RWE - UK Generation & Supply Consolidated Segmental Statement

for the year ended 31 December 2014

Executive Summary

Supply Domestic segment

- In 2014 the domestic supply segment provided 3.1m customers with 11.5 terawatt hours (TWh) of electricity and 2.2m customers with 994m therms (29.1 TWh) of gas. Compared to 2013 there was a significant reduction in domestic supply volumes (quoted in TWh) of 27% (electricity down 21%, gas down 29%) reflecting:
  - the milder winter temperatures in 2014 resulting in lower consumption by customers;
  - the continuing trend of lower per capita consumption as customers change their energy usage behaviours and the benefits arising from energy efficiency measures implemented in recent years;
  - a net loss of customers in the domestic segment reflecting competitive pressures in the UK energy market and the continued growth of alternative suppliers to the traditional energy companies.
- As a consequence of the factors above, total domestic revenues fell by 22% to £3bn (2013: £3.9bn) with revenues in electricity down 19% and gas down 25%.
- Total Domestic fuel costs fell by 30.6% reflecting the large decline in volumes and also the reduction in commodity prices compared to 2013.
- However, despite the 27% reduction in volumes, total domestic direct costs only fell by 16% as:
  - network and transportation providers increased the unit costs they charge us to supply gas and electricity to our customers' homes;
  - the ongoing cost of fulfilling government mandated environmental and social obligations which are driven by policy rather than supply volume.
- The indirect costs incurred to serve our customers and run the domestic segment fell by 2% compared to 2013. In 2014 considerable time and resources were invested to improve our customer service and billing performance following the introduction of a new billing system for our domestic customers in 2013. Excluding these costs, the reduction in underlying indirect costs is greater than the headline 2%, as the benefits of the end to end business transformation programme are realised. This programme is committed to drive efficiencies, improve our customer service and place the customer at the heart of the Supply business.
- The decline in domestic revenues, combined with; increasing unit costs charged by the network and distribution companies; ongoing environmental and social obligation costs and indirect costs as described above, resulted in EBIT (earnings before interest and tax) for the domestic supply segment falling 39.4% to £80m (2013: £132m).
- EBIT margin for the domestic supply segment fell to 2.7% (2013: 3.4%). The average EBIT generated for a domestic customer in 2014 was £10.87/customer for electricity and £20.89/customer for gas.

Supply Non-domestic segment

- The non-domestic segment supplied 361k customers with 34 TWh of electricity and 52k customers with 336m therms (9.8 TWh) of gas. Compared to 2013 there was an increase in non-domestic supply volumes (quoted in TWh) of 16% (electricity up 3%, gas up 105%).
- The large increase in non-domestic volumes reflects the inclusion of the new commercial arrangements with Telecom Plus that became effective from 1 December 2013.

Executive Summary (continued)

Supply Non-domestic segment (continued)

- Under the old commercial arrangement with Telecom Plus plc, that existed until 30 November 2013, the earnings derived from this were included in the domestic segment. The new arrangement, effective from 1 December 2013, requires the earnings to be included in the non-domestic segment. Please refer to section 10 of the basis of preparation for a detailed explanation of this.
- The underlying trends in the non-domestic segment are similar to those outlined for the domestic segment above. Increased unit costs charged by network and transportation providers, higher environmental/social obligation and indirect costs saw overall EBIT for the non-domestic segment fall by 11.8% to £75m. EBIT margin for the non-domestic supply segment fell to 2% (2013: 2.5%).

Overall Supply segment

- The overall decline in volumes and revenues, combined with increasing network, obligation and indirect costs, saw EBIT for the supply segment fall by 28.6% to £155m (2013: £217m) and the EBIT margin reduce to 2.3% (2013: 3%).

Energy Generation

- RWE's UK conventional power station fleet generated 33.4 TWh of electricity compared to 36.3 TWh in 2013 and 42.4m in 2012. This is a cumulative reduction of 21% in two years.
- In 2014 the conventional generation segment generated a loss at the EBIT level of £(151)m. This reflects the continuing challenges in the UK market which is characterised with very low margins and a steady shift to non-fossil generation.
- In 2014 RWE Generation UK decommissioned 3 power stations removing around 3.7 GW of UK generating capacity. They were all subject to lifetime limitations resulting from the implementation of EU emission regulations for large combustion plant. A further 1.4 GW of capacity will be decommissioned in 2015.
- The conventional generation segment incurred a £(191)m impairment charge against the carrying value of certain assets. This write down is reflective not just of the loss incurred in 2014 but also that margins will remain depressed over the foreseeable future. In addition staff severance costs of £(5)m were incurred in relation to plant closures and ongoing efficiency programmes as the generation segment manages its cost base to reflect the reduced scale of operations going forward. Impairment and severance costs are excluded from the CSS in accordance with Ofgem guidelines. Including these costs, the loss in the conventional generation segment would have been £(347)m.

Overall earnings and capital investment

- The combined EBIT for RWE-UK Generation & Supply (RWE-UK G&S) in 2014 was £37m, a fall of £(201)m compared to the £238m EBIT generated in 2013. Taking into account the £(213)m of severance and impairment losses that are excluded from the CSS the Generation and Supply segments made a loss of £(176)m.
- Against this overall loss making position, capital investment in the RWE-UK conventional Generation and Supply segments totalled £192m in 2014. A further £323m was invested in UK Renewables in 2014. Together that is £515m invested in the UK, equivalent to £96 for every domestic gas and electricity customer served in 2014.

1. Background to the Consolidated Segmental Statement ("CSS")

- On 21 October 2009 the Office of Gas and Electricity Markets ("Ofgem") introduced two licence conditions (Electricity Supply and Gas Supply Licence Condition 19A and Electricity Generation Licence Condition 16B) requiring certain energy companies to publicly report separate financial results for their generation and supply businesses.
- The requirement arose from Ofgem's "Energy Supply Probe" with the objectives of:
  - Providing better transparency on how revenues, costs and profits are earned across the segments;
  - Improving comparability across the industry;
  - Assisting users to interpret the individual company results more clearly.
- The Licence Conditions (LC's) were effective from year ended 31 December 2009. In accordance with the LC's, RWE-UK G&S has prepared and published its CSS for the years ended 31 December 2009 to 2013 and now 2014. These are available to view on the website, www.npower.com.

2. New RWE AG group reporting structure effective from 1 January 2013

- Up to and including 2012, RWE AG managed and reported the UK Generation and Supply businesses as a single "United Kingdom segment" in the RWE AG Annual Report.
- On 1 January 2013 responsibility for steering nearly all RWE AG's conventional power stations across Europe was transferred to RWE Generation SE, a wholly owned subsidiary of RWE AG. All the power stations operated by the Generation segment in the UK (and owned by the RWE Generation UK plc legal entity) became subject to this steering model.
- Following the changes in group reporting structure, the revenues and profits of the UK Generation and Supply businesses are disclosed in the RWE AG Annual Report 2014 as follows:
  - The revenues and operating results of the UK Supply business are disclosed within the segment "Supply United Kingdom" contained on page 177.
  - The revenue from conventional power generation in the UK is disclosed in note 2 to the "Segment reporting Divisions 2014" table on page 177.
  - The operating result from conventional power generation in the UK is disclosed in the "Operating Result" table on page 50.
- The reporting structure of RWE-UK G&S's operations is summarised in section 4 to assist users in understanding how the CSS has been prepared and how it links into the segment disclosures in the RWE AG Annual Report 2014.

3. How RWE-UK G&S are working to improve external confidence and trust in the CSS

3.1 The CSS is prepared from segmental data in the RWE AG Group audited Annual Report

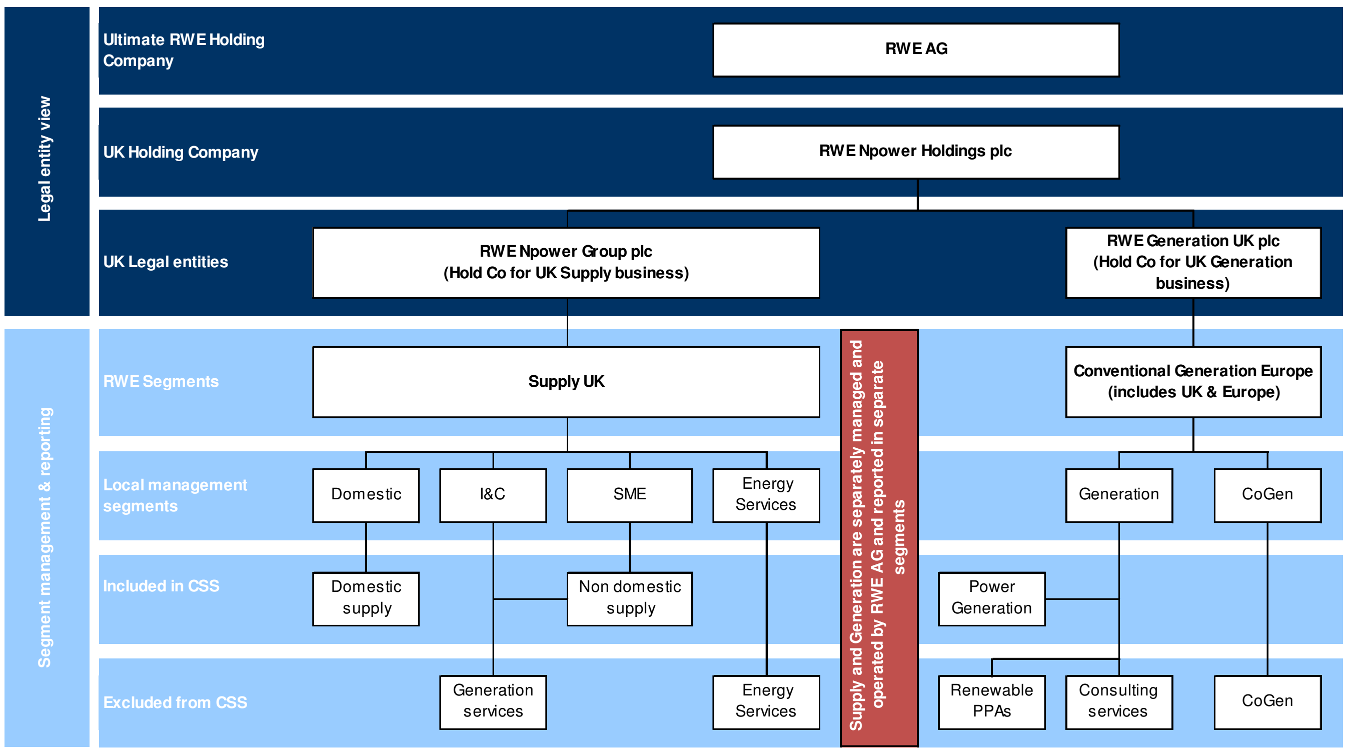
- The RWE-UK G&S CSS is prepared from the underlying UK Generation and Supply revenue and operating profits that are disclosed in the RWE AG Annual Report 2014. The Consolidated Financial Statements of RWE AG are audited by PricewaterhouseCoopers (PwC) Germany under International Standards on Auditing.

3.2 Independent audit of the 2014 CSS by PricewaterhouseCoopers LLP

- In the 2013 CSS, RWE-UK G&S committed to commission an independent audit of the 2014 CSS by an external auditor.
- In accordance with this commitment, which was subsequently made a requirement in the modified Licence Conditions 16B and 19A that became effective on 18 December 2014, the Directors of RWE Npower Holdings plc (the Company) appointed the RWE-UK G&S external auditor, PricewaterhouseCoopers LLP, to perform an audit of the 2014 CSS.
- The report of the independent auditor is included on pages 20 to 21 of the 2014 CSS.

4. RWE-UK G&S legal and management structure

- Detailed below is a summarised, high level view of the legal entity and management and reporting structure of the RWE-UK G&S operations in the UK. From a legal entity perspective the UK conventional generation and supply business are owned by the Company.
- Following the change in the RWE Group steering and reporting structure from 1 January 2013 the UK Supply and Conventional generation businesses are separately managed and steered by RWE AG group (see section 2 above).
- At the UK level the Supply business is organised into four sub-segments being: Domestic; Industrial & Commercial (I&C), Small & Medium Enterprises (SME) and Energy Services.
- The activities that are excluded from the CSS are explained further in sections 5 & 8.



5. Legal entities included in the 2014 CSS

- The CSS includes the revenues and costs attributable to the generation and electricity and gas supply activities of all subsidiaries of the Company that held an electricity generation or an electricity/gas supply licence AND engaged in generation or gas/electricity supply activities during the year ended 31 December 2014.
- A list of the legal entities (all of which are ultimately owned 100% by the Company) which held a generation or supply licence and traded during 2014 are detailed below:

Company registration No	Legal entity	Licences		Business Activities	
		Generation	Supply	Generation	Supply
3892782	RWE Generation UK plc	x	x	Yes	No
3653277	Npower Ltd		x	No	Yes
3768856	Npower Commercial Gas Ltd		x	No	Yes
2999919	Npower Gas Ltd		x	No	Yes
3432100	Npower Northern Ltd		x	No	Yes
3782443	Npower Direct Ltd	x	x	No	Yes
3937808	Npower Yorkshire Ltd		x	No	Yes

- Some of the entities above have trading activities that are excluded from the scope of Ofgem's requirements. These activities are referred to as "out of scope" and the revenues and costs attributable to these activities are excluded from the CSS. Examples of such "out of scope" activities include:
  - Generation Services relating to the provision of consultancy and advice to business customers in the supply segment;
  - Engineering, maintenance and technical consultancy services provided to external business customers of the generation segment;
  - Power Purchase Agreements (PPA's) with affiliated Wind Farm operators.
- The CSS does not include the revenues and costs of subsidiaries or entities that do not hold a generation or gas/electricity supply licence such as:
  - the legal entities that operate Combined Heat and Power plants (the CoGen segment in the diagram in section 4 above);
  - the legal entities that provide energy services such as boiler installation and maintenance to domestic customers, metering services to third parties or electrical/mechanical installation services to the private and public sector (the Energy Services segment in the diagram in section 4 above).
- The CSS does not include subsidiaries of the Company that held either electricity generation or gas/electricity supply licences but which were dormant and had no trading activities during the year ended 31 December 2014.
- Any profit or loss created through RWE Supply & Trading (RWEST) acting on behalf of RWE's supply or generation businesses in the wholesale markets is attributed to the supply or generation business as appropriate.
- In addition the CSS includes the revenues and costs of two joint venture entities that are held by other companies in the RWE AG Group. Information on the two joint venture companies included within the CSS is set out in section 9.

RWE-UK Generation & Supply Consolidated Segmental Statement for the year ended 31 December 2014

Ofgem Consolidated Segmental Statement

- The notes in sections 1-5 above and 6-15 below are integral to gaining a full and proper understanding of the CSS and should be read in conjunction with the statement.
- A full reconciliation between the RWE-UK G&S segment revenue and operating result for year end 2014 (as reported in the RWE AG Annual Report 2014) to the 2014 CSS is presented in section 14 below.

YE 2014 Consolidated Segmental Statement		GENERATION: Electricity Generation: Conventional	GENERATION: Electricity Generation: Renewable	GENERATION: Aggregate Generation	SUPPLY: Electricity: Domestic	SUPPLY: Electricity: Non-domestic	SUPPLY: Gas: Domestic	SUPPLY: Gas: Non-domestic	SUPPLY: Aggregate Supply
Total revenue	**£m**	**1,637**	**136**	**1,773**	**1,688**	**3,448**	**1,330**	**371**	**6,837**
Revenue from sales of electricity and gas	£m	*1,597*	*136*	*1,733*	*1,688*	*3,448*	*1,330*	*371*	*6,837*
Other revenue	£m	*40*	*-*	*40*	*-*	*-*	*-*	*-*	*-*
Total operating costs	**£m**	**(1,612)**	**(48)**	**(1,660)**	**(1,631)**	**(3,386)**	**(1,264)**	**(351)**	**(6,632)**
Direct fuel costs	£m	*(1,048)*	-	*(1,048)*	(682)	(1,922)	(654)	(222)	(3,480)
Direct costs	£m	(329)	(16)	(345)	(642)	(1,297)	(375)	(90)	(2,404)
Transportation costs	£m	*(108)*	*(16)*	*(124)*	*(413)*	*(789)*	*(309)*	*(88)*	*(1,599)*
Environmental & social obligation costs	£m	*(217)*	*-*	*(217)*	*(222)*	*(494)*	*(60)*	*-*	*(776)*
Other direct costs	£m	*(4)*	*-*	*(4)*	*(7)*	*(14)*	*(6)*	*(2)*	*(29)*
Indirect costs	£m	(235)	(32)	(267)	(307)	(167)	(235)	(39)	(748)
WACO F/E/G	£/MWh, p/th	37.87	N/A	N/A	59.40	56.17	65.80	66.20	N/A
EBITDA	**£m**	**25**	**88**	**113**	**57**	**62**	**66**	**20**	**205**
Depreciation and amortisation	£m	(176)	(55)	(231)	(23)	(6)	(20)	(1)	(50)
EBIT	**£m**	**(151)**	**33**	**(118)**	**34**	**56**	**46**	**19**	**155**
Volume	TWh, MThms	33.4	1.3	N/A	11.5	34.2	994.1	335.8	N/A
Customer numbers	000s	N/A	N/A	N/A	3,128	361	2,202	52	5,743
EBIT Margin		**(9.2%)**	**24.3%**	**(6.7%)**	**2.0%**	**1.6%**	**3.5%**	**5.1%**	**2.3%**
Supply Total Domestic EBIT Margin									**2.7%**
Supply Total Non-domestic EBIT Margin									**2.0%**

2014 EBIT including severance and impairment costs		GENERATION: Electricity Generation: Conventional	GENERATION: Electricity Generation: Renewable	GENERATION: Aggregate Generation	SUPPLY: Electricity: Domestic	SUPPLY: Electricity: Non-domestic	SUPPLY: Gas: Domestic	SUPPLY: Gas: Non-domestic	SUPPLY: Aggregate Supply
2014 EBIT per CSS	**£m**	**(151)**	**33**	**(118)**	**34**	**56**	**46**	**19**	**155**
Severance Costs[1]	£m	(5)	-	(5)	(5)	(3)	(5)	(1)	(14)
Impairment	£m	(191)	(3)	(194)	-	-	-	-	-
2014 EBIT incl severance & impairment costs	**£m**	**(347)**	**30**	**(317)**	**29**	**53**	**41**	**18**	**141**
EBIT Margin		**(21.2%)**	**22.1%**	**(17.9%)**	**1.7%**	**1.5%**	**3.1%**	**4.9%**	**2.1%**
Supply Total Domestic EBIT Margin									**2.3%**
Supply Total Non-domestic EBIT Margin									**1.9%**

Note 1: Severance costs have been allocated across the various supply segments on the same basis as indirect overheads and costs as described in section 12.4.

Note 2: See Appendix on page 19 for Glossary of terms and summarised 2013 CSS.

Basis of preparation

- The following notes on pages 8 to 15 provide a summary of the basis of preparation of the 2014 CSS.

6. Basis of preparation of the Consolidated Segmental Statement for the year ended 31 December 2014

- The 2014 CSS is organised into two main segments being Generation and Supply. These main segments are then organised into six sub segments being conventional generation, renewable generation, domestic electricity supply, non-domestic electricity supply, domestic gas supply and non-domestic gas supply.
- The 2014 CSS has been prepared by RWE-UK G&S in accordance with the modified Licence Conditions 16B & 19A that became effective from 18 December 2014. These require the CSS to be prepared from and "reconciled with audited figures (prepared under International Financial Reporting Standards ("IFRS")) published in group accounts".
- The financial results of RWE-UK G&S are fully reflected in the consolidated financial statements of its ultimate parent company, RWE AG, which are prepared under IFRS and subject to independent external audit.
- In section 14 RWE-UK G&S have presented a complete reconciliation between the Generation and Supply segment revenues and earnings before interest and tax, as reported in the CSS, to the UK Generation and Supply revenues and operating result disclosed in the 2014 RWE AG Annual Report which can be found by following the link below:

  http://www.rwe.com/web/cms/mediablob/en/2696788/data/110822/6/rwe/investor-relations/reports/RWE-Annual-Report-2014.pdf

7. Transfer pricing between the segments and with the rest of the RWE AG Group

- The Generation segment sells capability to the UK branch of RWEST via an asset tolling agreement. This arrangement is explained in detail in section 11.1.1. The Supply segment sources its wholesale commodity requirements for power and gas from RWEST in the UK. This arrangement is explained in detail in section 12.2.
- There are no specific wholesale energy supply agreements between the Generation and Supply segment.
- Both the Generation and Supply segments receive and provide central support services to each other and also to and from other divisions of the RWE AG Group. These are mainly support services and functions such as IT, HR, Transactional Accounting, Tax and Internal Audit.
- In accordance with RWE AG Group policy, the arrangements specified above are "arm's length". This means the price which independent third parties would have agreed with each other under comparable business conditions.
- There have been no changes to transfer pricing policies and procedures in 2014.

Basis of preparation

8. Financial items excluded from the CSS

- Ofgem has published Guidelines on preparing the CSS to ensure consistency and comparability across the respective CSS's of the industry.
- Paragraph 1.6 of the Guidelines sets out examples of financial items that Ofgem would expect to be excluded from the CSS. These include:
  - Mark to market adjustments;
  - Profits or losses on disposals;
  - Restructuring costs that have been classified as such in the Group's annual report. The classification of costs as non-operating is governed by a RWE AG Corporate Business Rule (CBR). To the extent that costs meet the definition of non-operating as set out in the CBR they are excluded from arriving at the operating result of the UK Generation and Supply segments in the RWE AG Annual Report. Likewise these non-operating costs are excluded from the CSS in accordance with the Ofgem guidelines; and
  - Impairment charges.
- Non-operating costs excluded from the 2014 CSS in accordance with the Ofgem guidelines were:
  - Employee severance costs of £5m and £14m in the Generation and Supply segments respectively;
  - Plant and land impairment costs of £191m in the Conventional Generation segment.
- Although these non-operating items are excluded from the CSS in accordance with Ofgem guidelines they represent real costs incurred by the segments in managing their operations. To aid transparency and understanding a supplementary table has been included on page 7 that shows the impact on the reported CSS EBIT of including these non-operational costs. This provides users with a complete picture of the EBIT of the Generation and Supply segments.
- A complete reconciliation between the Generation and Supply segment revenues and earnings before interest and tax, as reported in the CSS, to the UK Generation and Supply revenues and operating result disclosed in the 2014 RWE AG Annual Report has been set out in section 14. A full description is provided of the financial items that were included in the operating result but excluded from the CSS to ensure compliance with the Ofgem guidelines above.

Basis of preparation

9. Affiliates Joint Ventures (JV's) included in the CSS

- RWE-UK G&S has no joint venture arrangements, therefore there are no joint ventures that should be included in the CSS.
- An affiliate company, RWE Innogy (UK) Ltd, has two joint venture interests in offshore wind farms which hold a generation licence and are engaged in generation activities.
- Although RWE Innogy (UK) Ltd does not form part of RWE UK G&S it is treated as an "Affiliate" for the purposes of the CSS.
- Accordingly, RWE Innogy (UK) Ltd's share of the revenues, costs and operating result in the two JV wind farms is included in the Generation segment of the CSS in accordance with paragraph 5 of the modified LC's. The details of the two JV's and the proportionate share of the results reflected in the CSS are as follows:
  - 50% of the operating result of Greater Gabbard Offshore Winds Ltd (company registered number: 04985731).
  - 60% of the operating result of Gwynt Y Mor Offshore Wind Farm Ltd (company registered number: 03697015). Due to the commercial arrangements in place this includes the operating result of RWE Innogy GYM 1 Ltd, RWE Innogy GYM 2 Ltd, RWE Innogy GYM 3 Ltd and RWE Innogy GYM 4 Ltd, (company registered numbers: 07233484, 07233494, 07233487 and 07233491).
- The proportionate share of the RWE Innogy (UK) Ltd interest in the JV's are reflected in the Renewables column in the CSS. Operating result is defined as the earnings before interest and tax.
- RWE Innogy (UK) Ltd and other RWE AG entities own interests in UK wind farms and generation plant that do not hold a generation licence. In accordance with the Ofgem guidelines for preparing the CSS the revenues and costs of the entities that own these power stations are not included in the CSS.

10. Change in disclosure of commercial arrangements with Telecom Plus plc

- On 20 December 2013 the Supply segment sold its 100% interest in Electricity Plus Supply Ltd (EPS) and Gas Plus Supply Ltd (GPS) to Telecom Plus plc (trading as Utility Warehouse) effective from 1 December 2013.
- GPS and EPS held gas and electricity supply licences and at the time of the sale supplied c.770k customers who had signed up for Utility Warehouse's bundled utility offering combining telephone, mobile, broadband and TV services.
- The revenues and costs under the commercial arrangements that existed up to the date of sale were recorded in the domestic segment of the 2013 CSS (and prior years). This is because the customers were supplied by a licensed entity owned by the supply segment.
- Following the sale of GPS and EPS (along with the respective electricity and supply licences) to Telecom Plus plc, the Supply segment no longer owned these customers. Accordingly no revenues or costs are shown in the supply segment in respect of the customers acquired by Telecom Plus.
- Prior to the sale of the two entities, the Supply segment entered into a 20 year energy supply agreement with GPS and EPS to fulfil their requirements for power and gas. From this point the revenues and costs associated with supplying power and gas to Telecom Plus plc are recorded in the non-domestic segment. This change is necessary to comply with the Ofgem guidelines as, under the new commercial arrangements, this is a supply of gas and power to a business (Telecom Plus plc) customer.

Basis of preparation

11. Generation segment

11.1.1 Overview of asset tolling arrangement

- RWE-UK G&S gas and coal power stations sell capability to the UK branch of RWEST via an arm's length asset tolling agreement. This means the price which independent third parties would have agreed with each other under comparable business conditions. In exchange for a capability fee, the asset tolling agreement provides RWEST in general with the option to deliver gas and coal to our power stations and have this converted into electricity. The initial fee is based on the option value derived from a combination of the forward markets at the time of the capability transfer together with back-tested and benchmarked option models. Transfer typically takes place 3 years ahead of generation.
- RWEST maintains a series of ring-fenced commercial asset optimisation trading books associated with the commercial management of these power station options and has an obligation to maximise and optimise the realised value of these books for the benefit of the Generation segment. All trading within these books on behalf of the Generation segment is backed by the assets and as such there is no speculative trading activity that takes place. The difference between the forward option value for the power station options and the value achieved by RWEST in these ring-fenced books is returned to the Generation segment as an adjustment to the initial capability fee.
- Our oil power stations (whilst making up a far smaller proportion of our fleet) are run on a different basis to the gas and coal power stations. The revenue represents the sale of electricity rather than a transfer of capability, however, the cost of oil procured and consumed for generation is netted off against revenue. RWEST still manage the positions in respect of the oil power stations and will seek to optimise them in respect of market conditions and plant availability, again passing any gains or losses in respect of this back to the Generation segment. RWEST received a management fee of circa £7m in 2014 (£6m in 2013) for managing this optimisation activity for the main Generation fleet. This fee is shown as part of our operating costs.

11.1.2. Change in basis of disclosing Generation revenue and fuel costs in the CSS

- The impact of the arrangements described in 11.1.1 above is that the revenue reported for the Generation segment in the 2014 RWE AG Annual Report is as follows:
  - Gas and coal stations. The reported revenue in the RWE AG Annual Report is the value of the initial capability payment plus any subsequent adjustment arising from optimisation. This is the gross margin of the capability transferred (net of fuel and carbon costs, including carbon price support tax).
  - Oil. The reported revenue in the RWE AG Annual Report is the gross margin after netting off the cost of fuel purchased and consumed for the volume generated.
- The revenue reported in the RWE AG Annual Report is therefore the gross margin and reflects the underlying contractual arrangements in place. However, this makes comparisons of the revenue and gross margin with other companies (who operate alternative trading models) difficult.
- Therefore to assist comparability with other companies an adjustment has been made to increase the revenue line by £1,048m. At the same time direct fuel costs have been increased in the CSS by the exact same amount (see section 14).

Basis of preparation

11.1.2 Change in basis of disclosing Generation revenue and fuel costs in the CSS (continued)

- The effect of these two management adjustments is to state revenue on a gross basis and therefore assist users in making comparisons with industry peers. Likewise in comparing direct fuel costs. The two adjustments net off to zero and have no impact on the reported EBIT in the CSS.

11.1.3 Renewable stations

- Also included within revenue from sale of electricity and gas is RWE Innogy (UK) Ltd's share of revenues from Greater Gabbard Offshore Winds Ltd and Gwynt Y Mor Offshore Wind Farm Ltd.
- Other elements included are ancillary services and balancing mechanism income.

11.1.4 Other revenue

- The balance of £40m in other revenue relates to ancillary services.
- Other revenue excludes earnings of £18m arising from the sale of power to RWEST. This power has been procured under long term Power Purchase Agreements (PPA's) with affiliated Wind farm operators and is then sold to RWEST at market prices under an arm's length arrangement. The earnings arise from the difference between the long term fixed price of the power under the PPA's to the prevailing market price at the time of sale to RWEST.
- The 2013 CSS included £24m of earnings in respect of these PPA's so as to provide users of the CSS with a complete picture of the Generation segment's trading arrangements with RWEST. However, these transactions are technically out of scope of the CSS as they do not form part of the licensed activities of the generation business and therefore have been excluded in 2014.

11.2 Direct fuel costs

- Overview of arrangements with RWEST:
  - Gas and coal. As described in section 11.1.1 above, under the asset tolling agreement operated in the UK, the Generation business does not procure gas, coal or biomass. However, the profits and losses of the UK gas and coal procurement activities managed by RWEST are accounted for in the Generation business.
  - Oil. The fuel is charged to the Generation P&L account as and when the fuel is burned at the power plants, and recognised within revenue in the CSS as a component of the overall spread earned from the power generated.
- In accordance with these commercial arrangements the company does not recognise any fuel costs as these are correctly netted off the revenue line which is effectively the gross margin (spread) achieved. RWE-UK G&S recognise that this is unhelpful for users of the CSS who are trying to draw comparisons with other industry peers who operate a different trading model. Therefore, as described in 11.1.2 above, an adjustment of £1,048m has been applied to the direct fuel costs (and a corresponding increase in the revenue line) so as to aid users of the CSS in making meaningful comparisons across the industry. The basis of determining this adjustment is set out in section 11.5 below.
- In summary the direct fuel costs comprise £1,048m being the adjustment to gross up revenue and direct fuel costs as described in section 11.1.2 above (see section 14).

Basis of preparation

11.3 Direct costs

- Direct costs for Generation are made up of transportation costs, environmental and social obligation costs and other direct costs.
- Transportation costs include network costs and Balancing Services Use of System Charges (BSUoS).
- Environmental and social obligation costs relate to EU ETS carbon emission costs and carbon tax.
- Other direct costs include market participation costs.

11.4 Indirect costs

- These comprise of directly attributable station operating and maintenance costs and the Generation segment's share of common costs. The basis of allocation of these common costs across the segments is described in section 13 below.
- In the CSS up to and including 2013 profits or losses on the sale of assets used or deployed in the Company's operational activities were included in the CSS as these were considered to be part of the normal trading activity of the business.
- The 2014 CSS excludes profits or losses arising from all sales of assets regardless of whether the assets were directly involved in the licensed operations of the generation segment or not in line with Ofgem guidelines.

11.5 Weighted average cost of fuel (WACOF)

- As described in section 11.1.1 above our Generation business operates a tolling arrangement and as a result does not directly procure gas, coal or biomass. Therefore, in order to comply with the LC's a notional WACOF has been derived as described below.
- Fuel volumes consumed to generate power have been determined at the "point of burn".
- Costs of fuel have been derived as follows:
  - Coal, biomass and oil costs are based on the average weighted cost of the fuel procured by RWEST and transferred to the Generation segment as and when consumed at the power plant.
  - Gas cost is based on the market prices at the time of exercise of the option by RWEST.
  - Carbon cost is based on the total cost of all certificates procured to surrender against emissions generated.
  - Carbon Price Support tax cost is based on the UK Governmental published rates.
- On the basis of the methodology set out above the total notional derived fuel cost is £1,265m and comprises:
  - £217m of purchased carbon allowances as required under the EU Emission Trading Scheme (EU ETS) for carbon dioxide (CO_2). These were classified as a direct cost in the RWE AG Annual report.
  - £1,048m being the adjustment to gross up revenue and direct fuel costs as described in section 11.1.2 above (see section 14).
- The notional WACOF is £37.9 per MWh based on total generation volumes of 33.4 TWh. This is calculated by dividing the total derived cost of fuel by the total generation volumes.

Basis of preparation

12. Supply segment

12.1 Revenue from sale of electricity and gas

- Revenue comprises the sale of electricity and gas to our domestic and non-domestic energy customers and is stated net of VAT. Government mandated social tariffs and discounts, such as the Warm Home Discount, and other social discounts, have also been deducted from revenue.

12.1.2 Other revenue

- The Supply segment has no “other revenues” arising from licensed activities. Other revenues comprise of non-licensed activities and therefore treated as out of scope for the purposes of the CSS.

12.2 Direct fuel (electricity and gas) costs

- Direct fuel costs reflects the costs of procuring electricity and gas to meet customer requirements, as well as losses, the energy element of reconciliation by difference costs, balancing and shaping costs. All of the direct fuel costs are included in the calculation of weighted average cost of electricity/gas (WACO E/G).
- These costs are captured at source between gas and electricity and then analysed between domestic and non-domestic based on the specific demand characteristics of the customer base. The weighted average cost differs between domestic and non-domestic because of different hedging approaches, in particular for flexible risk management products.
- Our supply business fulfils its wholesale commodity requirements via RWEST on an arm’s length basis. This means the price which independent third parties would have agreed with each other under comparable business conditions. RWEST received a management fee of £2.4m in 2014 (£2.7m in 2013) for this service. All of our licenced activities procure their electricity or gas in this fashion.

12.3 Direct costs

- Direct costs for Supply are broken down into transportation costs, environmental and social obligation costs and other direct costs.
- Transportation costs include all network costs, gas transportation costs (including the transport element of reconciliation by difference which is included in the segment to which the supply relates) and BSUoS charges. Transportation costs are primarily allocated directly to the customer segment and fuel type to which they relate. The information flows received from the industry processes specifically identify the customer segment and fuel type via the identifier, in the case of electricity costs, or the shipper, in the case of gas costs.
- Environmental & social obligation costs for domestic supply include Renewable Obligations Certificates (ROCs), Energy Company Obligation (ECO) and Feed in Tariff (FIT) costs. Non-domestic supply includes the costs of Levy Exemption Certificates (LECs), ROCs and FIT.
- FIT costs are allocated based on the segment in which the feed in tariff customers reside. ROCs are allocated to segments in proportion to respective customer meter volumes.
- ECO costs are specific to the domestic segment and allocated between domestic gas and electricity customers based on customer numbers.
- Other direct costs include brokers’ costs, sales commissions and any wider Smart metering programme costs.

Basis of preparation

12.4 Indirect costs comprise:

- Indirect costs for Supply include operating costs such as sales and marketing, bad debt, cost to serve, billing and metering costs and IT & staff costs.
- Costs that are directly attributable to a segment are charged to that segment in the CSS.
- Customer service costs (such as billing, customer service and metering) are allocated across the segments based on relevant drivers depending on their nature. These drivers include customer numbers, meter points, and number of customer gains and losses.
- Overheads and costs which are not directly attributable to supply segments are allocated between the domestic, non-domestic, gas and electricity segments in proportion to the indirect costs that are directly attributable from an activity based costing (ABC) methodology.

12.5 Supply volumes

- These are at the customer meter point (i.e. net of losses) and include estimates for supply between the last meter read and 31 December 2014.

12.6 Supply customer numbers

- For both domestic and business segments the customer numbers are based on the average number of distinct meter points (MPANs for electricity and MPRNs for gas).

13. Common costs between Generation and Supply

- Up to and including year end 2012 RWE AG managed and reported its UK Generation and Supply businesses as a single consolidated segment. With effect from 1 January 2013 (see section 2 above) the UK Generation business is overseen by and reported as part of RWE Generation SE along with the majority of RWE AG's conventional power stations across Europe. As a consequence of this the UK businesses were reported as follows in the 2014 RWE AG Annual Report:
  - A specific segment capturing the supply activities of the UK business;
  - A segment relating to the pan European Generation business (with separate disclosure of the UK Generation revenue and operating result).
- As part of the programme to prepare for the new segmental structure, a detailed analysis was performed of the activities and services provided by the UK shared corporate functions in 2012 (such as Finance, Legal, HR, Procurement, Risk Management, Internal Audit and Tax) to support the respective Supply and Generation businesses. This involved a bottom up analysis of the time spent by each function supporting each business which in turn provided a detailed and accurate assessment of how the shared corporate costs for 2012 should be allocated between the UK Supply and Generation segments. It is this detailed assessment that determined the allocation of the shared costs in both the 2014 CSS and the 2014 operating result (as disclosed in the RWE AG Annual Report 2014) between the respective segments.

14. Reconciliation of Generation and Supply revenue and operating result for year end 2014 as reported in the RWE AG Annual Report 2014 to revenue and EBIT per the 2014 CSS

Reconciliation of Revenue and Operating Result ('OR') in RWE Annual Report to Revenue and EBIT in Ofgem CSS	Currency	Operating Result (OR)[i]				Segmental Revenue		
		Generation segment OR [iv]	Supply segment OR [iii]	Total OR [ii]		Generation segment[vi]	Supply segment[vii]	Total Revenue[v]
OR / Revenue (in Euros) as published in RWE Annual Report 2014	€m	(384)	227	(157)		814	9,320	10,134
Average exchange rate [viii]	£1 GBP =	€ 1.245	€ 1.245	€ 1.245		€ 1.245	€ 1.245	€ 1.245
OR / Revenue (translated to GBP) as per RWE Annual Report	£m	(309)	183	(126)	a	653	7,485	8,138
EBIT / Revenue per YE 2014 Ofgem Consolidated Segmental Statement [ix]	£m	(118)	155	37	b	1,773	6,837	8,610
Variance	£m	191	(28)	163	= b-a	1,120	(648)	472
Reconciled as follows:	**Notes**							
Remove "Out of Scope" activities/transactions	1	1	(29)	(28)		(63)	(653)	(716)
Remove PPAs with affiliated windfarms	2	(18)	-	(18)		(74)	-	(74)
Include operating result from affiliate's JV interests	3	32	-	32		136	-	136
Items specifically excluded from the CSS as required by Ofgem guidelines	4	191	1	192		-	-	-
Reclassification between revenue and costs for the CSS	5	-	-	-		73	5	78
Remove one-off transactions	6	(15)	-	(15)		-	-	-
Gross up of Generation Revenue	7	-	-	-		1,048	-	1,048
Total Variance	£m	191	(28)	163	= b-a	1,120	(648)	472

Notes

i - Operating result (OR) = EBITA (earnings before interest, taxation and non-operating amortisation).

ii - 2014 Operating result of the total United Kingdom segments being the sum of the Supply and Generation segments in the United Kingdom.

iii - 2014 Operating result of the United Kingdom Supply segment as per Page 177 of RWE AG Annual Report 2014.

iv - 2014 Operating result of the United Kingdom Generation segment as per Page 50 of RWE AG Annual Report 2014 (excludes Renewables).

v - 2014 Revenue of the total United Kingdom segments being the sum of the Supply and Generation segments in the United Kingdom.

vi - Generation revenue from power generation in the United Kingdom as per Page 177 of the RWE AG Annual Report 2014.

vii - 2014 Supply revenue of the United Kingdom as per Page 177 of the RWE AG Annual Report 2014.

viii - Please refer to foreign currency translation statement on Page 128 of RWE AG Annual Report 2014.

ix - Year end 2014 CSS per page 7 of this document.

14. Reconciliation of Generation and Supply revenue and operating result – explanatory notes

1. Removal of revenue and operating result of "out of scope" activities and entities that do not hold a generation or supply licence (see section 5). This includes:
   - Generation Services activities that relate to the provision of consultancy and advisory services to business customers in the supply segment;
   - Engineering, maintenance and technical consultancy services provided to external business customers of the generation segment;
   - The results of legal entities that operate Combined Heat and Power plants and which do not hold generation licences;
   - The results of legal entities that provide energy services such as boiler installation and maintenance to domestic customers, metering services to third parties or electrical / mechanical installation services to the private and public sector.
2. Removal of Power Purchase Agreements (PPA's) with affiliated Wind Farm operators.
3. Inclusion of the share of the revenue and operating profit of RWE Innogy (UK) Ltd's joint venture interest in (see section 9):
   - Greater Gabbard Offshore Winds Ltd.
   - Gwynt Y Mor Offshore Wind Farm Ltd.
4. Removal of impairments and unrealised mark to market adjustments that are specifically excluded from the CSS as required by the Ofgem guidelines.
5. Reclassification of revenue and costs in the CSS. This is purely a reclassification with no impact on EBIT.
6. Removal of transactions that do not arise from the ongoing activities of RWE-UK G&S operations or relate to periods prior to the publication of the 2009 CSS.
7. £1,048 million in relation to grossing up of Generation revenue and direct fuel costs (see section 11).

15. Business function template

• Prepared in accordance with Annex 2 of the Ofgem Guidelines.

Business function	Generation	Supply	Another part of the business	Notes
Operates and maintains generation assets	√	-	-	
Responsible for scheduling decisions	P/L	-	F	i
Responsible for interactions with the Balancing Market	P/L	P/L	F	ii
Responsible for determining hedging policy	P/L	√	F	iii
Responsible for implementing hedging policy / makes decisions to buy/sell energy	P/L	√	F	iii
Interacts with wider market participants to buy/sell energy	P/L	P/L	F	iv
Holds unhedged positions (either short or long)	P/L	√	F	v
Procures fuel for generation	P/L	-	F	vi
Procures allowances for generation	P/L	-	F	i
Holds volume risk on positions sold (either internal or external)	P/L	√	F	vii
Matches own generation with own supply	P/L	P/L	F	viii
Forecasts total system demand	-	-	F	ix
Forecasts wholesale price	-	√	F	x
Forecasts customer demand	-	√	-	
Determines retail pricing and marketing strategies	-	√	-	
Bears shape risk after initial hedge until market allows full hedge	P/L	√	F	xi
Bears short term risk for variance between demand and forecast	-	√	F	xii

Key

√ : Function resides and profits/losses recorded in segment
P/L : Profit/losses of function recorded in segment
F : Function resides
\- : Neither function nor profit/losses reside in segment

i - Carried out on behalf of RWE-UK Generation by RWEST.

ii - Carried out on behalf of RWE-UK G&S by RWEST.

iii - The overarching hedging and risk management principles are determined by RWE AG. The Supply segment determines its own specific hedging strategy and how this is implemented (taking into account the principles set by RWE AG) and uses RWEST as a route for the transactions. For the Generation segment the hedging policy is implemented and transacted on its behalf by RWEST (again reflecting the overarching principles established by RWE AG).

iv - External commodity transactions are carried out by RWEST on behalf of RWE-UK G&S.

v - Hedging of Generation positions is carried out by RWEST on behalf of RWE-UK Generation. The Supply business manages its own decisions in line with RWE AG policy using RWEST as a route for the transactions.

vi - Please refer to sections 11.1, 11.2 and 11.5 above.

vii - In the short term market this is carried out by RWEST on behalf of RWE-UK G&S. In other periods, RWE-UK Supply manage the risk themselves and RWEST manage the risk on behalf of Generation.

viii - Commercial management of Supply and Generation performed separately by Supply business and RWEST respectively. The vast majority of volumes are transacted externally.

ix - Total system demand at a UK level is observed but is not a direct input into the optimisation of the Supply or Generation segments.

x - Long term views of wholesale prices are produced by RWE AG, medium term by the Supply business (aligned with RWE AG forecast), and shorter term forecasts by RWEST.

xi - RWEST manages shape risk for Generation, and the Supply business manages this risk themselves.

xii - The Supply business manages this risk until within-day when it is managed by RWEST based on RWE-UK G&S forecasts. All profits/losses sit within Supply.

Appendix 1 – Glossary of terms

WACO F/E/G The weighted average cost of fuel, electricity and gas is calculated by dividing direct fuel costs by volumes.

EBITDA Earnings before interest, tax, depreciation and amortisation, calculated by subtracting total operating costs from total revenue.

EBIT Earnings before interest and tax calculated by subtracting depreciation and amortisation from EBITDA.

EBIT Margin EBIT profit margin expressed as a percentage, calculated by dividing EBIT by total revenue and multiplying by 100.

Volume Volumes for the Supply business segments are supplier volumes at the meter point i.e. net of losses. Generation volume is the final metered volume of power that can actually be sold in the wholesale market, i.e. after losses up to the point where electricity is received under the Balancing and Settlement Code.

Appendix 2 – 2013 summarised CSS (unaudited)

		GENERATION	SUPPLY				
2013 Summarised CSS		Total Generation	Electricity		Gas		Aggregate Supply
			Domestic	Non-domestic	Domestic	Non-domestic	
Total revenue	£m	2,327	2,063	3,180	1,781	177	7,201
EBIT	£m	21	110	90	22	(5)	217
EBIT Margin		0.9%	5.3%	2.8%	1.2%	(2.8%)	3.0%
Supply Total Domestic EBIT Margin							3.4%
Supply Total Non-domestic EBIT Margin							2.5%
WACO F/G/E		46.20	61.10	55.81	73.3	72.2	N/A

		GENERATION	SUPPLY				
2013 EBIT including non-operating costs		Total Generation	Electricity		Gas		Aggregate Supply
			Domestic	Non-domestic	Domestic	Non-domestic	
EBIT (as above)	£m	21	110	90	22	(5)	217
Severance Costs	£m	(44)	(16)	(4)	(14)	(1)	(35)
Impairment	£m	(35)	-	-	-	-	-
EBIT incl non-operating costs	£m	(58)	94	86	8	(6)	182
Supply Total Domestic EBIT Margin							2.6%
Supply Total Non-domestic EBIT Margin							2.4%

- 2013 revenues for Domestic Electricity Supply have been restated from £2,091m to £2,063m. This restatement is to deduct government mandated social tariffs and discounts, and other social discounts (previously shown within direct costs), and have been made to be consistent with the new Ofgem presentation requirements for 2014.
- Other than these adjustments, the 2013 summarised CSS has been extracted from the unaudited CSS for 2013 which was subject to certain agreed upon procedures by PricewaterhouseCoopers LLP.

Independent auditor's report to the Directors of RWE Npower Holdings Plc and its Licencees

We have audited the accompanying statement (the 'Consolidated Segmental Statement' or 'CSS') of RWE Npower Holdings Plc and its Licencees (as listed in footnote ii) as at 31 December 2014 in accordance with the terms of our agreement dated 19 December 2014. The CSS has been prepared by the Directors of RWE Npower Holdings Plc and its Licencees based on the requirements of Ofgem's Standard Condition 19A of the Gas and Electricity Supply Licences and Standard Condition 16B of the Electricity Generation Licences (together, the 'Licences') and the basis of preparation on page 8.

Directors' responsibility

The Directors are responsible for the preparation of the CSS in accordance with the Licences and the basis of preparation on page 8 and for maintaining the underlying accounting records and such internal control as the Directors determine is necessary to enable the preparation of the CSS that is free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the CSS based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the CSS is free from material misstatement. The materiality level that we used in planning and performing our audit is set at £18m for each of the following segments:

- Aggregate Generation
- Supply – Electricity Domestic
- Supply – Electricity Non-Domestic
- Supply – Gas Domestic
- Supply – Gas Non-Domestic

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the CSS. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the CSS, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the CSS in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the CSS.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion the attached CSS of RWE Npower Holdings Plc and its Licencees as at 31 December 2014 is prepared, in all material respects, in accordance with:

- the requirements of Ofgem's Standard Condition 19A of the Gas and Electricity Supply Licences and Standard Condition 16B of the Electricity Generation Licences established by the regulator; and
- the basis of preparation on page 8.

Independent auditor's report to the Directors of RWE Npower Holdings Plc and its Licencees (continued)

Basis of Accounting and Restriction on Distribution

Without modifying our opinion, we draw attention to page 8 of the CSS, which describes the basis of preparation. The CSS is prepared in order for RWE Npower Holdings Plc and its Licencees to meet the Licence requirement of the Regulator Ofgem rather than in accordance with a generally accepted accounting framework. The CSS should therefore be read in conjunction with both the Licences and the basis of preparation on page 8. This basis of preparation is not the same as segmental reporting under IFRS and /or statutory reporting. As a result, the schedule may not be suitable for another purpose.

This report, including our conclusions, has been prepared solely for the Board of Directors of RWE Npower Holdings Plc and its Licencees in accordance with the agreement between us, to assist the Directors in reporting on the CSS to the Regulator Ofgem. We permit this report to be disclosed on the website www.npower.com, to enable the Directors to show they have addressed their governance responsibilities by obtaining an independent assurance report in connection with the CSS. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Board of Directors and RWE Npower Holdings Plc and its Licencees for our work or this report except where terms are expressly agreed between us in writing.

PricewaterhouseCoopers LLP

London

28 April 2015

i) The maintenance and integrity of this website is the responsibility of the Directors of RWE Npower Holdings Plc; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the CSS since it was initially presented on the website.

ii) Licence holders: Supply licence holders (Npower Ltd, Npower Commercial Gas Ltd, Npower Gas Ltd, Npower Northern Ltd and Npower Yorkshire Ltd). Generation licence holders (Gwynt Y Mor Offshore Wind Farm Ltd and Greater Gabbard Offshore Winds Ltd). Supply and Generation licence holders (RWE Generation UK plc and Npower Direct Ltd).