

Reviewing the Consolidated Segmental Statements

12 August 2020

Introduction

Energy UK is the trade association for the energy industry with over 100 members spanning every aspect of the energy sector – from established FTSE 100 companies right through to new, growing suppliers and generators, which now make up over half of our membership.

We represent the diverse nature of the UK's energy industry with our members delivering almost all (90%) of both the UK's power generation and energy supply for over 27 million UK homes as well as businesses. The energy industry invests over £13.1bn annually, delivers around £85.6bn in economic activity through its supply chain and interaction with other sectors, and supports over 764,000 jobs in every corner of the country.

This is a high-level response to Ofgem's consultation reviewing the Consolidated Segmental Statements. We would be happy to discuss any of the points made in further detail with Ofgem or any other interested party if this is considered to be beneficial.

Executive Summary

Energy UK fully supports Ofgem's aim of ensuring that it retains a mechanism to provide transparency and market intelligence on the sectors that it regulates. However, we do not believe that Ofgem's proposed reformed Consolidated Segmental Statements (CSS) will be the most suitable vehicle to achieve this aim, and the granularity in data that it is seeking to collect goes far beyond what is currently collected by suppliers. If the proposed changes go ahead, then suppliers will need to undertake burdensome systems changes to accommodate the data collection required at a time when the sector, and the UK economy as a whole, is recovering from the immediate COVID-19 emergency and longer-term economic impacts.

Ofgem's proposals for additional information to be included in the CSS also appear to go beyond Ofgem statutory powers in places. For example, the request to include granular financial data on unregulated activities. We are also concerned about Ofgem's overall approach to industry engagement on the review of CSS, including significant policy questions being asked outside of formal consultations, limiting stakeholders' ability to scrutinise proposals in full.

Energy UK and our members would welcome further engagement with Ofgem to allow greater feedback on the data metrics that will be required through any reformed CSS and the overall policy approach. We are concerned that to date Ofgem has not been clear enough with suppliers on the exact aim it is seeking to achieve, so full and robust feedback on individual data items may not be possible at this time. It will also be important to ensure that there is no unnecessary duplication or overlap with other reporting requirements already in place or being progressed elsewhere, such as the Supplier Licensing Review.

In this response we have outlined an alternative approach, utilising a streamlined RFI for key metrics that we believe would place less unnecessary burden upon suppliers, while still providing Ofgem with

market monitoring and transparency. A commitment for further engagement with suppliers to explore this approach, and the exact data items that would be proportionate, would be welcome.

Alternative Approach for Efficient Market Monitoring

Energy UK has overall concerns with the granularity and complexity of data that Ofgem is currently proposing to require suppliers to submit on an annual basis, many of which do not align with how suppliers currently capture data. This could lead to significant systems changes being required, leading to undue burdens being placed on suppliers at a time when a number of other market reforms are ongoing, requiring significant resources. We believe that data requests have to be targeted and proportionate, and the proposals being consulted upon do not currently meet these criteria.

Energy UK is, therefore, proposing that Ofgem adopts an alternative mechanism to achieve its aims, whilst reducing unnecessary burden being placed on suppliers. We believe that Ofgem should develop a more streamlined and standardised financial reporting RFI that will enable the collection of the most relevant information in the most efficient manner. With a streamlined RFI, collecting only the fundamental data required to provide sufficient market insight, all suppliers will be able to provide responses in a reasonable timeframe and without unnecessary, and wide-spread systems changes. Any trends identified from this base of information could then be investigated further by Ofgem on a supplier-by-supplier basis in line with proposals being progressed through the Supplier Licensing Review. A greater frequency could also allow Ofgem a closer to real time view of the market and any emerging trends in key areas. This greater frequency will be possible as the data being sought will be more proportionate than that being proposed by Ofgem in this consultation.

We understand that Ofgem will intend to use CSS submissions for supporting work such as its annual review of Conditions for Effective Competition. As part of the streamlining aspect of our proposal, we would suggest decoupling ongoing market monitoring (through the RFI) from the wider data that Ofgem may need to complete that work. We note that the first assessment of Conditions for Effective Competition will have been completed without this granularity of information. This decoupling would allow Ofgem to aggregate the key financial information on an annual basis. If it is required, and developed to be proportional to its justified usage, Ofgem could set out an additional annual request for key information needed to complete the Conditions for Effective Competition review.

We would urge Ofgem to continue engagement with industry through workshops focussed on identifying the base data required to meet its aim of market monitoring, built upon the data that suppliers already collect as far as possible, and using the existing CSS template as a foundation. In doing so, it may be prudent to focus on high-level metrics, as the more granular the data becomes the greater the difference in ways individual suppliers would measure that data, which could impact upon the quality of submissions and Ofgem's ability to compare effectively.

It will be important to ensure that any data required under the CSS (including through our alternative approach) is consistent with current reporting requirements and those being developed through the Supplier Licensing Review to avoid any unnecessary duplication or contradiction, and subsequent costs to suppliers and their customers.

The assumption with our proposal is that it would remove the need for any ongoing specific COVID-19 RFI to avoid unnecessary duplication in financial reporting. Lessons should also be learned from both versions of the COVID-19 financial RFI and the need to target the information to specific areas of concern, and Ofgem should ensure that data collected would give an accurate picture of the market that it targets. For example, Ofgem should ensure that any data requests for non-domestic suppliers are appropriate and relevant to the practices of non-domestic suppliers.

Below we have compared the alternative proposal against the key standards that Ofgem outlined in the consultation for a reformed CSS requirement:

Representative – captures the overall market and reflects the market structure and its dynamics

The streamlined RFI mechanism can capture as much of the market as Ofgem's proposals if a similar threshold is set as currently proposed.

However, Ofgem should consider a whole-market approach to the streamlined RFI, covering all suppliers submitting a key set of data that is proportionate to its intended use. Financial monitoring of this key set of proportionate data should be a "one size fits all" regardless of supplier size, which is consistent with both versions of the COVID-19 RFI, allowing Ofgem to capture the overall market in a clearer way than proposed. The simplified standardised reporting would give Ofgem easier access to the information currently filed under Statutory Accounts, which are not user friendly to gather monitoring data on all active licensed suppliers.

If there is sufficient justification, the level of granularity in the RFI could be staggered based upon a supplier's market share or customer numbers, or asked as a targeted response to trends or a specific for concern through measures already proposed in the Supplier Licensing Review package of reforms such as a dynamic assessment or independent audit (where proportionate to the significance of the concern). However, it will be key to ensure that this granularity is proportionate and justified by a clearly defined use, based upon data already collected by suppliers in practice, and does not pose a material burden on suppliers' systems or costs as they grow in size.

Robust – provides confidence that the reported figures are derived correctly

Using lessons learnt from the recent COVID-19 RFIs, it will be important to ensure that the data definitions in the RFI are tightly defined so that all suppliers are submitting data consistently. We believe that this can be easily achieved through a streamlined RFI that is based upon the data already collected by suppliers and aligning submissions with individual company year ends, when suppliers do a robust close of their accounts.

Ofgem's current proposals ask for levels of data granularity that suppliers do not currently collect. This will require supplier system development in order to capture this data, which opens up the risk of figures not being derived correctly from the outset and will require rigorous testing regimes. Any changes to requirements will need to have sufficient lead-in time phase in any new data requests to ensure that the data is captured appropriately.

Consistent – provides consistency in figures to enable aggregation and comparison

As above, the streamlined RFI will provide better consistency than current proposals if it is based upon data that suppliers currently collect with high-level metrics. Supplier allocate costs differently, so a broader metric would allow suppliers to include all the costs they deem as part of the business. While the exact make up of these costs would differ, it would give Ofgem a more consistent view of suppliers' cost bases.

The more regular and consistent data submissions can be aggregated and compared accordingly. The streamlined RFI will also allow Ofgem to aggregate submissions over a period of time to spot trends in shorter time periods, and act if necessary, to prevent consumer detriment.

Useful – provides information that is relevant, meaningful and timely

Our alternative proposal will enable Ofgem to collect relevant and meaningful data on a timelier basis than its current proposals. This will ensure that Ofgem can effectively monitor the market it regulates, spotting trends closer to real time than an annual, complex submission would allow.

Accessible – presented in a way that can be understood by interested parties

Data that is not commercially sensitive, or which could distort competition, could just as easily be presented in accessible ways as Ofgem's current proposals. There would be difficulties in making Ofgem's current proposals accessible or made public as it would contain commercially sensitive data

and information that would not tie back to suppliers' financial accounts, giving interested parties a confusing picture of the state of the market.

Pragmatic– requests information that already exists within firms, as far as possible

Ofgem's current proposals go far beyond requesting data that already exists within firms. There is a fundamental disconnect between Ofgem's view of how suppliers operate, and how they operate in practice. A streamlined RFI focusing on key financial market intelligence metrics would be a more pragmatic approach, whilst still providing all the benefits outlined above.

As we have seen from the recent COVID-19 RFIs, not all suppliers collect data in the same way so there will always likely be a need for some suppliers to change data collection or systems to accommodate a new reporting requirement. This should, however, be minimised as far as possible, and the RFI we are proposing could achieve this with minimal disruption to the wider market.

Proportionate – balances volume of information and market coverage.

Energy UK believes that Ofgem should seek to collect key information from all suppliers operating in the market. However, this baseline data requirement must be proportionate and have a clearly justified use and must not be a duplication of data that is already being provided via other information requests or available within the public domain.

With a staggered approach, Ofgem could ensure that it captures the key metrics of the whole market, whilst also seeking a higher level of granularity of information from suppliers as they grow in market share. In doing so, Ofgem would only publicly report on the baseline data received, so as to not distort the market by publishing data collected from just the larger suppliers.

Our members would welcome the opportunity to work in partnership with Ofgem to develop this alternative proposal to ensure that it effectively achieves Ofgem's aims while better suiting market conditions.

Response to Initial Proposals

Energy UK has provided feedback below on the key aspects of Ofgem's initial proposals. We believe that this feedback would be applicable to both Ofgem's proposals and our alternative proposal outlined above.

1. Scope

Energy UK does not agree with Ofgem's rationale for maintaining the requirement for vertically integrated suppliers also submitting data on their generation arm. We do not believe that it would be a proportionate approach, and would not provide the continuity that Ofgem is seeking.

Energy UK would urge Ofgem to pursue a supplier-only requirement through the supply licence, and if it deems it appropriate to capture data from generators then it should also pursue a specific condition for the generation licence. This would ensure that Ofgem is directly comparing supply activities with supply activities, and generation activities with generation activities in a clear and consistent manner.

2. Threshold

Energy UK understands Ofgem's need for reliable data across the market, and supports the underlying aim of expanding the scope of the requirement. However, we believe that only including suppliers at the 50,000-customer threshold will only make a marginal difference to its monitoring ability. For example, we note that a significant number of suppliers that have failed had not breached the 50,000-customer threshold.

As outlined in our alternative proposal above, we believe that Ofgem could better achieve its aim by capturing all suppliers in the requirement for submitting a streamlined set of key financial metrics, but

consider increasing some granularity of data as suppliers grow in size. However, any additional granularity over and above the base requirements for all suppliers would need to be proportionate, based upon data already collected by suppliers, and have a clearly defined and justified purpose. Any additional requests for data will also need to be phased in to allow suppliers sufficient timescales to collect the data and amend systems.

In moving forward, we would also urge Ofgem to ensure that there is clarity in any threshold requirement that is included, setting out clearly whether it is all accounts, all meter points, or based on only electricity or gas meters. It should also ensure that any threshold also properly accounts for how the non-domestic market works in practice, noting that single non-domestic customers could have a number of meter points.

3. Annual Audit

Energy UK fully supports the removal of the annual audit requirement and welcomes this proposal from Ofgem.

However, we would welcome clarity on the process that will be followed by Ofgem to impose an audit onto a supplier. Given the substantial cost that would be incurred by suppliers having to undergo an audit, we believe that there should be a robust process in place that requires senior-level sign-off from within Ofgem to impose the requirement on an individual supplier.

4. Additional Financial Information

Energy UK's members are best placed to provide detailed feedback on the specific financial data metrics being proposed by Ofgem, and the impacts they would have upon their systems and costs.

However, while we agree that Ofgem needs to have market-monitoring data to best regulate, it must be proportionate with a robust justification and clearly defined use case. We do not agree that Ofgem has proven that the additional financial data is needed in the policy consultation. Any additional data requested of suppliers will have a cost implication and so needs to be kept to only what is required to meet the overall aim of market monitoring and transparency.

At a high level, we believe that there is currently a disconnect between Ofgem's assumption of the data suppliers currently collect, and the granularity data that suppliers currently collect in practice. This will lead to significant impacts upon suppliers if this level of data granularity is progressed, which has not been sufficiently reflected in Ofgem's Impact Assessment. For example, there is little consistency in how suppliers split their non-domestic customers between microbusiness, SME and I&C customers, and nor would they necessarily have specific cost allocations for particular types of business customers such as not-for-profits. The introduction of any specific definitions to support standardised reporting would not reflect what suppliers and customers see, it would increase costs and not provide an accurate view of the market, leading to potentially incorrect and confusing assumptions about the energy market.

We believe that Ofgem also needs to provide greater clarity on its justification for collecting the granularity of data that it ultimately does. Data collected needs to have a clear rationale and use, rather than just being used as a data-collecting exercise by itself.

Some aspects of the proposed additional financial information appear to primarily be for the purpose of completing the annual Conditions for Effective Competition review. As outlined in our alternative proposal above, we believe that these metrics should be decoupled from a streamlined financial monitoring request to reduce the unnecessary burden on suppliers and distinguish between separate rationales. This will also better reflect that the Conditions for Effective Competition review will no longer be required after 2022, as the price cap has been legislated to finish no later than the end of 2023.

We also question the suitability of seeking data on "other revenue", as these will be dependent upon how suppliers' businesses are structured. For example, if all activities are undertaken in one company then these would be reported, whereas under some company structures this data would not have to be

collected. This creates undue burden on some suppliers based on the structure of their business and inconsistencies in the data gathered and analysed by Ofgem, undermining its usefulness as a metric.

5. Reporting Year

Energy UK is concerned that suppliers risk facing substantial additional costs if the proposed level of granularity goes ahead, and where Ofgem's proposed year-end is different to a supplier's end of financial year. We do not believe that aligning the CSS (or alternative approach) with suppliers' end of financial years would affect Ofgem's ability to make comparisons. Energy UK members are best placed to provide specific details, but it has been highlighted that Ofgem's Impact Assessment has omitted a number of key costs that suppliers would face if the reporting year is changed.

6. Implementation and Transition

While the exact length of any implementation period is dependent upon the ultimate decision by Ofgem, it is clear that Ofgem's proposals will need a long lead time to enable systems development and testing to ensure data quality. Given the change in reporting requirements proposed, even currently obligated suppliers would need to change systems accordingly, and then begin to collect the data required for the proposed annual submission. It will not be an easy transition for any supplier and this should not be underestimated. Of particular concern is that these systems changes will be required alongside other ongoing changes, such as the Faster Switching Programme and other regulatory reforms.

Energy UK's alternative proposal for a streamlined RFI mechanism would be an easier transition, if based upon the COVID-19 RFI and utilising lessons learned, but it would still require some system changes by suppliers so it could not be a seamless transition.

We would welcome clarity as to the expectations of the requirements of suppliers' currently obligated to submit their CSS, and whether they would be required to submit two separate and different submissions within the same year based on Ofgem's proposed timeline.

Energy UK and our members would urge Ofgem's continued engagement with suppliers on the details of its proposals, their impacts on suppliers' systems, and the required changes for any proposals. This will ensure that any implementation period is realistic in its length, and the data required is proportionate for its use.

If you would like to discuss the above or any other related matters, please contact me directly on 020 7747 2931 or at steve.kirkwood@energy-uk.org.uk.