

Final Proposals and Statutory Consultation Reviewing the Consolidated Segmental Statement Energy UK response

11th August 2021

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 over 80% of both the UK's power generation and energy supply for the 28 million UK homes as well as businesses. The energy industry invests £13bn annually, delivers £31bn in gross value added on top of the £95bn in economic activity through its supply chain and interaction with other sectors, and supports 738,000 jobs in every corner of the country.

This is a high-level response to Ofgem's Final Proposals and Statutory Consultation - Reviewing the Consolidated Segmental Statement. 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. We are supportive of Ofgem obtaining greater financial insight from a wider range of suppliers within the market and welcome Ofgem's approach to auditing, and the changes it has made to account for suppliers' financial reporting years and the range of accounting standards.

However, we remain concerned that the granularity of data that Ofgem is seeking goes far beyond what is currently captured by suppliers. If Ofgem proceeds on the basis of its final proposals, 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 still recovering from the Covid-19 pandemic and the longer-term economic impacts.

We believe that Ofgem has still not been clear enough with suppliers on its exact logic for requesting additional data at that level of granularity, including how/why it will be used by Ofgem and exactly how the requested data will better support customers. Nor has Ofgem been explicit with regards to the system changes required to accommodate the granularity requested. We, therefore, urge Ofgem to review its proposals to ensure that it is only collecting data that it requires and that there is no unnecessary duplication or overlap with the other reporting requirements that are already in place or being progressed elsewhere, such as the Supplier Licensing Review.

We explore below in further detail our enduring, overarching concerns with Ofgem's proposals in this space, including the areas where we still feel greater clarity is required from Ofgem.

Data Granularity

As was made evident in our previous response, Energy UK has significant concerns with the granularity and complexity of data that Ofgem is seeking, particularly with regards to the proposed OPEX breakdown and segmentation proposals. The final proposals still ask for levels of data granularity that suppliers do not currently collect, nor do they align with how suppliers currently capture data. 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.

We, therefore, reiterate our belief that there is still a disconnect between Ofgem's assumption of the data suppliers currently collect, and the granularity of data that suppliers collect in practice. Some Energy UK members have expressed concern that the burden imposed by Ofgem of increasing the granularity of data to the proposed extent and the updated data and financial systems that will be required, may be disproportionately felt by smaller suppliers and new entrants to the CSS. If this excessive level of data granularity is progressed, this could lead to significant and expensive system and reporting changes (including development and testing) being required in order to capture this data, leading to undue burdens being placed on suppliers of all sizes across the market at a time when a number of other market reforms are ongoing, requiring significant resources.

Comparability

We remain concerned that a number of data items will require suppliers to make assumptions on costs to be included. Different suppliers will invariably make different assumptions. We are, therefore, concerned that this will undermine the comparability of that data and the usefulness of its collection.

Confidentiality

Energy UK remains concerned by and disappointed with Ofgem's ambition to publish suppliers' financial data within the public domain. We do not feel that Ofgem has fully addressed the collective concerns raised by stakeholders to its initial proposals.

To build on this, we are greatly concerned that Ofgem has not adequately considered the impacts to competition and to a supplier's investment status by making the information it is requesting public. We note that Ofgem has not provided transparency of its considerations in this space part of an impact assessment. Without examining the output, we, therefore, question how suppliers can have confidence that Ofgem has fully considered the implications of its proposals. Additionally, within Ofgem's updated guidance, it is seeking for suppliers to provide a description of their hedging strategy, with no indication that this information will remain confidential. Energy UK strongly objects to this information being made public. If Ofgem is to proceed with its proposals, this will likely mean that all suppliers will make confidentiality requests at the time of submission, which will be more burdensome for Ofgem to manage rather than address suppliers' concerns around confidentiality in these proposals.

We, therefore, urge Ofgem to provide greater clarity on its logic and justification behind these proposals, detailing the exact tangible benefits it envisages from the publication of this data.

Further Comments

Below, Energy UK has also provided feedback on the key aspects of Ofgem's final proposals, many of which feed into our overarching concerns.

1. Scope – Supply & Generation Activities

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, continues to 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. Scope - Customer Number Threshold

Energy UK supports Ofgem's final proposal to have separate thresholds for domestic and non-domestic customers, measured in meter points. We would welcome Ofgem's commitment to periodical reviews of the threshold levels, to ensure these remain appropriate for both the domestic and non-domestic markets. We also believe that this would be a good opportunity to potentially align the customer threshold to BEIS' plans for the WHD and extend to all suppliers with over one thousand domestic customers.

However, we are concerned that its proposal to have a variable non-domestic threshold will introduce a level of complexity and uncertainty that will create unnecessary difficulties for non-domestic suppliers. It is not clear that non-domestic suppliers will get sufficient notice ahead of becoming obligated by a changing threshold, potentially becoming obligated for reporting requirements that it has not had time to adequately prepare for in its systems and processes. We believe that a fixed, non-variable threshold for non-domestic suppliers would be more suitable, and will provide non-domestic suppliers with certainty around their reporting obligations each year.

3. Annual Audit

As stated in our previous response, Energy UK fully supports the removal of the annual audit requirement and welcomes this as Ofgem's final proposal.

We do, however, believe that it would be beneficial for suppliers if Ofgem were to prepare a framework or an overview to indicate where an audit would be requested if it deems a CSS submission to not have been prepared in accordance with the licence conditions, revised guidelines and/or revised templates. For example, we would welcome clarity as to whether Ofgem would issue a supplier with a warning and provide an opportunity to rectify the issue first, prior to requesting that a full audit be undertaken.

4. Additional Financial Information Requirements

Energy UK remains unsupportive of a number of Ofgem's final proposals. We feel strongly that many of the proposals do not meet Ofgem's own stated aims to ensure the information provided within the CSS is: Robust, Consistent, Useful, Accessible, Pragmatic and Proportionate. We would restate our overarching concerns regarding the level of data granularity requested and note that Ofgem's proposals for additional information to be included in the CSS go far beyond what is currently captured by suppliers, as well as above what is currently required by other regulators. To reiterate, 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. As they stand, Ofgem's proposals are expected to have a significant adverse impact on suppliers, at a time when many are still recovering from the effects of the Covid-19 pandemic and other resource-heavy industry change programmes are continuing.

In addition, the data granularity and limited definitions will require suppliers to make assumptions in the data they report under various categories. These assumptions will limit the comparability of the data for Ofgem, undermining any benefits of their collection.

With regards to microbusiness breakdown, there is little consistency in how suppliers split their non-domestic customers between microbusiness, SME and I&C customers, and Ofgem does not currently take into account this variability. We propose that Ofgem should, for the purposes of reporting, define a microbusiness as the full licence definition of microbusiness, plus those customers that a supplier has deemed to be a microbusiness. To build on this, we would like to make clear the difficulties of not including the 'deemed' approach – specifically, that rigidly applying the microbusiness definition would mean an entirely new process for many suppliers and the effort required should also not be

underestimated. For instance, information to determine a customer's size (FTE and turnover) can only be sourced directly from each customer. We think Ofgem could achieve its aims in this area by breaking non-domestic information down to just two categories: microbusinesses (using the adjusted definition) and non-microbusinesses. This approach still allows Ofgem to assess the microbusiness segment, but has the benefit of avoiding suppliers taking a new and potentially arbitrary approach to defining their SME & I&C segments.

On the final proposals around separating out indirect operational costs, Ofgem has not clearly articulated its logic behind this separation and categorisation; nor has Ofgem specified how it intends to make use of these categories, which suppliers do not currently use themselves. For example, the vague definition of innovation will again lead to suppliers making assumptions which will inevitably lead to incomparable data being received by Ofgem across the market.

Further to this, Ofgem has not been clear about the purpose of separating out costs to serve domestic PSR customers. Given that the PSR does not capture financial vulnerabilities, we do not think that Ofgem should use it as a proxy measure of vulnerability in general across suppliers' customer bases, and nor can it be used to make any conclusions about customers in vulnerable circumstances. In addition, we do not believe that it would be useful for Ofgem's stated intention - being on the PSR is an attribute of a customer that is constantly changing, not a customer type in itself that generally remains static. As such, there appears to have been very little consideration to the structure of these proposals around PSR, which will lead to a varying ways of cost allocation.

In addition, it is not clearly defined what constitutes a cost-to-serve PSR customer, and there is a significant range of needs of different vulnerabilities captured on the PSR. It is unclear what benefits Ofgem envisages from seeking to collect this data from suppliers.

We would also argue that the proposal for suppliers to include a high-level summary balance sheet goes above and beyond what is required for Ofgem's purposes. Whilst we do not have any major objections to this proposal, we would welcome insight from Ofgem on the arising tangible benefits it envisages from the inclusion of a high-level balance sheet.

5. Transition Period

Given the proposed level of change, we do not believe a 6-month transitional period affords suppliers enough time to make the relevant changes. The proposed changes will require suppliers to re-analyse past years' data, which is significant considering that most reporting changes take place for future reporting periods. The proposed 6-month timeline also overlaps with other considerable regulatory reform already in or nearing implementation phase, such as, Faster Switching, Market-wide Half Hourly Settlement and the potential changes emitting from the Microbusiness review. There is a limit on how much change suppliers can make to their systems and processes at any one time without risking timely delivery of compliant solutions. Due to the level of uncertainty that remains with these proposals we would, therefore, request that implementation is pushed back until the 2022 CSS.

If you would like to discuss the above or any other related matters, please contact me directly at paige.truelove@energy-uk.org.uk.