

The Company Secretary

SSE Energy Supply Limited  
55 Vastern Road  
Reading Berkshire  
RG1 8BU, UK

14 December 2015

Dear Sir/Madam

### **Derogation to allow a differentiation in payment method differential**

This letter sets out the decision of the Gas and Electricity Markets Authority (the “**Authority**”) to grant SSE Energy Supply Limited (company number 03757502 – electricity) and Southern Electric Gas Limited (company number 02716495 – gas) (each a “**Licensee**” and collectively, “**SSE**”), an enduring derogation from certain standard conditions of its gas and electricity supply licences. This derogation will enable SSE to continue offering zero payment method differential through its white label, and under the brand of, **Ebico** to its EquiGas and EquiPower tariffs if Ebico introduces additional tariffs with positive payment method differential.

The relevant Directions are attached and will be published. These Directions will remain in force, in accordance with their terms, on an enduring basis, unless revoked or varied in writing by the Authority. Any change in circumstances relevant to the Directions must be reported to the Authority as soon as possible.

This letter constitutes the Notice, under section 49A of the Electricity Act 1989 and section 38A of the Gas Act 1986, of the reasons for the Authority’s decision to issue the attached Directions. Capitalised terms used in this letter, which are not defined herein, have the meaning given to them in the standard conditions of the Licensee’s electricity and gas supply licences.

### **Background to the Derogation Request**

Ebico is one of SSE’s white labels, which they consider to have a distinct social business model. Its profits are donated to its charity, the Ebico Trust, which supports initiatives to improve the energy efficiency of the homes of low-income householders. Ebico currently offers a single gas tariff (EquiGas) and a single electricity tariff (EquiPower). Both tariffs have zero standing charge, meaning that the customer only pays for what they use. They also have zero payment method differential, meaning that all customers within a distribution region pay the same price regardless of their payment method.<sup>1</sup> Ebico indicates that the zero payment method differential allows it to socialise the higher cost of serving prepayment meter (PPM) customers across its entire customer base.

The Authority received a request from SSE on 16 October 2015 for a derogation from complying with the requirements in sub-paragraph 22B.7A (b) and (c) of its gas and electricity supply licences. Ebico

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<sup>1</sup> There are 14 licensed electricity distribution network operators (DNOs) in Britain and eight gas distribution networks (GDNs). Each covers a separate geographical region and is responsible for regional distribution services. Energy suppliers can face different costs associated with the supply in each region.

wishes to introduce additional tariffs with a non-zero payment method differential, some of which will be targeted at consumers in vulnerable situations.

The rules for White Labels in SLC 22B.7A of paragraph 4 of SLC 31D of the gas and electricity supply licences require a domestic supplier to ensure that any payment method differentials are cost reflective and applied in the same way. This applies to all of the licensee's White Label Tariffs of the same White Label Tariff Provider. However, paragraph 30 of SLC 31D provides that the Authority may issue directions relieving a licensee of its obligations to comply with SLC 31D to such extent and subject to such conditions as the Authority may direct.

Without a derogation, Ebico would not be allowed to offer additional tariffs with non-zero payment method differential while maintaining zero payment method differential for its existing tariffs. SSE has submitted that complying with the payment method differential rule would result in higher prices for existing vulnerable customers particularly those on PPM tariffs as they may have to increase the price for PPM customers to ensure that the differential is applied in the same way across all its tariffs. SSE also indicated that the EquiGas and EquiPower tariffs are attractive to low energy usage customers, particularly PPM customers who may benefit from paying less overall.

### **The Authority's Decision**

We have considered our principal objective and statutory duties, including our duty to protect the interests of future and existing consumers, in carrying out our functions to promote competition where appropriate and to have regard to the interests of vulnerable consumers. We have also taken into consideration the information submitted by SSE. We consider that the proposal to maintain the existing zero payment method differential on Ebico's EquiGas and EquiPower tariffs while all Ebico's new tariffs would have the same (non-zero) payment method differential, would have the potential to benefit consumers in a way that is consistent with our consumer outcomes.<sup>2</sup> We do not consider that granting this derogation undermines the objectives of the Retail Market Review (RMR).

In our derogations guidance, we indicated that we would consider social tariffs and schemes specifically targeted towards vulnerable customers when assessing the need for derogation from RMR rules.<sup>3</sup> This includes considering the consumer outcomes set out in our corporate strategy, particularly the impact on bills and social outcomes. In this case, we consider that Ebico's zero payment method differential can help in reducing the bills of its prepayment customers by allowing cross subsidisation by Direct Debit customers. This social characteristic of Ebico's business model is communicated to Ebico's customers and any resulting profit it makes is paid into Ebico Trust, which is used for charitable ends.

The RMR rules were introduced to increase consumer engagement in order to stimulate competition in the retail market, in part by reducing tariff complexity.<sup>4</sup> Having the same payment method differential across all tariffs of a given supplier is aimed at making comparison easier for consumers. While we recognise that allowing SSE to continue offering zero payment method differential on Ebico's EquiGas and EquiPower tariffs may increase complexity in consumer decision-making, we consider that this would be more than offset by the expected benefits accruing to consumers in vulnerable circumstances targeted by the tariffs.

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<sup>2</sup> Our desired consumer outcomes are set out in our corporate strategy. See "Ofgem: Our Strategy" published on 18 December 2014 available here: <https://www.ofgem.gov.uk/publications-and-updates/corporate-strategy>

<sup>3</sup> See "Guidance for derogation requests from domestic Retail Market Review (RMR) licence conditions", published on 22 June 2015 available here: [https://www.ofgem.gov.uk/sites/default/files/docs/2015/06/guidance\\_for\\_derogation\\_requests\\_from\\_domestic\\_retail\\_market\\_review\\_licence\\_conditions\\_version\\_2\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2015/06/guidance_for_derogation_requests_from_domestic_retail_market_review_licence_conditions_version_2_0.pdf)

<sup>4</sup> In this document we use the term "market" as shorthand for referring to different segments of the energy sector. For the avoidance of doubt, these terms are not intended to describe or otherwise suggest the approach that may be taken by Ofgem for the purposes of market definition in competition law investigations.

Last year, we highlighted concerns raised by stakeholders, including MPs and consumer groups, about suppliers withdrawing zero standing charge tariffs since the RMR rules were introduced.<sup>5</sup> We consider that such tariffs may be suitable for some consumer groups and consider that the direct financial benefits resulting from consumer savings and the social benefits would likely outweigh any potential detrimental impacts arising from any increase in complexity.

We consider that this derogation decision is consistent with our interpretation of the aims of the EU gas and electricity directives in respect of payment method differentials, in that the ultimate aim is to protect the interest of customers that may have no choice but to accept more expensive payment methods.<sup>6</sup> In addition, we consider that this decision is in line with our objective as a National Regulatory Authority to protect the interest of vulnerable consumers.

Therefore, the Authority grants the Licensee an enduring derogation from sub paragraphs (b) and (c) of SLC 22.B7A for White Labels within paragraph 4 of SLC 31D of its gas and electricity supply licences in respect of the Licensee's white label's EquiGas and EquiPower tariffs, subject to the terms of the attached Directions. Please note that the Licensee is required to comply with the cost reflectivity requirements in SLC 27.2A, which requires that any difference in terms and conditions as between payment methods for paying charges for the supply of gas or electricity should reflect the costs to the supplier of the different payment methods. Please also note that the Licensee is required to ensure full compliance with the Cheapest Tariff Messaging (CTM) requirements, as specific in its supply license, by providing consumers with personalised information on how much they could save by switching tariffs within Ebico's tariffs and from Ebico to SSE's tariffs.

If you would like to discuss any aspects of this letter, please contact Jibirila Leinyuy on 0207 901 7000 or [Derogations@ofgem.gov.uk](mailto:Derogations@ofgem.gov.uk).

Yours sincerely,

**Neil Barnes**  
**Associate Partner, Retail Markets**

Signed on behalf of the Authority and authorised for that purpose.

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<sup>5</sup> See our 20 June 2014 open letter available here: [https://www.ofgem.gov.uk/sites/default/files/docs/2015/05/open\\_letter\\_-\\_treatment\\_of\\_low\\_and\\_zero\\_consumers\\_of\\_gas\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2015/05/open_letter_-_treatment_of_low_and_zero_consumers_of_gas_0.pdf)

<sup>6</sup> Ofgem has previously expressed this interpretation for the purposes of SLC 27.2A in the 2009 guidelines on cost reflectivity available here: [https://www.ofgem.gov.uk/sites/default/files/docs/2009/08/2-19\\_-\\_guidelines\\_on\\_cost\\_reflectivity\\_and\\_undue\\_discrimination\\_in\\_supply.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2009/08/2-19_-_guidelines_on_cost_reflectivity_and_undue_discrimination_in_supply.pdf)

## **ATTACHMENT: Electricity Supply Licence**

The Company Secretary

SSE Energy Supply Limited  
55 Vastern Road  
Reading Berkshire  
RG1 8BU, UK

### **Direction issued to SSE Energy Supply Limited (company number 03757502, the "Licensee") by the Gas and Electricity Markets Authority – Treatment of adjustments for payment methods**

1. This Direction is issued by the Gas and Electricity Markets Authority (the "**Authority**") pursuant to paragraph 24 of Standard Licence Condition ("**SLC**") 31D of the electricity supply licence granted under section 6(1)(d) of the Electricity Act 1989 (the "**Licence**").
2. Capitalised terms used in this Direction which are not defined in this Direction shall have the meaning given to them in the Licence.
3. In this Direction the "**EquiPower and EquiGas Tariffs**" mean the Licensee's zero standing charge Tariffs of the same name which constitute Evergreen Supply Contracts and which are aimed at low energy users.
4. Paragraph 24 of SLC 31D provides that the Authority may issue directions relieving the Licensee of its obligations to comply with SLC 31D to such extent and subject to such conditions as the Authority may direct.
5. The considerations taken into account in, and the reasons for, the Authority's decision are set out in the accompanying letter to the Licensee dated 14 December 2015.
6. The Authority hereby directs, pursuant to paragraph 24 of SLC 31D, that the Licensee is, on an enduring basis and subject to the Licensee's continuing compliance with the condition in paragraph 7 of this Direction, relieved of certain of its obligations under paragraph 4 of SLC 31D such that the amended drafting for White Label Tariffs in sub-paras (b) and (c) of condition 22B.7A does not apply to the EquiPower and EquiGas Tariffs. Therefore the EquiPower and EquiGas Tariffs may maintain their zero payment method differential, whilst allowing subsequent future tariffs to have a difference in the Charges for Supply of Electricity as between payment methods as described further in the accompanying letter to the Licensee dated 14 December 2015.
7. The Licensee is required to report any change of circumstances relevant to this Direction to the Authority in writing.
8. This Direction shall take immediate effect on and from the date of this Direction and shall remain in effect on an enduring basis, unless revoked or varied in writing by the Authority.

Dated: 14 December 2015

**Neil Barnes**  
**Associate Partner, Retail Markets**

Signed on behalf of the Authority and authorised for that purpose.

## **ATTACHMENT: Gas Supply Licence**

The Company Secretary

SSE Energy Supply Limited  
55 Vastern Road  
Reading Berkshire  
RG1 8BU, UK

### **Direction issued to and Southern Electric Gas Limited (company number 02716495, the "Licensee") by the Gas and Electricity Markets Authority – Treatment of adjustments for payment methods**

1. This Direction is issued by the Gas and Electricity Markets Authority (the "**Authority**") pursuant to paragraph 24 of Standard Licence Condition ("**SLC**") 31D of the gas supply licence granted under section 7A(1) of the Gas Act 1986 (the "**Licence**").
2. Capitalised terms used in this Direction which are not defined in this Direction shall have the meaning given to them in the Licence.
3. In this Direction the "**EquiPower and EquiGas Tariffs**" mean the Licensee's zero standing charge Tariffs of the same name which constitute Evergreen Supply Contracts and which are aimed at low energy users.
4. Paragraph 24 of SLC 31D provides that the Authority may issue directions relieving the Licensee of its obligations to comply with SLC 31D to such extent and subject to such conditions as the Authority may direct.
5. The considerations taken into account in, and the reasons for, the Authority's decision are set out in the accompanying letter to the Licensee dated 14 December 2015.
6. The Authority hereby directs, pursuant to paragraph 24 of SLC 31D, that the Licensee is, on an enduring basis and subject to the Licensee's continuing compliance with the condition in paragraph 7 of this Direction, relieved of certain of its obligations under paragraph 4 of SLC 31D such that the amended drafting for White Label Tariffs in sub-paras (b) and (c) of condition 22B.7A does not apply to the EquiPower and EquiGas Tariffs. Therefore the EquiPower and EquiGas Tariffs may maintain their zero payment method differential, whilst allowing subsequent future tariffs to have a difference in the Charges for Supply of Gas as between payment methods as described further in the accompanying letter to the Licensee dated 14 December 2015.
7. The Licensee is required to report any change of circumstances relevant to this Direction to the Authority in writing.
8. This Direction shall take immediate effect on and from the date of this Direction, and shall remain in effect on an enduring basis, unless revoked or varied in writing by the Authority.

Dated: 14 December 2015

**Neil Barnes**  
**Associate Partner, Retail Markets**

Signed on behalf of the Authority and authorised for that purpose.