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Dear Timothy

### **Improving Reporting Transparency**

SSE welcomes the opportunity to comment on Ofgem's consultation on Improving Reporting Transparency. Ofgem's proposals seek to provide greater transparency for consumers in the expectation that this will lead to increased confidence in competition. We recognise the importance of providing a clear indication of the profit margins earned by energy suppliers in fostering confidence in the market. SSE engaged constructively with the independent review of segmental statements conducted by BDO and welcomes their finding that the financial information they contain is "fair and appropriate."

We welcome efforts to build consumer trust in the competitive market, and the benefits that effective competition has delivered. However, we are concerned that in some areas Ofgem does not appear to have acknowledged the tension that exists between improving the transparency of the profitability of individual companies and improving the comparability of segmental statements provided by different companies (which differ considerably in their structure, operation, accounting and size). This issue is particularly relevant in considering Recommendations 6 and 8, which we describe below and cover in more detail in our answers to the specific questions in the attached appendix.

#### **Recommendation 6 – report fuel costs in generation segment**

SSE considers Generation and Wholesale activities to be part of one integrated business activity. SSE manages its fuel procurement by aggregating fuel requirements for all assets and for gas supply customers and managing the risk on the net position. Requiring SSE to report fuel and carbon costs under generation would also require the inclusion of all fuel procurement and wholesale trading activity in the same segment. Generation receives its income from providing capacity to wholesale energy trading through Power Purchase Agreements (PPAs). We therefore do not have the data required to present an income statement for the generation segment in the manner that would be required by this proposal.

Our suggested solution to this would be to publish a footnote to our Consolidated Segmental Statement (CSS) with aggregated fuel and carbon costs for our thermal generation, and report the number and value of EU ETS allowances. In particular this would alleviate our concern that implementing this proposal would result in confusion amongst shareholders and city analysts who refer to our CSS and expect to be able to reconcile items to the treatment in our company accounts.

#### **Recommendation 8 – reconciliation based on EBITDA**

This recommendation would require us to reconcile against a number that does not appear explicitly in our published accounts. Reconciliation to EBITDA would introduce additional items into the reconciliation which are not necessarily available in our annual report. We are concerned that trust in the CSS and in energy suppliers will be damaged if the analysis required to reconcile the data to audited accounts is either obscure or not easily accessible.

Reconciliation based on EBIT is completely transparent and we believe that this is a far more important consideration for the CSS. We would therefore suggest that the reconciliation based on EBIT as currently used by five companies should not be changed. If Ofgem are minded to improve consistency of reconciliation then requiring that one company changes their current methodology to use EBIT would be more consistent with the principles of better regulation.

#### **Other recommendations and issues**

We are concerned at the suggestion of including a capital employed figure for generation and aggregated supply activities to help calculate ROCE. We believe that the CSS already provides transparency on profitability of generation and supply activities. It is also noteworthy that even when energy supply was price controlled the profit calculation was based on percentage of turnover, not ROCE. There are features of generation and supply that make ROCE an inappropriate measure of profitability and SSE do not believe that this metric would enhance either comparability or transparency of profits reported.

#### **Conclusion**

SSE welcomes measures that can enhance consumer confidence in the effectiveness of competition in energy supply. We are ready to support proposals which we believe will help to build trust by improving transparency of the profitability of energy companies. However we remain concerned at the tendency for Ofgem to promote comparability of financial reporting at the expense of transparency. Given that part of the purpose of the CSS is to promote competition by informing potential new entrants to the energy supply market of the margins currently earned, we believe that there is merit in Ofgem considering whether smaller suppliers should also be required to publish statements. Our more detailed response is contained in the attached appendix.

We will continue to engage with Ofgem in a constructive manner in order to arrive at the best possible outcome for consumers in the GB energy supply market. Please contact me on 01738 456726 if you wish to discuss any the points raised in this response.

Yours sincerely

A handwritten signature in black ink that reads 'Roger Hutcheon'.

Roger Hutcheon  
**Regulation**