

To: All holders of a gas and/or
electricity supply licence

Email: priceprotectionpolicy@ofgem.gov.uk.

Date: 25 August 2023

Domestic Gas and Electricity (Tariff Cap) Act 2018

Section 4(2)

Notice of modification to the standard licence condition 28AD of all Gas and Electricity Supply Licences (the "Notice")

1. Each of the companies to whom this notice is addressed holds either (1) an electricity supply licence granted, or treated as granted, pursuant to section 6(1)(d) of the Electricity Act 1989; or (2) a gas supply licence granted, or treated as granted, pursuant to section 7A(1) of the Gas Act 1986.
2. The Gas and Electricity Markets Authority ('the Authority')¹ gives notice that it has decided to modify the standard conditions of all gas and electricity supply licences granted or treated as granted under section 6(1)(d) of the Electricity Act 1989 and section 7A(1) of the Gas Act 1986, pursuant to section 1 of the Domestic Gas and Electricity (Tariff Cap) Act 2018 ('the 2018 Act'), by amending Standard Licence Condition (SLC) 28AD (Regulation of charges for Domestic Customers supplied under certain Domestic Supply Contracts), namely the conditions which impose a cap on all standard variable and default rates that may be charged by the holders of a supply licence for the supply of gas or electricity under domestic supply contracts, subject to section 3 of the Act (exemptions from the tariff cap). The modifications are set out in Annex 1 and Annex 2.
3. The Authority has decided to amend SLC 28AD and Annex 1 of SLC 28AD of the Gas and Electricity Supply Licences.

¹ The terms "the Authority" and "we" are used interchangeably in this document.

4. The effect of this modification is to amend the Earnings Before Interest and Tax (EBIT) allowance in the default tariff cap to revise the allowance and introduce a hybrid methodology which the Authority considers is more appropriate. The modifications will introduce a new fixed EBIT component and alter the EBIT percentage from the current value. This will help ensure that the EBIT allowance remains cost- and risk-reflective, contributing to the resilience of the sector and to better quality of services – which both protects and benefits customers.
5. This Notice is published alongside a decision setting out the case for change and our detailed considerations of the methodological approach. Further details of the reasons for and effects of these modifications can be found in the main decision document, which is available at: <https://www.ofgem.gov.uk/publications/changes-methodology-price-cap-earnings-tax-ebit-allowance-decision>
6. A copy of the modifications and other documents referred to in this Notice have been published on our website (<https://www.ofgem.gov.uk>). Alternatively, you can request a copy by emailing foi@ofgem.gov.uk.
7. The modifications will take effect on the 1 October 2023.



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Dan Norton

Deputy Director, Retail Price Protection

Duly authorised on behalf of the Gas and Electricity Markets Authority

25 August 2023

Annex 1 – Modifications to the standard licence conditions of electricity supply licences

Deletions are denoted with a strike-through and new text is denoted with a double underlining.

Condition 28AD of the electricity supply licence

Modification: Amend existing paragraph

28AD.13 For the purposes of paragraph 28AD.7, 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 Benchmark Metering Arrangement l , for Payment Method p , shall be calculated as follows:

$$E_{i,j,k,l,p} = \frac{\text{EBIT Fixed Component}_i + ((\text{EBIT Percentage}_i \times (\text{WC}_{i,j,k,l} + \text{NC}_{i,j,k,l} + \text{PC}_{i,j,k,l,p} + \text{AA}_{i,j,k,l} + \text{OC}_{j,k,l,p} + \text{PA}_{i,j,k,l,p})))}{\text{EBIT}}$$

where:

EBIT Fixed Component means the Baseline Value for the Earnings Before Interest and Tax Margin Fixed Component, as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.17.

EBIT Percentage 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.17.

Modification: Amend selected definitions from existing paragraph

28AD.40

'**Baseline Value**' means the values as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.17 and in the format set out at Annex 1. These are the values of the Baseline Value for the Operating Cost Allowance, the Headroom Allowance Percentage, the Earnings Before Interest and Tax Margin Percentage, the Earnings Before Interest and Tax Margin Fixed Component, the Payment Method Adjustment Additional Cost and Payment Method Adjustment Percentage;

'**Earnings Before Interest and Tax Allowance**' means the amount to reflect a return on capital, calculated by the sum of

- a) the figure arrived at by applying the Earnings Before Interest and Tax Margin Percentage by the sum of the Wholesale Cost Allowance, the Network Cost Allowance, the Policy Cost Allowance, the Adjustment Allowance, the Operating Cost Allowance and the Payment Method Adjustment, in Charge Restriction Region i , Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , for Payment Method p ; and
- b) the Earnings Before Interest and Tax Fixed Component,

which the Authority is to calculate for the periods and within the timeframes specified in this condition 28AD in accordance with paragraph 28AD.13;

'Earnings Before Interest and Tax Fixed Component' means the amount, expressed as a value as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.17 and in the format set out in Annex 1, in order to calculate part of the Earnings Before Interest and Tax Allowance;

'Earnings Before Interest and Tax Margin Percentage' means the value, expressed as a percentage as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.17 and in the format set out in Annex 1, by which the Wholesale Cost Allowance, the Network Cost Allowance, the Policy Cost Allowance, the Adjustment Allowance, the Operating Cost Allowance and the Payment Method Adjustment is to be multiplied in order to calculate part of the Earnings Before Interest and Tax Allowance;

Modification: Amend table in Annex 1

Annex 1 – Format for publishing Baseline Values and Initial Value of the CPIH Index

Baseline Values

Earnings Before Interest and Tax Margin Percentage Allowance

<u>EBIT Fixed Component</u>	
<u>EBIT Percentage</u>	

Annex 2 – Modifications to the standard licence conditions of gas supply licences

Deletions are denoted with a strike-through and new text is denoted with a double underlining.

Condition 28AD of the gas supply licence

Modification: Amend existing paragraph

28AD.12 For the purposes of paragraph 28AD.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 Benchmark Metering Arrangement l , for Payment Method p , shall be calculated as follows:

$$E_{i,j,k,l,p} = \frac{\text{EBIT Fixed Component}_i}{\text{EBIT Percentage}_i} \times (\text{WC}_{i,j,k,l} + \text{NC}_{i,j,k,l} + \text{PC}_{i,j,k,l,p} + \text{AA}_{i,j,k,l} + \text{OC}_{j,k,l,p} + \text{PA}_{i,j,k,l,p})$$

where:

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

EBIT Percentage 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.

Modification: Amend selected definitions from existing paragraph

28AD.40

'Baseline Value' means the values as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.16 and in the format set out at Annex 1. These are the values of the Baseline Value for the Operating Cost Allowance, the Headroom Allowance Percentage, the Earnings Before Interest and Tax Margin Percentage, the Earnings Before Interest and Tax Margin Fixed Component, the Payment Method Adjustment Additional Cost and Payment Method Adjustment Percentage;

'Earnings Before Interest and Tax Allowance' means the amount to reflect a return on capital, calculated by the sum of

- a) the figure arrived at by applying the Earnings Before Interest and Tax Margin Percentage by the sum of the Wholesale Cost Allowance, the Network Cost Allowance, the Policy Cost Allowance, the Adjustment Allowance, the Operating Cost Allowance and the Payment Method Adjustment, in Charge Restriction Region i , Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , for Payment Method p ; and
- b) the Earnings Before Interest and Tax Fixed Component,

which the Authority is to calculate for the periods and within the timeframes specified in this condition 28AD in accordance with paragraph 28AD.12;

'Earnings Before Interest and Tax Fixed Component' means the amount, expressed as a value as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.16 and in the format set out in Annex 1, in order to calculate part of the Earnings Before Interest and Tax Allowance;

'Earnings Before Interest and Tax Margin Percentage' means the value, expressed as a percentage as specified by the Authority by publishing a statement in Writing in accordance with paragraph 28AD.16 and in the format set out in Annex 1, by which the Wholesale Cost Allowance, the Network Cost Allowance, the Policy Cost Allowance, the Adjustment Allowance, the Operating Cost Allowance and the Payment Method Adjustment is to be multiplied in order to calculate part of the Earnings Before Interest and Tax Allowance;

Modification: Amend table from Annex 1

Annex 1 – Format for publishing Baseline Values and Initial Value of the CPIH Index

Baseline Values

Earnings Before Interest and Tax Margin Percentage Allowance

<u>EBIT Fixed Component</u>	
<u>EBIT Percentage</u>	