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Andrew Ryan
Head of Regulatory Finance Policy
Ofgem
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Our ref

Your ref

Date

27 January 2022

Dear Andrew

Statutory Consultation on licence modifications relating to Last Resort Supply Payment (LRSP) claim process

I am writing on behalf of Western Power Distribution (South Wales) plc, Western Power Distribution (South West) plc, Western Power Distribution (East Midlands) plc and Western Power Distribution (West Midlands) plc in relation to the above consultation letter issued on 30 December 2021.

We have been working with Ofgem via the Electricity Network Association to facilitate the Last Resort Supply Payment claim process. We are conscious of the very short timescale available to industry parties to reach a conclusion on funding the recently submitted Supplier of Last Resort (SOLR) levy claims, for which a derogation has been granted to allow for the full recovery of these amounts through an adjustment to our 2022/23 network charges.

We understand that GEMA has now agreed to adopt "Plan B", subject to some clarifications from a third party financing provider, which would delay the recovery of these claims.

We would expect GEMA to have considered very carefully the merits of delaying the impact on customers' bills via a third party financing arrangement which may result in additional risks and costs to a number of parties. We note that this may impact customers overall via "*adjustments for interest and other payments as the Authority may direct*". In line with the Authority's general duty to protect the interests of existing and future consumers, GEMA should ensure that the least cost option is adopted, and financing costs are minimised.

We agree with the drafting points highlighted in the collective response submitted by the Electricity Networks Association and also have some additional comments to make. In principle we are supportive of arrangements agreed by industry parties and financial institutions.

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We welcome the development of the distribution licence modification to provide the level of clarity that satisfies all parties and will enable such an arrangement to exist. In addition to the ENA letter, please note the following comments:

(a) Enduring Solution

We recognise that this has been an expedited process and further consideration needs to be given as to whether this is an enduring solution or whether amendments are required to ensure this process could potentially be used in the future should a need arise. It must be recognised that bringing in a third party into this process could add additional complications and risk.

The proposed licence modifications drafts this as an enduring solution and we do not object to this in principle but we do believe that introducing such complex arrangements as enduring solutions requires a much more detailed and thorough risk assessment than that which is currently being undertaken due to time constraints.

(b) Liability to Pay Claims

We note that no reference is made in the proposed licence modifications with regards to the fact that, for claims exceeding the materiality threshold, the networks will not be liable to pay claims to an original SoLR or a permitted assignee until the corresponding increase to Distribution Use of System ("DUoS") charges becomes billable. We can be comfortable with this not being explicitly stated in the licence but we would expect this to be clearly stated and published in the Ofgem's policy statement or in any other relevant public documentation.

A set of words has been proposed which we support "the liability for the licensee will not crystallise until the particular Regulatory Year at such time as the corresponding increase to the Use of System Charges becomes billable by the licensee".

We would also like to note that the licence modification drafting should be clear in stating that in all situations and circumstances, payment of a valid claim to an LRSP permitted assignee discharges any requirement to pay the amount to the related original claimant/electricity supplier.

(c) Forecast Claim Payments

If due to the financing arrangements, or changes made to it, DNOs are put in an over recovery position through no fault of their own, we do not expect penalty interest to be applied. We request that Ofgem confirms in the policy statement that it would agree that interest would be applied at 1.5% if this is the case as per CRC2A.19.

Ofgem should also specify in the policy statement the time period over which third party payments will be made so that both suppliers and networks can forecast the impact on their prices.

We have previously expressed concerns about the potential for price volatility in 2025/26 and 2026/27 if prices are set on a 15 month notice period based on non-final allowed income figures potentially resulting in large K factors for these two years of the price control period.

(d) RIIO-ED2 Derogations and Pass Through arrangements

The proposed modifications to the distribution licence would extend the SOLR recovery period from 2022/23 into the ED2 period. We request that Ofgem confirms in a policy statement that the pass-through arrangements and necessary derogations will be extended into the ED2 period.

(e) ED2 Change in Corporate Tax Rate

WPD are keen to initiate further discussions with Ofgem to ensure that any tax impact for the networks, resulting from a corporate tax change rate in 2023, is mitigated. This is relevant for the claims below materiality threshold payable in the year 2022/23 and for bad debt expenses being incurred currently which will be recovered through increased DUoS when the increased tax rate is effective. We request confirmation that the effect of the change in the corporate tax rate on bad debt from 19% in ED1 to 25% in ED2 will be mitigated so that this can be reflected in the ED2 licence drafting of SOLR bad debt pass through costs.

If you wish to discuss further please contact me at pbranston@westernpower.co.uk.

Yours sincerely

A handwritten signature in black ink, appearing to read 'p branston', with a large, stylized initial 'P'.

PAUL BRANSTON
Regulatory & Government Affairs Manager