



Making a positive difference
for energy consumers

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

Email: retailpriceregulation@ofgem.gov.uk

Date: 18 May 2020

Domestic Gas and Electricity (Tariff Cap) Act 2018

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

1. The Gas and Electricity Markets Authority ('the Authority')¹ proposes 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 Act'). These proposed modifications are set out in Appendix 1 and Appendix 2.
2. We are proposing to modify the standard supply conditions, incorporated in supply licences by virtue of section 8 of the Gas Act 1986 or section 8A of the Electricity Act 1989, 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 or electricity under domestic supply contracts ('the tariff cap conditions'), subject to section 3 of the Act (exemptions from the tariff cap).
3. In November 2019, following Judicial Review proceedings, the High Court concluded that the Authority must reconsider the wholesale allowance for the first cap period of

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

the default tariff cap ('the cap'), and make such adjustments to the allowance as it considers appropriate in the light of that reconsideration.²

4. We propose to modify Standard Licence Condition ('SLC') 28AD of the electricity and gas supply licences in order to introduce an "adjustment allowance" component to the cap methodology.
5. We propose to use the adjustment allowance to address the outcome of the Judicial Review in cap period five. For future periods, we propose to maintain the adjustment allowance in the cap methodology but at '0' where there are no further adjustments required.
6. We propose to introduce a new annex to SLC 28AD, alongside the new adjustment allowance, within which we will set out the calculations for the value of the adjustment allowance in each period.
7. We propose to set the adjustment allowance so that it changes the maximum variable charge in the default tariff cap. We propose to include the new component as condition "28AD.10A". We propose this approach so that we may preserve the numbering of the licence conditions and cause minimum disturbance to the drafting of the existing conditions. However, we must highlight that the new adjustment component is not related to the preceding condition, which is the Policy Cost Allowance at 28AD.10.
8. We therefore propose to make the modifications to SLC 28AD in the gas and electricity supply licences as set out in Appendix 1 and Appendix 2.
9. We are also taking the opportunity to propose to correct typographical errors in the gas SLC 28AD. We have set out a table with the proposed modifications to the conditions, in Appendix 3.
10. These proposed licence modifications would have effect in relation to supply licences, whenever granted, and domestic supply contracts, whenever entered into.
11. A more detailed description of the reasons for and effects of this proposed licence modification can be found in the accompanying document to this Notice, which is available at: <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-reassessing-wholesale-allowance-first-default-tariff-cap-period>

² [2019] EWHC 3048 (Admin): <https://www.bailii.org/ew/cases/EWHC/Admin/2019/3048.html>

12. 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 library@ofgem.gov.uk.
13. Any representations with respect to the proposed licence modifications must be made on or before **Friday 26 June 2020** to retailpriceregulation@ofgem.gov.uk.
14. 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.
15. 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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Anna Rossington

Duly authorised on behalf of the Gas and Electricity Markets Authority

18 May 2020

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

We have included the sections of the SLCs we have decided to remove or amend below. Deletions are shown in strike through and 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.7 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;
- (c) Benchmark Metering Arrangement; and
- (d) Payment Method

in accordance with the following formula:

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

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

ChargeMax_{i,j,k,l,p} means the Benchmark Maximum Charge in Charge Restriction Region *i*, in 28AD Charge Restriction Period *j*, at Benchmark Annual Consumption Level *k*, for Benchmark Metering Arrangement *l*, and Payment

Method p ;

- $WC_{i,j,k,l}$ means the Wholesale Cost Allowance in Charge Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , calculated in accordance with paragraph 28AD.8;
- $NC_{i,j,k,l}$ means the Network Cost Allowance in Charge Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , determined in accordance with paragraph 28AD.9;
- $PC_{i,j,k,l}$ means the Policy Cost Allowance in Charge Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , calculated in accordance with paragraph 28AD.10;
- $AA_{i,j,k,l,p}$ means the Adjustment Allowance in Charge Restriction Region i , in Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , for Payment Method p calculated in accordance with paragraph 28AD.10A;
- $OC_{j,k,l}$ means the Operating Cost Allowance in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , calculated in accordance with paragraph 28AD.11;
- $PA_{i,j,k,l,p}$ means the Payment Method Adjustment in Charge

Restriction Region i , in Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , for Payment Method p calculated in accordance with paragraph 28AD.12;

$E_{i,j,k,l,p}$ means the Earnings Before Interest and Tax Allowance in Charge Restriction Region i , in Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l , for Payment Method p , calculated in accordance with paragraph 28AD.13;

$H_{i,j,k,l,p}$ means the Headroom 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 calculated in accordance with paragraph 28AD.14.

Adjustment Allowance

28AD.10A For the purposes of 28AD.7, the Adjustment Allowance in 28AD Charge Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l and for Payment Method p is a sum of adjustments to the default tariff cap, subject to paragraph 28AD.16, calculated in accordance with the methodology set out in Annex 8.

Payment Method Adjustment

28AD.12 For the purposes of paragraph 28AD.7, the Payment Method Adjustment in Charge Restriction Region i , in 28AD Charge Restriction Period j , at

Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l and for Payment Method p shall be calculated as follows:

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

where:

$PAAC_{0,p}$ 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.17 or, from time to time and following consultation, and in relation to the Baseline Value for Fully-Interoperable Smart Prepayment only, re-published by the Authority by way of a statement in Writing where it appears to the Authority that it is necessary to amend the Baseline Value for Fully-Interoperable Smart Prepayment.

$PAP_{l,p}$ means the Baseline Value for the Payment Method Adjustment Percentage, for Benchmark Metering Arrangement l , for Payment Method p , as published by the Authority by way of a statement in Writing pursuant to paragraph 28AD.17 or, from time to time and following consultation, and in relation to the Baseline Value for Fully-Interoperable Smart Prepayment only, re-published by the Authority by way of a statement in Writing where it appears to the Authority that it is necessary to amend the Baseline Value for Fully-Interoperable Smart Prepayment.

$CPIH_j$ has the meaning given to in paragraph 28AD.11.

$CPIH_0$ has the meaning given to in paragraph 28AD.11.

Earnings Before Interest and Tax Allowance

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:

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

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.17.

Headroom

28AD.14 For the purposes of paragraph 28AD.7, the Headroom 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:

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

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.17.

$PA_{i,j,k,l,p}$ means the Payment Method Adjustment 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 calculated in accordance with paragraph 28AD.12.

Data sources

28AD.16 The Authority may from time to time, and following consultation, amend the methodology set out in Annex 2, Annex 3, ~~Annex 4~~, Annex 5 or Annex 8 by way of a statement in Writing, where the Authority considers that either:

- (a) there has been a significant and unanticipated change of circumstances such that Annex 2, Annex 3, Annex 4, ~~Annex 5~~ or Annex 8 no longer reflects an efficient level of any of the Wholesale Cost Allowance, Network Cost Allowance, Policy Cost Allowance, ~~Smart Metering Net Cost Change~~ or Adjustment Allowance; or
- (b) there is a typographical or mathematical error in any of Annex 2, Annex 3, Annex 4, or Annex 5, or Annex 8 such that an amendment is necessary in order to ensure the proper functioning of the relevant methodology.

Definitions for condition

28AD.40 In this condition:

‘Adjustment Allowance’ means a sum of adjustments to the default tariff cap, 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 , 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 8.

Annex 8 – Methodology for Adjustment Allowance

.xlsx file available at <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-reassessing-wholesale-allowance-first-default-tariff-cap-period>

Appendix 2 – 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 remove or amend below. Deletions are shown in strike through and 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:

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

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 ;

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

$NC_{i,j,k}$	means the Network Cost Allowance in Charge Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , 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;
<u>$AA_{i,j,k,p}$</u>	<u>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;</u>
$OC_{j,k}$	means the Operating Cost Allowance in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , 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.

Adjustment Allowance

28AD.10A For the purposes of 28AD.6 the Adjustment Allowance in 28AD Charge

Restriction Region i , in 28AD Charge Restriction Period j , at Benchmark Annual Consumption Level k , for Benchmark Metering Arrangement l and for Payment Method p is a sum of adjustments to the default tariff cap, subject to paragraph 28AD.15, calculated in accordance with the methodology set out in Annex 8.

Payment Method Adjustment

28AD.11 For the purposes of paragraph 28AD.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:

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

$PAAC_{0,p}$ 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 or, from time to time and following consultation, and in relation to the Baseline Value for Fully-Interoperable Smart Prepayment only, re-published by the Authority by way of a statement in Writing where it appears to the Authority that it is necessary to amend the Baseline Value for Fully-Interoperable Smart Prepayment.

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 or, from time to time and following consultation, and in relation to the Baseline Value for Fully-Interoperable Smart Prepayment only, re-published by the Authority by way of a statement in Writing where it appears to the Authority that it is necessary to amend the Baseline Value for Fully-Interoperable Smart Prepayment.

$CPIH_j$ 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 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 Payment Method p , shall be calculated as follows:

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

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 28AD.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:

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

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

Data sources

28AD.15 The Authority may from time to time, and following consultation, amend the methodology set out in Annex 2, Annex 3, Annex 4, ~~Annex 5~~ or Annex 8 by way of a statement in Writing, where the Authority considers that either:

- (a) there has been a significant and unanticipated change of circumstances such that Annex 2, Annex 3, Annex 4, ~~Annex 5~~ or Annex 8 no longer reflects an efficient level of any of the Wholesale Cost Allowance, Network Cost Allowance, Policy Cost Allowance, ~~Smart Metering Net Cost Change~~ Adjustment Allowance; or
- (b) there is a typographical or mathematical error in any of Annex 2, Annex 3, Annex 4, or Annex 5 or Annex 8 such that an amendment is necessary in order to ensure the proper functioning of the relevant methodology.

Definitions for condition

28AD.33 In this condition:

'Adjustment Allowance' means a sum of adjustments to the default tariff cap, 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 , 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 8.

Annex 8 – Methodology for Adjustment Allowance

.xlsx file available at <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-reassessing-wholesale-allowance-first-default-tariff-cap-period>

Appendix 3 – Table of proposed modifications to standard conditions of all gas supply licences: correction of typographical errors.

We have included the sections of the SLCs we have decided to remove or amend below.

Deletions are shown in strike through and new text is double underlined.

Condition	Alteration	Reason for alteration
28AD.2	in order to comply with paragraph 28AD <u>.2</u> ,	To correct a cross-referencing typographical error
28AD.5	ChargeMax(m) and ChargeMax(nil) are defined as described in paragraph 28AD <u>.6</u> .	To correct a cross-referencing typographical error
28AD.7	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error
28AD.8	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error
28AD.9	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error
28AD.10	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error
28AD.11	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error
28AD.12	For the purposes of paragraph 28AD <u>.6</u>	To correct a cross-referencing typographical error

Condition	Alteration	Reason for alteration
28AD.12	the Earnings Before Interest and Tax Allowance in Charge Restriction Region <i>i</i>	To correct a typographical error
28AD.13	For the purposes of paragraph 28AD.6	To correct a cross-referencing typographical error
28AD.17	(a) determine the Benchmark Maximum Charges which shall apply for the First Charge Restriction Period <i>j</i> by calculating such values in accordance with paragraph 28AD.6; and	To correct a cross-referencing typographical error
28AD.18	determine the updated Benchmark Maximum Charges which shall apply for the any forthcoming 28AD Charge Restriction Period <i>j</i> by calculating such values in accordance with paragraph 28AD.6	To correct a cross-referencing typographical error
28AD.33	Charge Restriction' means the obligation set out in paragraph 28AD.2;	To correct a cross-referencing typographical error