Appendix 2.2: Industry background

Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>1</td>
</tr>
<tr>
<td>Evolution of major market participants</td>
<td>1</td>
</tr>
<tr>
<td>The Six Large Energy Firms</td>
<td>3</td>
</tr>
<tr>
<td>Gas producers other than Centrica</td>
<td>35</td>
</tr>
<tr>
<td>Mid-tier independent generator company profiles</td>
<td>35</td>
</tr>
<tr>
<td>The mid-tier energy suppliers</td>
<td>40</td>
</tr>
</tbody>
</table>

Introduction

1. This appendix contains information about the following participants in the energy market in Great Britain (GB):

   (a) The Six Large Energy Firms – Centrica, EDF Energy, E.ON, RWE, Scottish Power (Iberdrola), and SSE.

   (b) The mid-tier electricity generators – Drax, ENGIE (formerly GDF Suez), Intergen and ESB International.

   (c) The mid-tier energy suppliers – Co-operative (Co-op) Energy, First Utility, Ovo Energy and Utility Warehouse.

Evolution of major market participants

2. Below is a chart showing the development of retail supply businesses of the Six Large Energy Firms:
Figure 1: Development of the UK retail supply businesses of the Six Large Energy Firms

Source: CMA research, Six Large Energy Firms.
The Six Large Energy Firms

3. This section of the appendix contains brief overviews of the Six Large Energy Firms: Centrica, EDF Energy, E.ON, RWE, Scottish Power (Iberdrola), and SSE.

Centrica

4. Below is a brief overview of Centrica plc (Centrica). It is set out as follows:

(a) The creation of Centrica.

(b) Corporate activity since 1997.

(c) Current divisional structure.

(d) Group financial performance and recent announcements.

(e) Businesses included in Ofgem’s Consolidated Segmental Statements (CSS).

The creation of Centrica

5. Figure 2 below shows the evolution of British Gas Corporation, through privatisation and various demergers into three companies: Centrica, National Grid and BG Group.
6. Centrica and National Grid\(^1\) (formerly National Grid Transco) are currently FTSE 100 quoted businesses. BG Group\(^2\) was a FTSE 100 quoted business

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\(^1\) National Grid was created by the merger of Lattice (which was demerged from BG plc, and which owned the gas transmission infrastructure in GB) with National Grid (which owned the electricity transmission infrastructure in England and Wales). As a result of this merger, National Grid became active in both the gas and electricity transmission network in GB. It also owns some gas distribution networks in the UK and has acquired electricity transmission assets in the USA.

\(^2\) BG Group (originally BG plc) was also created from the 1997 British Gas plc demerger. In 1999 it undertook a further demerger, separating its gas transmission infrastructure assets (which became Lattice) from its
until early 2016 when it became part of Royal Dutch Shell. Centrica’s background is as follows.

7. Centrica was created from the 1997 demerger of British Gas plc into BG plc and Centrica. This demerger created two different businesses. Centrica assumed the UK retail operations (including the British Gas retail brand in GB) as well as the Morecombe gas fields (UK upstream gas assets which it could use to service its customer base). We discuss Centrica’s corporate development since this demerger and its current structure in the sections that follow.

8. Following the demerger, Centrica developed and acquired a number of different businesses, for example the Goldfish credit card, the AA and telecommunications business OneTel. As well as diversifying away from energy, it also made some acquisitions in this period which form the basis for some of its current divisional structure, for example Rough gas storage and Direct Energy in North America.

9. From about 2006, Centrica made numerous and significant investments in upstream oil and gas assets in the UK, Norway and Canada. As a result of these acquisitions, Centrica’s global oil and gas division expanded its reserves and production significantly.

10. From 2006, Centrica also made a number of bolt-on acquisitions to its Direct Energy business in North America, which grew in importance to the group. Other notable acquisitions were a 20% stake in British Energy, which operates eight nuclear plants in GB, as well as further gas storage assets and the acquisition of Bord Gais Energy in the Republic of Ireland.

Current divisional structure and financial performance

11. Prior to 2016 Centrica had five divisions which all detail below is based upon. We discuss the principal activities and show the relative importance of the different businesses within each division below. For comparability purposes, it is most useful to view the contributions of each business to profitability on a post-tax basis. This is because the Centrica Energy division has a large oil and gas E&P business and therefore pays a very high rate of tax relative to

international oil and gas exploration and production (E&P) assets (which became BG Group). BG was highly successful in oil and gas exploration, mostly outside the UK, with significant interests in Australia, Trinidad and Tobago and the USA. It was also a large producer of liquefied natural gas (LNG). In early 2016 it became part of Royal Dutch Shell.

EDF Energy owns a majority 80% stake.
Centrica’s other divisions (it paid tax\(^4\) at a rate of 71% of earnings before interest and tax (EBIT) in 2015).

12. British Gas is Centrica’s energy supply business in the UK. It supplies gas and electricity to 9 million homes and over 730,000 businesses. This division also offered a range of energy related residential services, for example boiler installation. The contribution of each of these activities to divisional profits after tax is shown below in Table 1.

**Table 1: British Gas division, split of profit after taxation in 2015**

<table>
<thead>
<tr>
<th>Service</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Residential Energy Supply</td>
<td>461</td>
</tr>
<tr>
<td>Residential Services</td>
<td>207</td>
</tr>
<tr>
<td>Business Supply and Services</td>
<td>−22</td>
</tr>
</tbody>
</table>

Source: Centrica. The loss in Business Supply predominately relates to the implementation of a new billing and CRM system.

13. Direct Energy is a North American energy supply business that Centrica has built up through a series of acquisitions since 2000. It supplies gas and electricity to homes and businesses in a number of states and provinces, most notably Texas. Following its acquisition of Clockwork in 2010, it is now the largest home services (eg air conditioning) provider in North America. It provides these services in all US states and Canadian provinces.

14. Centrica Energy includes international oil and gas E&P, UK power generation and trading. The contribution of each of these activities to divisional profits after tax in 2015 is shown below in Figure 3.

\(^4\) For example, before the recent changes to the upstream tax regime, the marginal tax rate for oil and gas extracted in the UK was 81% on income from fields paying Petroleum Revenue Tax (PRT), 30% on production income from qualifying new fields if that income is wholly covered by field allowance, and 62% otherwise. PRT applied to UK fields consented before March 1993.
15. International oil and gas E&P is a leading oil and gas producer in the UK as well as owning a significant and growing international portfolio, including in Trinidad, Canada, the Netherlands and Norway. This business has grown rapidly through acquisition in the last decade.

16. UK power generation owns a fleet of six gas-fired power plants (CCGT), offshore wind projects as well as a 20% stake in EDF Energy’s eight nuclear power stations in the UK (formerly owned by British Energy). It decided not to participate with EDF in new build nuclear plants in the UK in 2013. In 2014, it announced the decision to put its three largest CCGT power stations up for sale (with a net book value of around £500 million). In 2015, it made the decision to retain ownership following a sales process after receiving bids significantly below internal valuation. Centrica’s UK Energy Supply fuel mix for the year to 31 March 2015 is shown below in Figure 4.
Figure 4: Centrica UK Energy Supply fuel mix (year to March 2015)

17. Centrica Storage is legally, financially and physically separated from all other Centrica businesses. Its assets include Rough gas storage, situated in the Southern North Sea, 18 miles of the coast of East Yorkshire, which stores gas on behalf of utilities, gas traders and gas producers, before processing it at its Easington terminal for onward distribution via the National Transmission System.

18. Bord Gais has been treated as a separate division since its acquisition in 2014.

19. In 2016 fundamental changes were announced to the way Centrica will be organised, establishing a single group of international businesses and creating 11 business units (North America Home, North America Business, UK Home, UK Business, Ireland, Exploration & Production, Nuclear, Centrica Storage, Distributed Energy & Power, Connected Home and Energy Marketing and Trading). Centrica will report in line with the new reporting segments for the first time at the 2016 interim results.

20. Table 2 below summarises the importance of each division described above to Centrica’s group profitability after tax in 2014 and 2015.

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5 The separation arrangements were agreed in the Undertakings given by Centrica in 2003 and most recently revised in April 2016. Centrica’s commercial gas storage team is separated from parts of Centrica that deal in gas supply, gas shipping, trading and storage procurement. A Code of Conduct prohibits the disclosure of commercially sensitive information by Centrica Storage to other parts of Centrica. Centrica (2012), Storage Code of Conduct.
Table 2: Contribution of divisions to Centrica’s group profitability in 2014 and 2015

<table>
<thead>
<tr>
<th>Division</th>
<th>Operating profit after tax £m</th>
<th>%</th>
<th>£m</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>British Gas</td>
<td>647</td>
<td>55</td>
<td>650</td>
<td>63</td>
</tr>
<tr>
<td>Centrica Energy</td>
<td>401</td>
<td>34</td>
<td>140</td>
<td>14</td>
</tr>
<tr>
<td>Direct Energy</td>
<td>99</td>
<td>9</td>
<td>187</td>
<td>18</td>
</tr>
<tr>
<td>Bord Gais</td>
<td>3</td>
<td>-</td>
<td>24</td>
<td>2</td>
</tr>
<tr>
<td>Centrica Storage</td>
<td>21</td>
<td>2</td>
<td>25</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,171</strong></td>
<td><strong>100</strong></td>
<td><strong>1,026</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Centrica.2015 accounts.
Note: Operating profit after tax is stated before exceptional items.

21. It can be seen from Table 2 that Centrica’s energy supply business, British Gas, contributes just over half of group profit after tax. The most relevant businesses for our investigation are British Gas, in particular the Residential Energy Supply sub-division, as well as the UK power generation business in Centrica Energy.

Group financial performance and recent announcements

Group financial performance

22. Table 3 below shows Centrica’s summary group performance from 2009 to 2015.

Table 3: Summary of Centrica’s group performance from 2009 to 2015

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>22</td>
<td>22.4</td>
<td>22.8</td>
<td>23.9</td>
<td>26.6</td>
<td>29.4</td>
<td>28.0</td>
</tr>
<tr>
<td>Adjusted EBIT, pre-exceptional</td>
<td>1.9</td>
<td>2.4</td>
<td>2.4</td>
<td>2.7</td>
<td>2.7</td>
<td>1.7</td>
<td>1.5</td>
</tr>
<tr>
<td>Exceptional items and certain re-measurements</td>
<td>(0.3)</td>
<td>0.7</td>
<td>(0.8)</td>
<td>(0.1)</td>
<td>(0.4)</td>
<td>(1.9)</td>
<td>(1.7)</td>
</tr>
<tr>
<td>Net income/(loss)</td>
<td>0.8</td>
<td>1.9</td>
<td>0.4</td>
<td>1.2</td>
<td>1</td>
<td>(1.0)</td>
<td>(0.9)</td>
</tr>
<tr>
<td>Net assets</td>
<td>4.3</td>
<td>5.8</td>
<td>5.6</td>
<td>5.9</td>
<td>5.3</td>
<td>3.0</td>
<td>1.3</td>
</tr>
<tr>
<td>Net debt</td>
<td>3.1</td>
<td>3.02</td>
<td>3.1</td>
<td>3.9</td>
<td>5</td>
<td>5.2</td>
<td>4.7</td>
</tr>
<tr>
<td>EPS*</td>
<td>21.3p</td>
<td>24.4p</td>
<td>25.1p</td>
<td>26.6p</td>
<td>26.6p</td>
<td>18.0p</td>
<td>17.2p</td>
</tr>
<tr>
<td>DPS†</td>
<td>12.8p</td>
<td>14.3p</td>
<td>15.4p</td>
<td>16.4p</td>
<td>17.0p</td>
<td>13.5p</td>
<td>12.0p</td>
</tr>
</tbody>
</table>

Source: Centrica accounts.
*Earnings per share, stated pre-exceptional items.
†Dividend per share.

23. From Table 3, we note that between 2009 and 2015:

(a) Centrica has increased its exposure to oil and gas exploration and production (via Centrica Energy). It has done this via numerous oil and gas acquisitions in the UK and overseas;

(b) Centrica has increased its exposure to North American energy supply and services, again mainly via a series of acquisitions;
(c) as a result of (a) and (b), Centrica group’s relative exposure to UK electricity and gas supply and power generation has reduced;

(d) net debt has increased from £3 billion to £4.7 billion over the period, mainly due to acquisitions. Leverage, as measured by net debt: equity, has increased from 72% to 362%; and

(e) exceptional items were relatively large throughout the period and give rise to significant volatility in the net profit attributable to Centrica. These include re-measurements relating to certain energy contracts as well as a number of significant asset write-downs that have occurred in the period. Table 4 below shows some examples of the asset write-downs between 2010 and 2015.

Table 4: Examples of Centrica’s pre-tax asset write-downs and impairments, 2010 to 2015

<table>
<thead>
<tr>
<th>Year</th>
<th>Description</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>Impairment of UK, Dutch, Norwegian and North American oil and gas E&amp;P</td>
<td>1,865</td>
</tr>
<tr>
<td>2015</td>
<td>Impairment of UK power generation assets</td>
<td>121</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of Nuclear investment</td>
<td>372</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of UK, Dutch, Norwegian and North American oil and gas E&amp;P</td>
<td>1,189</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of UK power generation assets</td>
<td>535</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of Nuclear investment</td>
<td>214</td>
</tr>
<tr>
<td>2013</td>
<td>Impairment of UK and North American oil and gas E&amp;P</td>
<td>699</td>
</tr>
<tr>
<td>2013</td>
<td>Impairment of UK Gas Storage assets</td>
<td>240</td>
</tr>
<tr>
<td>2012</td>
<td>Impairment Investment in nuclear new build</td>
<td>231</td>
</tr>
<tr>
<td>2012</td>
<td>Group restructuring</td>
<td>214</td>
</tr>
<tr>
<td>2011</td>
<td>Impairment of UK power generation assets</td>
<td>226</td>
</tr>
<tr>
<td>2011</td>
<td>Group restructuring</td>
<td>154</td>
</tr>
<tr>
<td>2010</td>
<td>Impairment of UK power generation assets</td>
<td>68</td>
</tr>
<tr>
<td>2010</td>
<td>Impairment of UK and North American oil and gas E&amp;P</td>
<td>95</td>
</tr>
</tbody>
</table>

Source: Centrica accounts.

Businesses included in the CSS

24. The CSS were introduced by Ofgem in 2009 and relate to those UK businesses which hold a supply or generation licence.\(^6\) It may be useful to understand which of Centrica’s businesses are included in these statements. They are:

(a) **British Gas** – residential and business supply, together ‘Supply’, are included in the CSS. The Energy Services (eg boiler replacement) part of this division is not included; and

(b) **Centrica Energy** – the UK power generation business (‘Generation’).

---

\(^6\) The aim of the remedy was to provide better visibility/transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
Together, the UK generation and supply businesses covered by the CSS contributed around 52% of Centrica’s group post-tax profit in 2015.

**EDF Energy**

Below is a brief overview of EDF SA (EDF). It is set out as follows:

(a) The history of EDF.

(b) Current divisional structure.

(c) Group financial performance, strategy and recent announcements.

(d) Businesses included in Ofgem’s CSS.

*The history of EDF*

**The group**

EDF was founded in 1946 as a result of the nationalisation of the electricity generation, transmission and distribution industry in France. It remained a vertically integrated monopoly until the electricity sector was first opened up to competition in France in 1999. In November 2004 it became a limited liability company, ahead of a partial stock market floatation in November 2005. The French state is an 84.5% shareholder and EDF also retains a significant number of small private shareholders. In May 2016 it had a market capitalisation of €22.44 billion.

EDF is the number one generator of nuclear power globally. This position can be traced to the rapid roll-out of nuclear power plants in France under the ‘Messmer Plan’ following the oil crisis in 1973, when many of the 58 nuclear plants that EDF owns and operates in France today were constructed.

In France, EDF owns businesses across the entire electricity supply chain that are involved in:

(a) generation, through its ownership of power plants. Most of the electricity generated is through nuclear power;

---

7 On April 8 1946, a law nationalising 1,450 French electricity and gas generation, transmission, and distribution companies was passed. The state-owned industrial and commercial entities created were known under the acronym EPIC (établissement public à caractère industriel et commercial).

8 EDF (2014), Shareholding structure.

9 90.4% of electricity generated by EDF in France was from nuclear power in 2014.
(b) transmission, through its ownership of RTE, the electricity transmission system operator in France. It operates (but does not own) the transmission network. This business is operationally independent, as required by EU legislation;

(c) distribution, through its ownership of ERDF, which operates the distribution network in most of France. This business is operationally independent, as required by EU legislation; and

(d) retail supply of gas and electricity to domestic and business customers.

30. EDF also has a majority stake in a consortium currently developing an LNG terminal at Dunkirk.

31. Since 1992, EDF has expanded internationally. Its main international businesses are in:

(a) the UK, which is discussed below;

(b) Italy, through its ownership of Edison, Fenice and a subsidiary of EDF Energies Nouvelles. Edison is the second largest power producer in Italy, with a strong focus on gas. Italy operates as the centre for EDF’s gas business; and

(c) Benelux, North America, Central and Eastern Europe and China.

(d) EDF Energie Nouvelles, which develops, installs and operates renewable energy facilities internationally.

32. Table 5 below shows the split of EDF’s electricity generation on a group basis in 2015.

<table>
<thead>
<tr>
<th></th>
<th>% Capacity</th>
<th>% Generation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nuclear</td>
<td>54</td>
<td>78</td>
</tr>
<tr>
<td>Coal/fuel oil</td>
<td>15</td>
<td>6</td>
</tr>
<tr>
<td>Hydro</td>
<td>16</td>
<td>7</td>
</tr>
<tr>
<td>CCGT/gas</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td>Other renewables</td>
<td>6</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: EDF Energy.

**EDF Energy – UK business**

33. EDF Energy (EDF UK) is the UK subsidiary of EDF Group. It has around 5.2 million customers and over 14,000 employees. Table 6 below shows the key acquisitions which led to the current business.
Table 6: Key acquisitions leading to creation of EDF Energy’s current UK business

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>November 1998</td>
<td>Acquisition of London Electricity Plc (former London Electricity board) for £[×].</td>
</tr>
<tr>
<td>July 1999</td>
<td>Acquisition of electricity supply business of SWEB plc (former South West electricity Board) for £[×].</td>
</tr>
<tr>
<td>2000-2001</td>
<td>Acquisition of 3 power stations (1 CCGT, 2 coal) at 3 sites (Cottam, West Burton, Sutton Bridge).</td>
</tr>
<tr>
<td>July 2002</td>
<td>Acquisition of SEEBOARD Plc (former South East Electricity Board) for £[×].</td>
</tr>
<tr>
<td>September 2008</td>
<td>Acquisition of 80% of British Energy (which operates 15 nuclear plants at 8 sites in the UK) for £[×].</td>
</tr>
<tr>
<td>July 2010</td>
<td>Sale of UK Electricity Distribution Networks business for €[×] (now called UK Power Networks).</td>
</tr>
</tbody>
</table>

Source: EDF Energy.

34. It can be seen from Table 6 that EDF UK was developed through the acquisition of three of the original England and Wales regional electricity companies (RECs), beginning with London Electricity in November 1998. It then added electricity generation through the initial acquisition of three thermal power plants in 2000/2001 and the subsequent purchase of 80% of British Energy (in which Centrica has a 20% minority stake) in 2009.

35. In 2010, it sold the electricity distribution network assets for London Seaboard and Eastern areas. This sale left EDF Energy in its current form, with interests in supply and generation.

36. Table 7 below shows the split of electricity generation by fuel type for EDF UK in 2015.

Table 7: Split of electricity generation by fuel type for EDF UK in 2015

<table>
<thead>
<tr>
<th>Capacity</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nuclear</td>
<td>62 73</td>
</tr>
<tr>
<td>Coal</td>
<td>28 19</td>
</tr>
<tr>
<td>CCGT and co-generation</td>
<td>9 7</td>
</tr>
<tr>
<td>Other renewables</td>
<td>1 1</td>
</tr>
</tbody>
</table>

Source: EDF Energy.

Current divisional structure and financial performance

37. EDF segments its business on a geographic basis. Table 9 below summarises the performance of the business segments in 2015.

Table 8: Performance of EDF's geographic business segments in 2015

<table>
<thead>
<tr>
<th></th>
<th>France</th>
<th>UK</th>
<th>Italy</th>
<th>Other int'l</th>
<th>Other</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>39.6</td>
<td>11.6</td>
<td>11.6</td>
<td>5.6</td>
<td>6.4</td>
<td>75.0</td>
</tr>
<tr>
<td>EBITDA</td>
<td>11.5</td>
<td>2.2</td>
<td>1.3</td>
<td>0.6</td>
<td>1.9</td>
<td>17.6</td>
</tr>
<tr>
<td>EBIT</td>
<td>4.6</td>
<td>-0.2</td>
<td>-0.81</td>
<td>-0.38</td>
<td>1.0</td>
<td>4.2</td>
</tr>
<tr>
<td>Total assets*</td>
<td>136.9</td>
<td>28.9</td>
<td>10.7</td>
<td>9.8</td>
<td>22.0</td>
<td>278.9</td>
</tr>
</tbody>
</table>

Source: EDF Energy.

*Asset figures breakdown also includes €70 billion of geographically un-allocated assets.
Note: EDF Energy’s underlying operating profits (EBIT) in 2015 was £664 million. The UK figure shown includes a one-off impairment charge of £796 million relating to the reduction in value of gas and coal generation and storage assets.
38. It also provides sales segmentation by activity. This is shown below in Table 9.

Table 9: Segmentation of EDF sales by activity in 2015

<table>
<thead>
<tr>
<th>Segment</th>
<th>€bn</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generation and supply – France</td>
<td>25.0</td>
<td>33</td>
</tr>
<tr>
<td>Generation and supply – RoW*</td>
<td>29.5</td>
<td>40</td>
</tr>
<tr>
<td>Distribution – France</td>
<td>14.6</td>
<td>20</td>
</tr>
<tr>
<td>Distribution – RoW</td>
<td>0.9</td>
<td>1</td>
</tr>
<tr>
<td>Other – RoW</td>
<td>4.6</td>
<td>6</td>
</tr>
<tr>
<td>Total</td>
<td>74.6</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: EDF Energy.
*Rest of World.
Note: The table excludes 'Transmission' in RoW, 'Other' in France and 'Eliminations', which each represent less than 1% of group sales.

39. It can be seen from Tables 8 and 9 that while EDF has significant international exposure (especially in terms of sales), France remains the most important profit centre for EDF, in 2015 it generated 82% of EDF’s positive EBIT.

Group financial performance and recent announcements

Group financial performance

40. Table 10 below shows EDF’s summary group performance over the last seven years.

Table 10: Summary of EDF’s group performance from 2009 to 2015

<table>
<thead>
<tr>
<th>Year</th>
<th>Sales</th>
<th>EBITDA</th>
<th>Net income</th>
<th>Equity</th>
<th>Net debt</th>
<th>EPS*</th>
<th>DPS†</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>66.3</td>
<td>17.5</td>
<td>3.9</td>
<td>28.0</td>
<td>42.5</td>
<td>2.14</td>
<td>1.15</td>
</tr>
<tr>
<td>2010</td>
<td>63.9</td>
<td>16.6</td>
<td>1.0</td>
<td>31.3</td>
<td>34.4</td>
<td>0.55</td>
<td>1.15</td>
</tr>
<tr>
<td>2011</td>
<td>65.3</td>
<td>14.8</td>
<td>3.0</td>
<td>30.6</td>
<td>33.3</td>
<td>1.63</td>
<td>1.15</td>
</tr>
<tr>
<td>2012</td>
<td>72.2</td>
<td>16.0</td>
<td>3.3</td>
<td>30.6</td>
<td>41.6</td>
<td>1.77</td>
<td>1.15</td>
</tr>
<tr>
<td>2013</td>
<td>71.9</td>
<td>16.8</td>
<td>3.5</td>
<td>26.3</td>
<td>33.4</td>
<td>1.84</td>
<td>1.25</td>
</tr>
<tr>
<td>2014</td>
<td>73.3</td>
<td>17.2</td>
<td>3.7</td>
<td>34.2</td>
<td>34.2</td>
<td>1.78</td>
<td>1.25</td>
</tr>
<tr>
<td>2015</td>
<td>75.0</td>
<td>17.6</td>
<td>1.4</td>
<td>35.2</td>
<td>37.4</td>
<td>0.32</td>
<td>1.10</td>
</tr>
</tbody>
</table>

*Earnings per share.
†Dividend per share.
Note: All financials are presented post-exceptional items.

41. From Table 10 we note the following:

(a) Profits have been relatively stable over the period. The significant reduction in net income in 2010 was driven by a number of non-recurring provision increases in Italy and the USA.

(b) Variations in net debt have to a large extent been driven by acquisition and disposal activity as well as high capital investments in its businesses. At the beginning of the period, net debt was at a relatively high level.
following the acquisitions of 80% of British Energy (for €11.1 billion) and 49.99% of Constellation Energy’s nuclear business in the USA (for €3.1 billion). Net debt then fell in 2010 following the disposal of its UK electricity distribution networks business for €6.7 billion and its stake in German electricity provider EnBW for €7.1 billion. The acquisition of Edison for €3.3 billion in 2012 resulted in another short term increase in net debt.

Businesses included in the CSS

42. The CSS were introduced by Ofgem in 2009 and relate to those UK businesses which hold a supply or generation licence.\(^{10}\) Only the UK supply and generation elements of EDF’s businesses are included in these statements. As we do not have a detailed breakdown of the UK business, it is not possible at this stage to say which elements are excluded from these statements (for example, trading and energy services).

E.ON

43. Below is a brief overview of E.ON SE (E.ON). It is set out as follows:

   (a) The history of E.ON group and E.ON UK.

   (b) Current divisional structure.

   (c) Group financial performance, strategy and recent announcements.

   (d) Businesses included in Ofgem’s CSS.

The history of E.ON

The group

44. E.ON is based in Essen and is the result of the merger of two of Germany’s largest industrial conglomerate groups (VEBA and VIAG) in June 2000. VEBA and VIAG were founded in the 1920s to serve as holding companies for German state-owned industrial enterprises. They owned businesses across a large number of sectors, including electricity, chemicals, logistics and real estate.

\(^{10}\) The aim of remedy was to provide better visibility / transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy, to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
45. VEBA and VIAG were privatised and listed on the DAX (the stock index of Germany's top 30 blue chips) in various stages during the 1960s and 1980s, with the government selling its final interest in 1988. Prior to the merger VEBA and VIAG narrowed their focus through a number of divestments. Following the merger, E.ON focused on the energy and chemicals sectors. Later, the focus became energy. During this process of focusing the business VEBA and VIAG (and then E.ON) undertook numerous disposals and acquisitions.

46. Today, E.ON is one of the world’s largest investor-owned energy businesses. It operates in Europe, Russia, and North America with more than 56,000 employees, 33 million customers and around €116 billion in sales.\(^{11}\) It also has joint venture businesses in Brazil and Turkey. Its businesses include renewables, conventional and decentralized power generation, natural gas, energy trading, retail and distribution.

47. Given the ongoing and fundamental changes in the energy markets, the board of management (Vorstand) of E.ON SE decided in late November 2014, with the supervisory board’s approval, to implement a new strategic orientation for the E.ON Group. Under the new strategic orientation, it is intended that the E.ON Group will focus on the Renewables, Energy Networks and Customer Solutions business areas, while retaining its nuclear power business in Germany. For this purpose, the E.ON Group intends, among other things, to combine its other current business areas, conventional generation (including hydro, but excluding the German nuclear energy activities), global energy trading (in particular the distribution of electricity and gas) and power generation in Russia as well as the interest in the Yuzhno Russkoye gas field, into an independent new company, Uniper SE, and to subsequently spin off the majority stake in the Uniper Group to the shareholders of E.ON SE. The approval of E.ON SE’s shareholders for the spin-off was sought at the E.ON SE Annual General Meeting of 8 June 2016.

**E.ON UK**

48. At privatisation, the electricity generation assets of England and Wales,\(^\text{12}\) which had previously been held by the Central Electricity Generation Board (CEGB), were split between three companies:\(^\text{13}\) Powrgen, National Power and Nuclear Electric. Powrgen was formed in 1989 and privatised in two tranches in 1991 and 1995.

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\(^{11}\) 2015.

\(^{12}\) In Scotland, electricity was privatised on a vertically integrated basis.

\(^{13}\) Two pumped storage units were transferred to National Grid.

A2.2-16
49. E.ON acquired Powergen in July 2002 and eventually renamed the business E.ON UK. The business is headquartered in Coventry.

50. A small number of significant acquisitions and disposals have developed the original Powergen electricity generation business into the vertically integrated (by virtue of common ownership) supply and generation businesses of E.ON UK.

51. East Midlands Electricity was the third largest REC. It added 2.3 million customers as well as the electricity distribution network in the region. At the time, Powergen said that that the acquisition would provide a platform to develop a national domestic supply business ahead of the full liberalisation of the electricity market.

52. TXU added a further 5.5 million customers and three coal fired power stations, making Powergen the largest electricity supplier in GB and second largest gas supplier (behind British Gas).

53. Midlands Electricity added an electricity distribution network contiguous to the East Midlands network which had been acquired in 1998. The two electricity distribution network businesses were merged and renamed Central Networks. By the time of this acquisition, distribution network assets had to be operated independently of retail businesses. Central Networks was eventually sold by E.ON as part of a global divestment programme in March 2011.

54. In October 2012, E.ON exited the Horizon nuclear joint venture that had been formed in 2009 with RWE to invest in new nuclear capacity in the UK. Hitachi acquired 100% of Horizon in October 2012.

55. In the UK, the conventional generation business is now under the ownership of Uniper UK Limited.

Current divisional structure and financial performance

56. Following the creation of Uniper, which now operates under its own management team, the E.ON Group now consists of E.ON and Uniper operating across a number of different regions (Germany, UK, Sweden, France, Netherlands, Hungary, Czech Republic, Slovakia, Romania and Russia, as well as joint ventures in Brazil and Turkey).

57. Under the E.ON Group, E.ON operations include:

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14 This process took place between July 2004 and December 2007.
15 See PR Newswire announcement 1998: Powergen to acquire East Midlands Electricity.
(a) Regional sales operations, which sells gas and electricity products to domestic and business customers.

(b) Regional energy networks.

(c) Renewables, which develops, builds and operates large renewable energy assets in a technology portfolio covering onshore and offshore wind and photovoltaic and concentrating solar power, primarily in Europe and North America.

(d) German nuclear generation.

58. Under the E.ON Group, Uniper operations include:

(a) Generation, which oversees and coordinates the operations of the E.ON Group’s generation portfolio (conventional and hydro generation) in Europe.

(b) Global Commodities, which buys and sells electricity, natural gas, LNG, coal, freight, and carbon allowances. In addition, it manages and develops assets at several stages of the gas value chain, including pipelines, long-term supply contracts, and storage facilities.

59. The UK regional business, E.ON UK, is engaged in the sale of gas and electricity products to almost eight million domestic and business customer accounts. It has five million electricity and three million gas customer accounts. The conventional generation business is now operated by Uniper UK Limited, as part of the E.ON Group.

60. Table 11 below provides a breakdown of E.ON’s UK operational generation capacity by type of generating fuel.

Table 11: Breakdown of E.ON Group’s UK generation capacity by fuel type (at 31/12/2015)

<table>
<thead>
<tr>
<th>Type</th>
<th>Number of sites</th>
<th>Capacity (MW)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Coal*</td>
<td>1</td>
<td>2,000</td>
</tr>
<tr>
<td>Gas*</td>
<td>5</td>
<td>4,635</td>
</tr>
<tr>
<td>Offshore wind</td>
<td>4</td>
<td>646</td>
</tr>
<tr>
<td>Onshore wind</td>
<td>14</td>
<td>257</td>
</tr>
<tr>
<td>CHP†</td>
<td>8</td>
<td>195‡</td>
</tr>
<tr>
<td>Biomass§</td>
<td>2</td>
<td>433</td>
</tr>
</tbody>
</table>


*Owned and operated by Uniper UK Ltd.
†Gas Combined Heat and Power.
‡Electrical output, sites also produce heat.
§Includes both Uniper and E.ON biomass.

61. In Table 12 below we show the segmental financial performance of the business in 2015, as presented in the group annual report.
Table 12: E.ON’s group segmental financial performance in 2015

<table>
<thead>
<tr>
<th></th>
<th>Sales (€bn)</th>
<th>EBITDA (€bn)</th>
<th>Operating cash-flow (€bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generation</td>
<td>7.5</td>
<td>1.5</td>
<td>1.5</td>
</tr>
<tr>
<td>Renewables</td>
<td>2.5</td>
<td>1.3</td>
<td>1.2</td>
</tr>
<tr>
<td>Global Commodities</td>
<td>87.9</td>
<td>0.2</td>
<td>-0.1</td>
</tr>
<tr>
<td>Exploration &amp; Production</td>
<td>1.7</td>
<td>0.9</td>
<td>0.9</td>
</tr>
<tr>
<td>Germany</td>
<td>19.3</td>
<td>2.2</td>
<td>1.7</td>
</tr>
<tr>
<td>Other EU countries</td>
<td>20.5</td>
<td>1.8</td>
<td>2.1</td>
</tr>
<tr>
<td>Non-EU Countries</td>
<td>1.1</td>
<td>0.3</td>
<td>0.4</td>
</tr>
<tr>
<td>Group Management/Consolidation</td>
<td>-24.3</td>
<td>-0.6</td>
<td>-0.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>116.2</td>
<td>7.6</td>
<td>7.0</td>
</tr>
</tbody>
</table>

Source: E.ON SE annual report 2015.

62. There is some additional breakdown of the segment ‘Other EU countries’, of which the UK supply business is a part. The information available for the UK is shown below in Table 13.

Table 13: Information relating to E.ON UK’s supply business

<table>
<thead>
<tr>
<th></th>
<th>2012 (€m)</th>
<th>2013 (€m)</th>
<th>2014 (€m)</th>
<th>2015 (€m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>9,701</td>
<td>9,714</td>
<td>9,346</td>
<td>9,546</td>
</tr>
<tr>
<td>EBITDA</td>
<td>289</td>
<td>378</td>
<td>384</td>
<td>384</td>
</tr>
<tr>
<td>Operating cash-flow</td>
<td>278</td>
<td>395</td>
<td>546</td>
<td>543</td>
</tr>
<tr>
<td>Investments</td>
<td>141</td>
<td>106</td>
<td>121</td>
<td>155</td>
</tr>
</tbody>
</table>

Source: E.ON SE annual report 2015.

63. It can be seen from Tables 12 and 13 that the UK regional business unit represents around 8% of E.ON group sales and around 5% of EBITDA. However, this underrepresents the UK’s importance to E.ON since it does not include the UK generation assets (which are reported as part of the Global Generation segment). In addition, Global Commodities may generate some profit from its interactions with E.ON’s retail and generation businesses in the UK.

Group financial performance and recent announcements

Group financial performance

64. Table 14 below shows E.ON’s summary group financial performance over the last seven years.
Table 14: Summary of E.ON’s group financial performance from 2009 to 2015

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>81.8</td>
<td>92.9</td>
<td>113</td>
<td>132.1</td>
<td>119.6</td>
<td>113.1</td>
<td>116.2</td>
</tr>
<tr>
<td>EBITDA</td>
<td>13.5</td>
<td>13.3</td>
<td>9.3</td>
<td>10.8</td>
<td>9.1</td>
<td>9.4</td>
<td>7.6</td>
</tr>
<tr>
<td>EBIT</td>
<td>9.6</td>
<td>9.5</td>
<td>5.4</td>
<td>7</td>
<td>5.6</td>
<td>4.7</td>
<td>4.4</td>
</tr>
<tr>
<td>Equity</td>
<td>44.7</td>
<td>45.6</td>
<td>39.6</td>
<td>38.8</td>
<td>36.6</td>
<td>26.7</td>
<td>19.1</td>
</tr>
<tr>
<td>Net debt</td>
<td>44.7</td>
<td>37.7</td>
<td>36.5</td>
<td>35.8</td>
<td>32.2</td>
<td>33.4</td>
<td>27.7</td>
</tr>
<tr>
<td>EPS*</td>
<td>€4.41</td>
<td>€3.07</td>
<td>–€1.16</td>
<td>€1.15</td>
<td>€1.10</td>
<td>–€1.64</td>
<td>–€3.60</td>
</tr>
<tr>
<td>DPS†</td>
<td>€1.50</td>
<td>€1.50</td>
<td>€1.0</td>
<td>€1.10</td>
<td>€0.60</td>
<td>€0.50</td>
<td>€0.50</td>
</tr>
</tbody>
</table>

Source: E.ON SE annual report 2015.
*Earnings per share.
†Dividend per share.
Note: EBITDA and EBIT are stated pre-exceptional items.

65. We note the following from Table 14:

(a) There has been a significant reduction in profitability over the last seven years. For example, EBIT has fallen by 55% and EPS has become negative.

(b) Financial performance reduced notably in 2011. This was caused by the shut-down of nuclear power stations in Germany following the Fukushima disaster, the introduction of a nuclear fuel tax as well as margin pressure in its gas business.

(c) During this period E.ON has reduced net debt from €44.7 billion to €27.7 billion. It has done this mainly through a series of asset disposals, for example the £4 billion sale in March 2011 of Central Networks.

(d) While E.ON has been profitable (as measured by pre-exceptional EBITDA/EBIT) during the period, it has generated low levels of positive free cash-flow. This has been caused in part by high levels of capital investment in its businesses.

Businesses included in the CSS

66. The CSS were introduced by Ofgem in 2009 and relate to those UK companies which hold a supply or generation licence. These companies operated within:

(a) Regional Business Unit UK.

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16 All German nuclear facilities are scheduled to close by 2022.
17 The aim of remedy was to provide better visibility/transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy, to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
(b) Global Generation – the UK generation element of this business is included.

**Iberdrola (Scottish Power)**

67. Below is a brief overview of Iberdrola SA (Iberdrola) and its UK subsidiary Scottish Power. It is set out as follows:

   (a) The history of Iberdrola and Scottish Power.

   (b) Current divisional structure.

   (c) Group financial performance, strategy and recent announcements.

   (d) Businesses included in Ofgem’s CSS.

**The history of Iberdrola and Scottish Power**

**Iberdrola**

68. Iberdrola is headquartered in Bilbao, Spain. It is the result of the 1991 merger of Iberduero and Hidroeléctrica Española. Its largest shareholder is Qatar Investment Authority, with a 9.7% stake.\(^\text{18}\)

69. In the late 1990s Iberdrola began expanding internationally, beginning in South America. In 2001, it decided to focus on the energy sector, investing in generation and electricity networks in Spain, Mexico and Brazil. It also began investing heavily in wind energy.

70. From 2006, it embarked on a further major international expansion, which led to the acquisitions of Scottish Power in the UK and Energy East (now Iberdrola USA). In 2011, it purchased the Brazilian company Elektro for US$2.4 billion.

71. As a result of its international expansion Iberdrola now has significant electricity businesses in Spain, the UK, the USA, Mexico and Brazil. Taking each in turn, further details are presented below:

   (a) In Spain it operates six nuclear plants, two coal fired power stations, eight CCGT power plants, 78 hydroelectric plants, 89 mini-hydroelectric

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\(^{18}\) Iberdrola Corporate Governance Report 2015.
plants and 195 wind farms. It also owns electricity distribution network assets and supply businesses\(^{19}\).

\((b)\) In the UK, through Scottish Power, Iberdrola operates three hydroelectric power plants, four CCGT power plants and 33 wind farms, and operated a coal-fired power plant which closed in March 2016. It also owns regulated electricity transmission (in Scotland) and distribution (in England, Scotland and Wales) network assets.\(^{20}\) We discuss the development of this business in greater detail below.

\((c)\) In the USA, it owns electricity generation, transmission, distribution and retail assets as well as a gas storage business.

\((d)\) In Brazil, it is the largest electricity distribution network owner and also owns electricity generation and retail businesses.

\((e)\) In Mexico, Iberdrola is the largest private power producer, owning six CCGT power plants and five wind farms.\(^{21}\)

**Scottish Power**

72. Iberdrola made an agreed bid for Scottish Power in November 2006, and the acquisition completed in 2007. The Iberdrola bid amounted to 777 pence per share\(^{22}\) plus a special dividend of 12 pence per share valuing the share capital at £11.6 billion. A year earlier Scottish Power had rejected a bid from E.ON in November 2005 at 570 pence per share.

73. Scottish Power was formed in 1990 and privatised in June 1991. It traces its history to the South of Scotland Electricity Board\(^{23}\) (SSEB), which was a vertically integrated public utility operating electricity transmission, distribution and supply in the south of Scotland. The North of Scotland Hydroelectric board (which became SSE) was the equivalent in the north of Scotland. Most of SSEB’s assets, the notable exception being the nuclear power stations, were included in the privatisation of Scottish Power.

74. It is worth noting that in Scotland the electricity industry was privatised on a vertically integrated basis, unlike England and Wales where the RECs initially

\(^{19}\) Iberdrola Integrated Report 2016.


\(^{22}\) Based on Iberdrola closing share price as at 27 November 2006, the day before the accepted offer was announced.

\(^{23}\) Which itself was a result of the 1955 merger of the South-East Scotland Electricity Board and the South-West Scotland Electricity Board.
owned the distribution network and retail supply but no power generation assets.

75. In 1995 Scottish Power acquired Manweb, a REC, expanding its reach into England and Wales. Between 1996 and 2006 it also acquired and then subsequently sold Southern Water and PacifiCorp (an electric power company based in the northwest USA). The sale of PacifiCorp to Berkshire Hathaway generated an impairment charge of £927 million. By 2002 Scottish Power fully demerged a telecommunications business that it had developed.

Current divisional structure and financial performance

76. Iberdrola organises its business into three segments:

(a) Networks contains the businesses that are regulated, for example Scottish Power's electricity transmission and distribution assets.

(b) Wholesale and Retail contains businesses that operate in liberalised energy markets, for example the electricity generation and supply businesses of Scottish Power.

(c) Renewables contains the renewable energy assets.

77. Iberdrola also segments its divisional financial performance by country. Spain, the UK, the USA, Brazil and Mexico represent the vast proportion of its geographic exposure.

78. Table 15 below summarises the profits (as measured by EBITDA) generated by each of the business segments and countries between 2009 and 2015.
It can be seen from Table 15 that Spain represents the largest component of Iberdrola’s profits, at around 47% of total EBITDA.

It can also be seen that the UK regulated networks business (which comprises electricity transmission and distribution assets in Scotland and electricity distribution assets in England and Wales) is much more significant than the other UK businesses. For example, between 2013 and 2015, UK networks generated 45% more EBITDA than the UK Wholesale & Retail and Renewables businesses combined.

Group financial performance and recent announcements

Group financial performance

Table 16 below shows Iberdrola’s summary group financial performance over the last seven years.
Table 16: Summary of Iberdrola’s group financial performance from 2009 to 2015

€bn

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>25.9</td>
<td>30.4</td>
<td>31.6</td>
<td>34.2</td>
<td>31.1</td>
<td>30.0</td>
<td>31.4</td>
</tr>
<tr>
<td>EBITDA</td>
<td>6.8</td>
<td>7.5</td>
<td>7.7</td>
<td>7.7</td>
<td>6.8</td>
<td>7.0</td>
<td>7.3</td>
</tr>
<tr>
<td>EBIT</td>
<td>4.5</td>
<td>4.8</td>
<td>4.5</td>
<td>4.4</td>
<td>2.2</td>
<td>3.9</td>
<td>3.8</td>
</tr>
<tr>
<td>Net income</td>
<td>2.8</td>
<td>2.9</td>
<td>2.8</td>
<td>2.8</td>
<td>2.6</td>
<td>2.3</td>
<td>2.4</td>
</tr>
<tr>
<td>Equity</td>
<td>29.0</td>
<td>31.7</td>
<td>33.2</td>
<td>34.1</td>
<td>35.3</td>
<td>35.8</td>
<td>41.0</td>
</tr>
<tr>
<td>Net debt</td>
<td>28.5</td>
<td>29.5</td>
<td>31.7</td>
<td>30.3</td>
<td>28.8</td>
<td>25.6</td>
<td>28.1</td>
</tr>
<tr>
<td>EPS*</td>
<td>€0.54</td>
<td>€0.52</td>
<td>€0.47</td>
<td>€0.45</td>
<td>€0.41</td>
<td>€0.36</td>
<td>€0.38</td>
</tr>
<tr>
<td>DPS†</td>
<td>€0.33</td>
<td>€0.34</td>
<td>€0.34</td>
<td>€0.34</td>
<td>€0.31</td>
<td>€0.28</td>
<td>€0.28</td>
</tr>
</tbody>
</table>

*Earnings per share.
†Dividend per share.
Note: In 2013 there was a significant positive tax effect which means that net income and EPS is not comparable with previous years.

82. From Table 16 we note the following:

(a) Between 2009 and 2012 Iberdrola reported a very stable level of profits (as measured by EBIT/EBITDA and net income), although it did acquire businesses which added to profits over this period (for example Elektro in Brazil) so the underlying profit performance was slightly negative.

(b) In 2013, EBIT fell by 50%. This was driven by one-off impairments in Brazil and the Renewables division. EBITDA fell by around 12%, mainly due to an increase in generation taxation in Spain of €0.5 billion.24

Businesses included in the CSS

83. The CSS were introduced by Ofgem in 2009 and relate to those UK businesses which hold a supply or generation licence.25 The CSS capture Iberdrola’s UK Wholesale & Retail and Renewables businesses, but not its UK Networks business. The renewables business may also contain some UK generation activity, which is captured in the CSS.

RWE AG

84. Below is a brief overview of RWE AG (RWE) and its UK subsidiaries. It is set out as follows:

(a) The history of RWE and its UK retail and generation subsidiaries.

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24 Iberdrola 2013 full year results presentation.
25 The aim of remedy was to provide better visibility/transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy, to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
(b) Current divisional structure.

(c) Group financial performance and recent announcements.

(d) Businesses included in Ofgem’s CSS.

The history of RWE

RWE

85. RWE is based in Essen, North Rhine-Westphalia. In 2013 it was the largest electricity producer in Germany. In the early 1990s it was an industrial conglomerate with interests that included energy, mining, raw materials, petroleum/chemicals, waste management and engineering. It has subsequently narrowed its focus to become a utility with a focus on the electricity and gas supply chain. RWE’s international expansion has been focused on Europe, although between 2001 and 2008 it owned American Water. RWE’s wholesale energy and commodities trading business, RWEST, operates globally.

86. Until very recently RWE operated across the entire electricity and gas supply chain, including the upstream production of oil and gas. However, it sold its upstream oil and gas production business (RWE Dea) in March 2015 which resulted in its main businesses being:

(a) power generation in Germany, the UK and the Netherlands;

(b) electricity distribution networks and supply in Germany;

(c) electricity, gas and energy services supply in the Netherlands and Belgium (this business is called Essent);

(d) electricity, gas and energy services supply in the UK (through npower);

(e) networks, generation and supply in Central Eastern and Southern Eastern Europe (through RWE East);

(f) renewables generation, through RWE Innogy; and

(g) Wholesale energy and commodities trading, through RWE Supply and Trading.

87. In December 2015 RWE announced that its renewables, grids and retail activities were being transferred into a new subsidiary and it planned to list the shares in the new subsidiary on the stock market.
88. The UK retail and generation arm of RWE traces its history back to National Power, which was one of the three England and Wales electricity generation companies formed from the CEGB during the privatisation of the UK electricity industry (the other two being Powergen and Nuclear Electric). It was created in 1990 and at that time generated around 50% of the electricity supplied in England and Wales, 91% of which was generated from coal.

89. It was privatised in March 1991 and the government sold its remaining 40% stake in 1995. It is worth noting that National Power’s business included a significant portfolio of international power generation assets that it had acquired after privatisation, which became a separate business (International Power) following the demerger of National Power in 2000.

90. From its beginnings as the largest power generator in England and Wales, the business then vertically integrated through the purchase and acquisition of the supply businesses of three RECs (Midlands, Yorkshire, Northern) as well Independent Energy and Calortex. During this period it also sold a significant amount of generation capacity, firstly in 1996 as following an Offer investigation and then with the sale of the giant Drax coal-fired power station in 1999 and Eggborough and Killingholme in 2000.

91. By the time National Power was demerged into Innogy and International Power in October 2000, Innogy owned eight UK power stations and had a market share of around 9% of generation (as compared to around 50% at privatisation in 1991).

92. In addition it is worth noting that RWE Group acquired Thames Water for £4.3 billion in 2001 and then subsequently sold it for £4.8 billion in December 2006 to a group led by Macquarie Group (both figures net of debt).

93. In October 2012, RWE npower plc sold its stake in Horizon Nuclear Power, which was a joint venture (with E.ON) set up to develop new build nuclear power plants in the UK. Hitachi acquired 100% of Horizon.

**Current structure and financial performance**

94. Table 17 below summarises the profits (as measured by EBITDA) generated by each of the group’s segments and geographies in 2012 and 2015.

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26 The largest power plant in the UK.
Table 17: Profits as measured by EBITDA generated by each of RWE Group’s business segments and geographies from 2012 to 2015

<table>
<thead>
<tr>
<th></th>
<th>€bn</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2012</td>
</tr>
<tr>
<td>RWE Group</td>
<td>9.3</td>
</tr>
<tr>
<td>Conventional Power Generation</td>
<td></td>
</tr>
<tr>
<td>of which:</td>
<td></td>
</tr>
<tr>
<td>Continental Western Europe</td>
<td>3.9</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>0.5</td>
</tr>
<tr>
<td>Supply/Distribution Networks Germany</td>
<td>2.3</td>
</tr>
<tr>
<td>Central Eastern and South Eastern Europe</td>
<td>1.3</td>
</tr>
<tr>
<td>Upstream Gas &amp; Oil</td>
<td>1.0</td>
</tr>
<tr>
<td>Supply Netherlands/Belgium</td>
<td>0.3</td>
</tr>
<tr>
<td>Supply United Kingdom</td>
<td>0.4</td>
</tr>
<tr>
<td>Renewables</td>
<td>0.4</td>
</tr>
<tr>
<td>Trading/Gas Midstream</td>
<td>(0.6)</td>
</tr>
<tr>
<td>Other, consolidation</td>
<td>(0.1)</td>
</tr>
</tbody>
</table>

Source: RWE 2013 and 2015 annual reports.

95. It can be seen from Table 17 that:

(a) the UK represents a relatively small proportion of group profit. In 2015 UK conventional power generation and UK supply contributed a little over 1% of RWE EBITDA (5.6% in 2014);

(b) conventional power generation no longer represents the most significant element of RWE’s EBITDA (31% in 2015 compared to 47% in 2012);

(c) Upstream Oil & Gas represented just under 11% of group EBITDA in 2013. RWE sold its upstream oil and gas production business (RWE Dea) in March 2015.

Group financial performance and recent announcements

Group financial performance

96. Table 18 below shows RWE’s summary group financial performance over the last seven years.
Table 18: Summary of RWE’s group financial performance from 2009 to 2015

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>47.7</td>
<td>53.3</td>
<td>51.7</td>
<td>53.2</td>
<td>52.4</td>
<td>48.5</td>
<td>48.6</td>
</tr>
<tr>
<td>EBITDA</td>
<td>9.2</td>
<td>10.3</td>
<td>8.5</td>
<td>9.3</td>
<td>7.9</td>
<td>7.1</td>
<td>7.0</td>
</tr>
<tr>
<td>EBIT</td>
<td>7.1</td>
<td>7.7</td>
<td>5.8</td>
<td>6.4</td>
<td>5.4</td>
<td>4.0</td>
<td>3.8</td>
</tr>
<tr>
<td>Net income*</td>
<td>3.5</td>
<td>3.8</td>
<td>2.5</td>
<td>2.5</td>
<td>2.3</td>
<td>1.3</td>
<td>1.1</td>
</tr>
<tr>
<td>Equity</td>
<td>13.7</td>
<td>17.4</td>
<td>17.1</td>
<td>16.5</td>
<td>12.1</td>
<td>11.8</td>
<td>8.9</td>
</tr>
<tr>
<td>Net debt</td>
<td>25.8</td>
<td>29.0</td>
<td>29.9</td>
<td>33.0</td>
<td>30.7</td>
<td>31.0</td>
<td>25.1</td>
</tr>
<tr>
<td>EPS†</td>
<td>€6.63</td>
<td>€7.03</td>
<td>€4.60</td>
<td>€4.00</td>
<td>€3.76</td>
<td>€2.09</td>
<td>€1.83</td>
</tr>
<tr>
<td>DPS‡</td>
<td>€3.50</td>
<td>€3.50</td>
<td>€2.00</td>
<td>€2.00</td>
<td>€1.00</td>
<td>€1.00</td>
<td>-</td>
</tr>
<tr>
<td>ROCE (RWE measure)</td>
<td>16.3%</td>
<td>14.4%</td>
<td>10.9%</td>
<td>12.0%</td>
<td>10.8%</td>
<td>8.4%</td>
<td>8.0%</td>
</tr>
</tbody>
</table>

Source: RWE annual reports.

*Stated pre-exceptional items.
†Earnings per share (based on adjusted net income).
‡Dividend per share.

Note: For 2015 fiscal year, dividend of €0.13 per preferred share was approved by the Annual General Meeting.

97. From Tables 17 and 18 we note the following:

(a) Sales and profits have reduced over the period and the dividend has been cut significantly. EBIT has fallen by 34%.

(b) RWE’s power generation business has been a key driver for the reduced levels of profits. For example, in 2010, its German power generation business alone reported EBITDA of €4.5 billion; by 2015 its entire power generation business (including the UK and the Netherlands) reported EBITDA of €2.0 billion.

Businesses included in the CSS

98. The CSS were introduced by Ofgem in 2009 and relate to those UK businesses which hold a supply or generation licence.28

SSE

99. Below is a brief overview of SSE plc (formerly known as Scottish and Southern Energy plc). It is set out as follows:

(a) The history of SSE plc.

(b) Corporate activity since 1998.

(c) Current divisional structure.

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27 RWE 2011 annual report.
28 The aim of remedy was to provide better visibility/transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy, to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
(d) Group financial performance and recent announcements.

(e) Businesses included in the CSS.

The history of SSE plc

100. SSE is the result of the 1998 merger of Southern Electric and Scottish Hydro Electric.

101. Southern Electric was formed in 1948 as the Southern Electricity Board to distribute electricity in Southern England. It was floated in 1990 as one of 12 England and Wales RECs. At privatisation, the RECs owned the local electricity distribution networks and monopoly retail operations but no power generation assets.29 The distribution network assets were later required to be operated separately and ring-fenced from the retail business under the Utilities Act 2000.

102. Scottish Hydro Electric traces its history back to Scotland’s hydroelectric power revolution, which began in 1943. The North of Scotland Hydroelectric board managed hydroelectric construction and then took control of the whole electric power supply chain in the north of Scotland (that is generation, distribution and retail). It was privatised as Scottish Hydro Electric in June 1991. In Scotland the electricity industry was privatised on a vertically integrated basis, unlike England and Wales where the RECs (for example, Southern Electric) initially owned no power generation assets.

Corporate activity since 1998

103. After expanding its supply business into South Wales, SSE has acquired additional generation capacity and upstream gas assets, thereby increasing its level of vertical integration. It also acquired gas distribution network assets from National Grid in its home areas of Scotland and Southern England in 2004 (via a joint venture). In addition SSE has built up its energy business in both Northern Ireland (NI) and the Republic of Ireland (ROI).

104. It is worth reiterating that the Scottish electricity industry was privatised in a vertically integrated structure and, as a result, the business required less corporate activity in order to achieve vertical integration.

105. SSE was part of the NuGeneration (NuGen) consortium with GDF Suez (now ENGIE) and Iberdrola (SSE had a 25% stake) which was set up to develop a

---

29 In England and Wales the electricity generation assets owned by the CEGB were privatised into three power generation companies – Powergen, National Power and Nuclear Electric.
new nuclear power station at Sellafield. In September 2011 it sold its stake to the other partners in the venture. Toshiba (through its Westinghouse subsidiary) is now the majority holder of NuGen.

Current divisional structure and financial performance

106. SSE has three divisions. These are as follows:

- Networks contains the regulated gas distribution and electricity and gas transmission and distribution assets. During financial year 2014/15, non-regulated network businesses (for example in Telecoms and Lighting Services) were moved out of the Networks and into the Retail division as part of a newly formed B2B enterprise business. The regulated electricity network assets are the legacy of the privatisation of Southern Electric (which owned the electricity distribution infrastructure in Southern England) and Scottish Hydro (which owned the electricity transmission and distribution network in Northern Scotland). The gas distribution assets are a result of an SSE acquisition from National Grid in 2004. SSE’s Networks businesses are regulated by Ofgem and ring-fenced from the remainder of SSE’s operations. Figure 5 below provides a breakdown of the Networks division EBIT in 2015.

Figure 5: Networks division, split of 2014/15 EBIT

- Retail supplies gas and electricity to more than eight million customers in Great Britain, NI and the ROI. It also supplies energy related services, such as gas boiler cover to domestic customers and metering services. Figure 6 below provides a breakdown of the Retail division EBIT in 2014/15.
Wholesale is comprised of four businesses: Generation operates and maintains the electricity producing assets; Energy portfolio management (EPM) procures fuel for the generation business and manages its interactions with the wholesale electricity market; Gas Storage operates and maintains SSE’s gas storage assets; and Gas Production ensures the efficient delivery of gas from the fields in which SSE has a share. Figure 7 below provides a breakdown of the Wholesale division EBIT in 2014/15 and Table 19 shows SSE’s electricity generation capacity and production in 2014/15 by fuel type.

Source: SSE.
Table 19: SSE’s GB electricity generation capacity and production in 2014/15 by fuel type

<table>
<thead>
<tr>
<th>Plant type</th>
<th>Capacity</th>
<th>Mothballed</th>
<th>Generation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>MW</td>
<td>MW</td>
<td>GWh</td>
</tr>
<tr>
<td>Thermal – coal</td>
<td>3,009</td>
<td>-</td>
<td>9,143</td>
</tr>
<tr>
<td>Thermal – gas/oil</td>
<td>5,330</td>
<td>1,915</td>
<td>9,788</td>
</tr>
<tr>
<td>Renewable – hydro</td>
<td>1,150</td>
<td>-</td>
<td>3,726</td>
</tr>
<tr>
<td>Renewable – onshore wind</td>
<td>1,552</td>
<td>-</td>
<td>3,486</td>
</tr>
<tr>
<td>Renewable – offshore wind</td>
<td>355</td>
<td>-</td>
<td>1,191</td>
</tr>
<tr>
<td>Renewables – biomass</td>
<td>38</td>
<td>-</td>
<td>63</td>
</tr>
<tr>
<td>Renewable – pumped storage/biomass</td>
<td>300</td>
<td>-</td>
<td>190</td>
</tr>
</tbody>
</table>

Source: SSE Preliminary Results 20 May 2015.

107. Table 20 below summarises the contribution to group profits of each of the divisions described above for 2013 and 2014 (note: SSE has a March year-end).

Table 20: Divisional contribution to overall SSE group profits in 2013–2015

<table>
<thead>
<tr>
<th></th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>EBIT/operating profit</td>
<td>£m</td>
<td>%</td>
<td>£m</td>
</tr>
<tr>
<td>Networks</td>
<td>874.24</td>
<td>49.1</td>
<td>955.42</td>
</tr>
<tr>
<td>Retail</td>
<td>409.1</td>
<td>22.9</td>
<td>292.0</td>
</tr>
<tr>
<td>Wholesale</td>
<td>508.6</td>
<td>28.5</td>
<td>634.6</td>
</tr>
<tr>
<td>Corporate unallocated</td>
<td>-12.9</td>
<td>-1.9</td>
<td>14</td>
</tr>
<tr>
<td>Total</td>
<td>1,779.0</td>
<td>1,880.1</td>
<td>1,881.4</td>
</tr>
</tbody>
</table>

Source: SSE annual report 2015.
Notes:
1. Operating profit is stated before exceptional items.
2. Note: columns do not sum – the difference is small unallocated corporate items.
3. SSE restated figures for 2013/14 to reflect changes to reporting structure due to the creation of Enterprise, part of the Retail segment – see SSE annual report 2015.

108. It can be seen from Table 20 that the regulated Networks division is the most significant contributor to profits at SSE, representing around 50% of operating profit before interest and tax. While most aspects of SSE’s business are relevant to our investigation the Retail business in GB and the Generation & EPM (in the Wholesale division) are particularly relevant.

**Group financial performance and recent announcements**

**Group financial performance**

109. Table 21 below shows SSE’s summary group performance over the last six years.
Table 21: Summary of SSE’s group performance from 2010 to 2015

<table>
<thead>
<tr>
<th></th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2010</td>
</tr>
<tr>
<td>Sales</td>
<td>21,550</td>
</tr>
<tr>
<td>Profit before tax*</td>
<td>1,316.9</td>
</tr>
<tr>
<td>EPS†</td>
<td>113.1</td>
</tr>
<tr>
<td>DPS‡</td>
<td>70.0</td>
</tr>
<tr>
<td>Net assets</td>
<td>3,121</td>
</tr>
<tr>
<td>Adjusted net debt (SSE measure incl hybrid capital)</td>
<td>5,292</td>
</tr>
</tbody>
</table>

Source: SSE statutory accounts 2010-2015.

* SSE measure.
† Earnings per share.
‡ Dividend per share.

110. From Table 21 and a review of recent SSE accounts we note the following:

(a) SSE has grown profit before tax at a compound rate of 3.5% over the period (on a pre-exceptional basis).

(b) Net debt has increased by £2.3 billion to £7.6 billion over the period. Leverage (as measured by net debt: equity) has also increased.

(c) SSE has increased its dividend every year since 1999. During the period since 1999 it has grown its dividend from 25.7p to 88.4p. It intends to grow the dividend by at least RPI in future.30

(d) There have been significant asset write-offs in the period, which are not captured in the SSE measure of profits (stated before exceptional items). These exceptional items (as well as other re-measurements on long-term energy contracts) help explain why net assets have not grown despite SSE being consistently profitable over the period. Table 26 below shows some examples of asset impairments from recent years.

Table 22: Examples of asset impairments 2011–2015

<table>
<thead>
<tr>
<th></th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>Impairment of coal-fired Generation assets</td>
</tr>
<tr>
<td>2015</td>
<td>Impairment of gas storage assets</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of thermal Generation assets</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of renewable Generation assets</td>
</tr>
<tr>
<td>2014</td>
<td>Impairment of gas storage assets</td>
</tr>
<tr>
<td>2013</td>
<td>Impairment of thermal Generation assets</td>
</tr>
<tr>
<td>2012</td>
<td>Impairment of Generation assets</td>
</tr>
<tr>
<td>2011</td>
<td>Impairment of Generation assets</td>
</tr>
</tbody>
</table>

Source: SSE.

30 SSE 2015 results presentation.
Businesses included in the CSS

111. The CSS were introduced by Ofgem in 2009 and relate to those UK businesses which hold a supply or generation licence.\(^{31}\) It may be useful to understand which of SSE’s businesses are included in these statements:

(a) Networks are not included.

(b) Retail – ‘Energy Supply’ included (GB only). ‘Energy Related Services’ (boiler insurance etc) are not included.

(c) Wholesale – ‘Generation’ included (GB only). EPM, Gas Storage and Gas Production are all excluded.

112. Together, GB generation and supply businesses covered by the CSS contributed around 35% of SSE’s group EBIT in 2014/15.

Gas producers other than Centrica

113. There are a number of other gas producers who are active in the market in Great Britain: Statoil, ExxonMobil, Total, Shell, BP, ENGIE and Gazprom.

Mid-tier independent generator company profiles

114. This section sets out information about the four largest independent generators in the market in Great Britain. We refer to these four generators as ‘mid-tier’ generators. They are:

(a) ENGIE (formerly GDF Suez);

(b) Drax Group;

(c) Intergen; and

(d) ESB International.

115. Table 23 below provides a quick summary of these generators’ attributes.

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\(^{31}\) The aim of the remedy was to provide better visibility/transparency regarding: (a) the profitability of different activities in the value-chain; and (b) the transfer price used by the supply and generation businesses to exchange wholesale energy, to alleviate concerns about cross-subsidisation. Ofgem (October 2009), Financial Information Reporting: Guidance, paragraph 1.3.
Table 23: Summary of mid-tier independent generators’ attributes

<table>
<thead>
<tr>
<th>Name</th>
<th>GB Generation capacity</th>
<th>Generation type</th>
<th>Supplier</th>
</tr>
</thead>
<tbody>
<tr>
<td>ENGIE</td>
<td>5GW (gross) 3.8GW (net)</td>
<td>CCGT,* Coal, Pumped storage, Wind</td>
<td>Yes – business customers</td>
</tr>
<tr>
<td>Drax</td>
<td>4GW</td>
<td>Coal, Oil, Biomass</td>
<td>Yes – business customers</td>
</tr>
<tr>
<td>Intergen</td>
<td>2.5GW</td>
<td>CCGT</td>
<td>No</td>
</tr>
<tr>
<td>ESB International</td>
<td>0.8GW</td>
<td>CCGT, Wind</td>
<td>No</td>
</tr>
</tbody>
</table>

Source: ENGIE, Drax, Intergen, ESB International.
*Combined Cycle Gas Turbine.

Notes:
1. For ENGIE, gross and net GB capacity figures are given because it does not own 100% of all of its plants.
2. ESB International has an additional 0.9GW (CCGT) under construction at Carrington.

ENGIE

116. GDF Suez changed its name to ENGIE in April 2015. ENGIE is headquartered in Paris and operates in more than 70 countries worldwide with sales of €74.7 billion in 2014. It is quoted on the Paris stock exchange and has a market capitalisation of around €47 billion. It operates globally in Power, Natural Gas, LNG and Energy Services.

117. It acquired 70% International Power\(^\text{32}\) in February 2011 and acquired the remaining 30% of the company in June 2012. ENGIE has various operations in the UK, including: electricity generation; oil and gas E&P; LNG; gas storage; engineering project management and construction; supply of electricity and gas to businesses; and environmental services and facilities management.

118. We briefly discuss its electricity generation and supply operations in GB below.

Generation

119. ENGIE has around 5GW of gross\(^\text{33}\) electricity generation capacity in the UK, making it the seventh largest generator in the UK by capacity. It represents around 6% of UK capacity, as of May 2016 ENGIE operates the following plants:

   (a) Two gas-fired power stations (Deeside, Saltend) that are each 75% owned and have combined capacity of 1,712 MW.

   (b) One coal-fired power station, with combined capacity of around 1GW. ENGIE owns 75% of Rugeley. ENGIE sold its 10% share of Eggborough\(^\text{34}\)

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\(^{33}\) Net capacity is around 4GW as GDF Suez does not have 100% ownership of all sites.

\(^{34}\) Eggborough has announced its intention to close. It applied for funding for conversion to biomass but was not selected.
to EPH in November 2014 and expects to cease market operations at Rugeley in the summer of 2016.

(c) One pumped storage facility, First Hydro, which is 75% owned and has capacity of 2,088 MW.

(d) Six wind farms, which are 50% owned, with combined capacity of 68 MW.

120. It is also a 40% shareholder in the NuGen joint venture, which was set up in 2009 to build a new nuclear power station at Sellafield. Toshiba is its joint venture partner, through its Westinghouse subsidiary.

Energy supply

121. ENGIE is a business-to-business supplier of energy in the UK. As of the end of March 2016 it supplied around 12,000 business premises with electricity and around 4,550 business premises with gas.

122. It also owns 30% of Opus Energy, which was established in 2002 and is an independent supplier to around 230,000 sites for electricity and 45,000 for gas as of the end of March 2016.

Drax Group

123. Drax power station was originally built, operated and owned by the Central Electricity Generating Board (CEGB). It was the last coal-fired power station to be built in the UK, completed in two stages in 1974 (three units) and 1986 (three units). Each unit has a capacity of 660MW, giving a total capacity of almost 4,000MW and making it the largest power station in the UK, meeting around 7% of UK electricity demand.

124. Drax power station was privatised as part of National Power and subsequently sold to AES Corporation in 1999. Following a significant drop in wholesale electricity prices in 2002, it experienced financial problems when its major customer went into administration. Creditors took control of the business and

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35 Pumped storage is a form of hydroelectric power generation used for load balancing during times of high demand.
36 Mitsui owns a minority 25% stake in First Hydro.
37 NuGen was originally a partnership between GDF SUEZ, Iberdrola (which owns Scottish Power) and SSE. Iberdrola and SSE have both now sold their positions in the venture.
38 Westinghouse Electric is a US based nuclear power company that is 87% controlled by Toshiba.
39 Opus Energy is also part-owned by Telecom Plus plc (trading as Utility Warehouse), a mid-tier independent energy supplier, which holds a 20% stake in Opus Energy.
40 Listed on the New York Stock Exchange, with a portfolio of electricity generation and distribution businesses.
following a re-financing Drax Group emerged in December 2005 as a quoted business for the first time. It is currently a constituent of the FTSE 250.

125. In March 2009 it acquired Haven Power, an electricity supplier focused on business customers. It has since significantly grown sales to small and medium sized enterprises (SMEs) and industrial and commercial (I&C) customers. It aims to grow this business to sell 12 to 15 TWh of electricity each year, which compares to its electricity generation of 26.2 TWh in 2013.

126. In July 2012, Drax announced that it would transform the business into a predominantly biomass-fuelled generator through burning sustainable biomass in place of coal. It has plans to convert three of its six generating units to burn biomass. The first of the three units were successfully converted in April 2013, and the new biomass receipt, storage and distribution systems to support the converted units were officially launched in December 2013. The biomass generation plants will rely on government subsidies (eg the Contracts for Difference Feed in Tariff (CfD FIT)).

127. Table 24 below shows Drax’s summary group financial performance over the last seven years.

Table 24: Summary of Drax’s group financial performance 2009 to 2015

<table>
<thead>
<tr>
<th>Year ending December</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>1.5</td>
<td>1.6</td>
<td>1.8</td>
<td>1.8</td>
<td>2.1</td>
<td>2.8</td>
<td>3.1</td>
</tr>
<tr>
<td>EBITDA</td>
<td>0.4</td>
<td>0.4</td>
<td>0.3</td>
<td>0.3</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
</tr>
<tr>
<td>EBIT</td>
<td>0.3</td>
<td>0.3</td>
<td>0.3</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
<td>0.1</td>
</tr>
<tr>
<td>EPS*</td>
<td>58p</td>
<td>64p</td>
<td>55p</td>
<td>51p</td>
<td>35p</td>
<td>24p</td>
<td>11p</td>
</tr>
</tbody>
</table>

*Earnings per share, stated pre-exceptional items.
Note: EBITDA and EBIT are stated pre-exceptional items.

128. It can be seen from Table 24 that EBIT fell in 2013 – this was due to the removal of free carbon allowances which were granted under the EU Emissions Trading System (ETS) scheme. Free carbon allowances were withdrawn for the electricity generation market from 1 January 2013.

129. We note that Drax in 2013, unlike the Six Large Energy Firms, holds a net cash position (of £71 million).

**Intergen**

130. Intergen is a global power generation firm with 12 power plants representing a total generation capacity of 7,322 MW. It aims to be a world leader in the development, ownership, and operation of power generation and related energy infrastructure. Its plants are located in the UK, the Netherlands,
Mexico and Australia. Intergen is jointly owned by the Ontario Teachers’ Pension Plan and China Huaneng Group.

131. In the UK, Intergen owns three CCGT power plants, located at:

(a) Rocksavage, Runcorn (810 MW), which opened in 1998;

(b) Coryton, Essex (800 MW), which opened in 2002; and

(c) Spalding, Lincolnshire (880 MW,) which opened in 2004. Centrica originally owned a 50% share of the equity in the project.

132. It is a Netherlands registered company (Intergen NV) and has a number of subsidiary companies in the UK. At this stage, there is limited available financial information.

**ESB International**

133. ESB Group (ESB) is a 95% state owned Irish electricity business.\(^4^1\) It is headquartered in Dublin and operates across electricity networks,\(^4^2\) power generation and supply in the ROI. It also built and owns a national fibre optic cable network in the ROI and owns the electricity transmission and distribution network in NI.

134. ESB had revenues of €3.4 billion in 2013 and made profit before tax of €526 million. ESBI has sales of over €500 million. Its assets in GB are focused on electricity generation, as follows:

(a) Corby Power Station, a 350 MW CCGT plant in Northamptonshire, opened in 1992. ESBI had previously been a minority owner of the plant but in 2011 took full control.

(b) Carrington Power Station, a 860 MW CCGT plant that is under construction near Manchester. It is expected to become commercially operational in 2016.

(c) A 25 MW wind farm in West Durham.

(d) A 66 MW wind farm in Fullabrook.

(e) A 35 MW wind farm in Myneed y Betws.

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\(^4^1\) The remaining 5% is held by an Employee Share Ownership Trust.

\(^4^2\) As Distribution system operator and Transmission asset owner. It is also the Transmission and Distribution network owner in NI.
135. We note that ESBI says that it is using its substantial CCGT expertise and experience to develop a generation portfolio in Britain of the order of 3,000 MW in the next decade, in addition to its existing assets. This ambition is dependent on prevailing market and regulatory conditions.

The mid-tier energy suppliers

136. This section provides an overview and brief history of the independent energy suppliers whom, for the purposes of our market investigation, we have provisionally classified as ‘mid-tier’ energy suppliers, namely: First Utility, Ovo Energy, Co-op Energy and Utility Warehouse.

137. The information contained in this part of the appendix was based on desktop research and confidential submissions from the relevant companies during the joint Ofgem/OFT/CMA assessment of the state of the energy market (published in March 2014) (phase 1).

138. A snapshot overview of the independent suppliers covered in this appendix is set out in Table 25 below. References to ‘run-rate’ revenues in this appendix mean the annual revenues that a supplier would have generated in its financial year, if the part-year revenue impact of customers joining and leaving during the year, was assumed to have had a full-year 12-month impact on revenues.

Table 25: Overview of mid-tier independent suppliers

<table>
<thead>
<tr>
<th>Supplier name</th>
<th>Year of market entry</th>
<th>Ultimate parent</th>
<th>Headquarters</th>
<th>Energy customers*</th>
<th>Energy supply revenues</th>
<th>Method of sourcing wholesale energy</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Utility</td>
<td>2006</td>
<td>Impello plc</td>
<td>Warwick</td>
<td>705,000‡</td>
<td>FY14: £562m</td>
<td>Structured deal with Shell (previously with Morgan Stanley)</td>
</tr>
<tr>
<td>Ovo Energy</td>
<td>2009</td>
<td>Ovo Group Ltd</td>
<td>Bristol</td>
<td>660,000†</td>
<td>FY13: £172m</td>
<td>Trading arrangement with third party</td>
</tr>
<tr>
<td>Co-op Energy</td>
<td>2010-11</td>
<td>The Midcounties Co-operative Ltd</td>
<td>Warwick</td>
<td>[x]&lt;sup&gt;[$]&lt;/sup&gt;</td>
<td>FY15: [x]&lt;sup&gt;[x]&lt;/sup&gt;</td>
<td></td>
</tr>
<tr>
<td>Utility Warehouse</td>
<td>2003</td>
<td>Telecom Plus plc (listed)</td>
<td>London</td>
<td>950,000 supply points*</td>
<td>FY14/15: £583.1m</td>
<td>Long-term wholesale supply agreement with npower (RWE)</td>
</tr>
</tbody>
</table>


*The number of customers are counted only once regardless of whether they are on single or dual fuel tariffs. The number of accounts or supply points however would count a customer twice if that customer was a dual fuel customer.
†Updated for 2016.
‡First Utility FY14 statutory accounts.

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43 ESBI website
44 If appropriate, company profiles of a selection of smaller energy suppliers may be prepared during the course of our investigation.
First Utility

Company overview

139. First Utility Limited (First Utility) is headquartered in Warwick. The company first entered the retail energy market in 2006. Over FY 2014, it employed an average of 477 staff, and currently supplies around 705,000 customers, over 90% of whom are on dual fuel contracts.

140. First Utility is a wholly-owned subsidiary of Impello plc (unlisted), which for its financial year (FY) ended 31 December 2014, generated consolidated revenues of around £562 million, almost all of which came from its GB energy supply business, with less than 1% from its telecoms reselling activities. Five of the eight directors who serve on the First Utility board of directors are also on the board of Impello plc.

141. During FY14, First Utility generated an operating profit (before exceptional items) of £10.8 million (prior year: £0.6 million) on total revenues of £562 million (prior year: £283 million), which resulted in an operating margin of 1.9% (prior year: 0.2%).

Brief history

142. First Utility has its origins in a previous business, First Telecom, which served around half a million domestic customers across the UK, France and Germany, before it was eventually sold in 2000.

143. It first entered the retail energy market in 2006, focusing on SME and new build customers, with a strategy to apply the ‘telecoms business model’ to energy supply, focusing on customer service and using smart meters to obtain accurate billing information. It considered that a ‘smart meter’ offering was a means of differentiating its business from those of the Six Large Energy Firms.

144. However, by 2009, its focus shifted to the mass market, although it cited a number of difficulties around rolling out smart meters. More recently, it took

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45 First Utility FY14 statutory accounts.
46 Ibid.
47 Impello plc FY14 statutory accounts.
48 First Utility FY14 statutory accounts.
49 FY13 exceptional items were -£3.6 million, relating to the termination of its trading counterparty arrangement with Morgan Stanley and First Utility’s withdrawal from the ‘new homes’ customer segment (source: First Utility statutory accounts for the year ended 31 December 2013).
50 First Utility statutory accounts for the year ended 31 December 2013.
the decision to exit the non-domestic sector, and that it believed its growth opportunity lay in the domestic sector.

145. In recent years, its customer base had grown significantly, eg during 2012, it grew its customer base from 60,000 to 170,000, and in October 2013 alone, it won around 100,000 customers. During its phase 1 hearing, First Utility stated that it had benefited from the Six Large Energy Firms’ recent price increase announcements, and from the subsequent media and political focus on energy prices and the benefits of switching energy suppliers. In its FY14 audited accounts, First Utility reported that by the end of FY14, its total energy customer base had increased by 123% during the year to 705,000 (2013: 314,131).

146. To accommodate its large growth in its customer base, in early 2013, First Utility stated during its phase 1 hearing that it had invested around £5 million into a new bespoke customer care and billing system that would enable it to scale up to serve between one and two million customers, with minimal further investment required. It also restarted rolling out smart meters to its customers (currently around 85,000 to 95,000 customers have smart meters installed).

Ovo Energy

Company overview

147. Established in September 2009, and headquartered in Bristol, Ovo Energy Limited (Ovo Energy) employs \[\times\] and currently supplies electricity and gas to around 660,000 customers, the majority of whom are on fixed tariff contracts, with around 95,000 customers on variable tariffs.

148. Ovo Energy is a wholly-owned subsidiary of Ovo Group Limited, which is majority owned by Stephen Fitzpatrick and his immediate relatives through direct shareholdings and a holding company.

149. For its financial year ended 31 December 13, Ovo Energy increased its customer base from around 131,000 (FY12) to 137,000, but generated an operating loss (before exceptional items) of –£67,000 (prior year: –£3 million operating loss) on total revenues of around £172 million (prior year: £103 million). On the back of a large advertising campaign, there was significant growth in FY14 up to 408,000 customers generating revenues of £317 million.

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51 First Utility statutory accounts for the year ended 31 December 2013.
52 \[\times\] staff based on average employees during FY13 (FY12: \[\times\] staff) (source: Ovo Energy FY13 statutory accounts).
53 Ovo Energy FY13 statutory accounts.
Due to the significant costs of acquiring these customers, this resulted in a £33.9 million operating loss.

**Brief history**

150. Since entering the retail market in 2009, Ovo Energy has grown its customer base to around 660,000 customers. It stated at its phase 1 hearing that its ambition was to grow its customer base to over one million over the next three years through marketing campaigns aimed at addressing customer disengagement, and highlighting the benefits of switching suppliers.

151. It stated that it had invested significantly in online platforms to deliver on its strategy to provide customers with the ‘best possible value and service’.

**Co-operative Energy**

**Company overview**


153. Co-op Energy is a wholly-owned subsidiary of The Midcounties Co-operative Limited (Midcounties Co-op), a cooperative society based in Warwickshire that includes food stores, pharmacies and funerals, with annual turnover for the year 2015/16 of around £1.25 billion.

154. By the end of its financial year ended 26 January 2016 (ie FY15), Co-op Energy grew its customer base from around [X] (FY14) to [Y], and reported FY15 revenues of £[Z] (prior year: £217 [Y]) and an operating loss (before exceptional items) of £[Z].

**Brief history**

155. Co-op Energy entered the energy supply market in 2010. In FY13, Co-op Energy saw a significant increase in its customer base, which it attributed to a number of factors, including its success in the switching initiatives.

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54 Total FY13 exceptional items of around [X] comprised [Z] in one-off start-up costs for the energy business, and [Z] in commissions paid to energy switching websites. The treatment of the latter as an exceptional item may be questionable (source: Midcounties Co-operative Annual Report and Accounts 2013).

orchestrated by the consumer group Which?, which saw [X] new customers join in a single day.\textsuperscript{56}

\textbf{Utility Warehouse}

\textit{Company overview}

156. Utility Warehouse is a wholly-owned subsidiary of its London-based ultimate parent company, Telecom Plus plc (Telecom Plus), which is listed on the London Stock Exchange and is a constituent of the FTSE 250 index, with a current market capitalisation of just over £772.5 million (as at 18 May 2016).\textsuperscript{57}

157. Telecom Plus trades under the ‘Utility Warehouse’ brand, and supplies domestic and small business customers with electricity and gas, as well as landline and mobile telephony, broadband services. For its latest financial year ended 31 March 2015 (ie FY15), Telecom Plus generated total consolidated revenues of £729.2 million (prior year: £659 million). Its energy supply business generated £583 million in FY14 (prior year: £528 million).\textsuperscript{58}

158. Telecom Plus also holds a 20% equity stake in another independent energy supplier, Opus Energy Group Limited (Opus Energy), which was acquired by Telecom Plus in 2002.\textsuperscript{59} Opus Energy generated FY15 revenues of £523 million (prior year: £434 million).\textsuperscript{60}

159. Utility Warehouse is one of the largest independent energy suppliers in GB with over 950,000 supply points, of which around 40% are ‘energy only’ contracts and the remaining 60% on a combination of ‘energy and other utility’ contracts. Utility Warehouse stated that 80% of its energy customers were on dual fuel contracts. The average annual revenue per customer (across all of Telecom Plus’s utility customers) for FY15 was around £1,279.\textsuperscript{61}

\textit{Brief history}

160. Utility Warehouse entered the market in 2003 and stated that its target was to grow its share of the energy supply market to at least 5%.

161. During 2012, Utility Warehouse added between 60,000 and 70,000 of net supply points (ie net of leavers) to its customer base, and a further 100,000 net supply points during 2013. It stated that all of these customers joined

\begin{itemize}
\item \textsuperscript{56} \textit{Midcounties Co-operative Annual Report and Accounts 2013.}
\item \textsuperscript{57} Source: London Stock Exchange (18 May 2016).
\item \textsuperscript{58} Telecom Plus Report and Accounts year ended 31 March 2015.
\item \textsuperscript{59} Telecom Plus Report and Accounts year ended 31 March 2015.
\item \textsuperscript{60} Telecom Plus Report and Accounts year ended 31 March 2015.
\item \textsuperscript{61} Telecom Plus preliminary FY14 results announcement.
\end{itemize}
through ‘word of mouth’ as it did not undertake any advertising, and did not ‘sell’ through switching websites. Instead, it works in partnership with over 44,000 independent (and part-time) distributors (known as ‘Partners’) who receive a ‘small share of the revenues’ from each new customer they introduce.62

162. In December 2013, Telecom Plus renewed and revised its ‘long-standing’ wholesale energy supply agreement with npower, which secured its wholesale supply on ‘improved commercial terms’ for a further 20 years. As part of this arrangement, Telecom Plus also acquired two of npower’s subsidiaries, Gas Plus Supply Limited and Electricity Plus Supply Limited, for a total consideration of £218 million.63 Telecom Plus had previously sold these two subsidiaries to npower in 2005, after Telecom Plus struggled to secure wholesale energy profitably.64 The disposals by npower were reported to be the result of rules introduced by Ofgem which restricted suppliers to offering four tariffs to their customers. These acquisitions did not result in a change in the number of customers served by Utility Warehouse given that npower’s subsidiaries were legal vehicles which held supply licences, and all of their customer relationships (around 770,000 accounts) were already managed, and served, by Utility Warehouse prior to these transactions.65

64 www.telegraph.co.uk (20 November 2013).
65 Although the acquired subsidiaries were owned by npower, all their customers prior to the acquisitions had been supplied under the Utility Warehouse brand and managed by Telecom Plus under a management services agreement entered into between Telecom Plus and npower in March 2006 (source: npower press release, 20 November 2013).