifications to SLC 28AD of the gas supply licence in order to amend the Wholesale Cost Allowance and Network Cost Allowance to include each payment method. At present, the drafting of the SLCs of the gas supply licence define payment methods; these are denoted by subscript “p” and consist of Standard Credit, Prepayment or Other Payment Method.
7. We therefore propose to make the modifications to SLC 28AD of the gas supply licence set out in Appendix 1.
8. These proposed licence modifications would have effect in relation to supply licences, whenever granted, and on domestic supply contracts, whenever entered into.
9. A more detailed description of the reasons for and effects of these proposed licence modifications can be found in the accompanying document to this Notice, which is available at:  
  
<https://www.ofgem.gov.uk/publications/price-cap-consultation-reflecting-prepayment-end-user-categories-default-tariff-cap>
10. Copies of the proposed modifications and other documents referred to in this Notice have been published on our website (www.ofgem.gov.uk). Alternatively, you can request a paper copy by emailing [retailpriceregulation@ofgem.gov.uk](mailto:retailpriceregulation@ofgem.gov.uk).
11. Any representations with respect to the proposed licence modifications must be made on or before **17 December 2021** by email to [retailpriceregulation@ofgem.gov.uk](mailto:retailpriceregulation@ofgem.gov.uk).
12. 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 they can be placed easily on our website.
13. If we decide to make the proposed modifications, they will take effect not less than 56 days after the decision is published.

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**Leonardo Costa**

**Duly authorised on behalf of the Gas and Electricity Markets Authority**

**19 November 2021**

## Appendix 1 – Draft of proposed changes to modify the standard conditions of all gas supply licences.

We have included the sections of the SLCs we have decided to amend below. New text is double underlined>.

### Condition 28AD. Regulation of charges for Domestic Customers supplied under certain Domestic Supply Contracts

#### Calculation of the Benchmark Maximum Charges for 28AD Charge Restriction Periods

28AD.6 For each 28AD Charge Restriction Period, the Authority will calculate the Benchmark Maximum Charge for each:

- (a) Benchmark Annual Consumption Level;
- (b) Charge Restriction Region; and
- (c) Payment Method

in accordance with the following formula:

$$\begin{aligned} ChargeMax_{i,j,k,p} &= (WC_{j,k,p} + NC_{i,j,k,p} + PC_{j,k} + AA_{i,j,k,p} + OC_{j,k,p} + PA_{i,j,k,p} \\ &\quad + E_{i,j,k,p} + H_{i,j,k,p}) \end{aligned}$$

where (the following units all being in pounds sterling):

$ChargeMax_{i,j,k,p}$  means the Benchmark Maximum Charge in Charge Restriction Region  $i$ , in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , and Payment Method  $p$ ;

$WC_{j,k,p}$  means the Wholesale Cost Allowance in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for payment method  $p$ , calculated in accordance with paragraph 28AD.7;

$NC_{i,j,k,p}$  means the Network Cost Allowance in Charge Restriction Region  $i$ , in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for payment method  $p$ , determined in accordance with paragraph 28AD.8;

$PC_{j,k}$  means the Policy Cost Allowance in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , calculated in accordance with paragraph 28AD.9;

$AA_{i,j,k,p}$	means the Adjustment Allowance in Charge Restriction Region $i$ , in Charge Restriction Period $j$ , at Benchmark Annual Consumption Level $k$ , for Payment Method $p$ calculated in accordance with paragraph 28AD.10A;
$OC_{j,k,p}$	means the Operating Cost Allowance in 28AD Charge Restriction Period $j$ , at Benchmark Annual Consumption Level $k$ , for payment method $p$ , calculated in accordance with paragraph 28AD.10;
$PA_{i,j,k,p}$	means the Payment Method Adjustment in Charge Restriction Region $i$ , in 28AD Charge Restriction Period $j$ , at Benchmark Annual Consumption Level $k$ , for Payment Method $p$ calculated in accordance with paragraph 28AD.11;
$E_{i,j,k,p}$	means the Earnings Before Interest and Tax Allowance in Charge Restriction Region $i$ , in 28AD Charge Restriction Period $j$ , at Benchmark Annual Consumption Level $k$ , for Payment Method $p$ , calculated in accordance with paragraph 28AD.12;
$H_{i,j,k,p}$	means the Headroom Allowance in Charge Restriction Region $i$ , in 28AD Charge Restriction Period $j$ , at Benchmark Annual Consumption Level $k$ , for Payment Method $p$ calculated in accordance with paragraph 28AD.13.

### Wholesale Cost Allowance

28AD.7 For the purposes of paragraph 28A.6 the Wholesale Cost Allowance in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for Payment Method  $p$ , shall be the Direct Fuel Cost Component calculated, subject to paragraphs 28AD.14 and 28AD.15 below, in accordance with the methodology and data sources set out in Annex 2. The value of the Wholesale Cost Allowance at nil consumption will be zero.

### Network Cost Allowance

28AD.8 For the purposes of paragraph 28A.6, the Network Cost Allowance in Charge Restriction Region  $i$ , in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for Payment Method  $p$ , shall be calculated based on the data within the published charging statements of the Network Companies and, subject to paragraphs 28AD.14 and 28AD.15 below, in accordance with the methodology and data sources set out in Annex 3.

### Payment Method Adjustment

28AD.11 For the purposes of paragraph 28A.6, the Payment Method Adjustment in Charge Restriction Region  $i$ , 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$  and for Payment Method  $p$  shall be calculated as follows:

$$PA_{i,j,k,p} = \left( PAAC_{0,p} \times \frac{CPIH_j}{CPIH_0} \right) + \left[ PAP_p \times \left( WC_{j,k,p} + NC_{i,j,k,p} + PC_{j,k} + AA_{i,j,k,p} + OC_{j,k,p} \right) \right]$$

$PAAC_{0,p}$  means the Baseline Value for the Payment Method Adjustment Additional Cost for Payment Method  $p$ , as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.16.

$PAP_p$  means the Baseline Value for the Payment Method Adjustment Percentage  $p$ , as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.16.

$CPIH_j$  has the meaning given to in paragraph 28AD.10.

$CPIH_0$  has the meaning given to in paragraph 28AD.10.

### Earnings Before Interest and Tax Allowance

28AD.12 For the purposes of paragraph 28A.6, the Earnings Before Interest and Tax Allowance in Charge Restriction Region  $i$ , in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for Payment Method  $p$ , shall be calculated as follows:

$$E_{i,j,k,p} = EBIT \times (WC_{j,k,p} + NC_{i,j,k,p} + PC_{j,k} + AA_{i,j,k,p} + OC_{j,k,p} + PA_{i,j,k,p})$$

where:

$EBIT$  means the Baseline Value for the Earnings Before Interest and Tax Margin Percentage, as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.16.

### Headroom

28AD.13 For the purposes of paragraph 28A.6, the Headroom Allowance in Charge Restriction Region  $i$ , in 28AD Charge Restriction Period  $j$ , at Benchmark Annual Consumption Level  $k$ , for Payment Method  $p$ , shall be calculated as follows:

$$H_{i,j,k,p} = HAP \times (WC_{j,k,p} + PC_{j,k} + AA_{i,j,k,p} + OC_{j,k,p} + PA_{i,j,k,p} + E_{i,j,k,p})$$

where:

*HAP* means the Baseline Value for the Headroom Allowance Percentage as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.16.

$PA_{i,j,k,p}$  means the Payment Method Adjustment in Charge Restriction Region *i*, in 28AD Charge Restriction Period *j*, at Benchmark Annual Consumption Level *k*, for Payment Method *p* calculated in accordance with paragraph 28AD.11

**‘Direct Cost Fuel Component’** means the component of the Wholesale Cost Allowance that is calculated to reflect the cost of wholesale gas purchases in 28AD Charge Restriction Period *j*, at Benchmark Annual Consumption Level *k*, for payment method *p*, and which the Authority is to calculate for the periods and within the timeframes specified in this condition 28AD in accordance with the methodology set out in Annex 2;

**‘Network Cost Allowance’** means the amount calculated to reflect the costs associated with transmission and distribution charges in Charge Restriction Region *i*, in 28AD Charge Restriction Period *j*, at Benchmark Annual Consumption Level *k*, for payment method *p*, which the Authority is to calculate for the periods and within the timeframes specified in this condition 28AD in accordance with the methodology set out at Annex 3;

**‘Wholesale Cost Allowance’** means the amount calculated to reflect the cost of wholesale gas in 28AD Charge Restriction Period *j*, at Benchmark Annual Consumption Level *k*, for payment method *p*, the component of which is the Direct Fuel Cost Component, and which the Authority is to calculate for the periods and within the timeframes specified in this condition 28AD in accordance with the methodology set out at Annex 2.