

# Ruddle Merz

The authoritative voice on business rates

Ruddle Merz Limited  
45 High Street  
Oakham  
Rutland  
LE15 6AJ

Telephone: 01572 757777  
Facsimile: 01572 757730  
E-mail: [enquiries@ruddlemerz.co.uk](mailto:enquiries@ruddlemerz.co.uk)  
Web Page: [www.ruddlemerz.co.uk](http://www.ruddlemerz.co.uk)

Paul O'Donovan  
Manager, Distribution Price Control Review  
Ofgem  
9 Millbank  
SW1P 3GE

12<sup>th</sup> April 2005

Dear Mr Donovan

## **Assessment of the Electricity Distribution Price Control Review Process Pass-through of Business Rates**

We refer to the document Assessment of the Electricity Distribution Price Control Review Process March 2005 91/05 and, in accordance with paragraph 1.6, we submit our comments on one element of the price control system namely the pass-through element of Business Rates

From 1 April 2005 all occupiers of non-domestic properties are able to challenge the rateable values included in the 2005 Rating List. If they are successful in getting their rateable values reduced, their costs are reduced. The effect of this cost reduction is that their profits are increased or they can reduce the prices they charge for their goods or services.

At paragraph 7.45. of Electricity Distribution Price Control Review Final Proposals document, it is stated that rateable values have now been established and Ofgem proposes that business rates on network assets should now be treated as a "pass through" item.

On 1 April 2005 the rateable values of electricity distribution network properties ceased to be prescribed by the government. The rateable values have been assessed by the Valuation Office adopting a conventional rating valuation approach. It is over fifty years since the electricity distribution companies' properties were conventionally valued for rating purposes. Many elements of the valuations could be subject to dispute. If agreement is not reached between the Valuation Office and the ratepayer, the rateable values are determined, after hearing evidence from both parties, by independent Valuation Tribunals or on appeal by the Lands Tribunal. In the circumstances it is considered that the rateable values should not be regarded as "established".

The prescription of British Telecom's network rateable value ceased in 1995 and, as a result of their appeal against the value set at the 1995 Revaluation, British Telecom negotiated a significant reduction in their rateable value in the 1995 List. This reduction will no doubt have enabled them to reduce their customer charges or increase their profits.

In view of the fact that business rates on electricity distribution network assets are treated as a "pass through" item in the 2005 to 2010 price review period, there would appear to be little incentive for the DNOs to challenge the rateable values set by the Valuation Office because the benefit of any reduction in rate liability will be deducted in their allowed revenue.

It seems particularly important that at the time when electricity distribution companies can first challenge their rateable values they should be incentivised to do so. The valuation approach adopted by the Valuation Office in the 2005 List may not be approved by the Valuation or Lands Tribunals. It may be that the rateable values in the 2005 List are too high and as a consequence the DNOs operating costs and charges are higher than they need to be.

It seems strange that Ofgem, which we understand is supposed to regulate income to that which is a proxy for that which would be produced in a competitive environment, should take out of consideration one element of operational costs, namely the amount of rates a company has to pay, which all other companies have to deal with, which a normal company operating in a competitive environment could endeavour to minimise.

It also seems strange that in a regulatory system that has as a “key theme” incentives for efficiency, DNOs are not given any incentive to challenge their rateable values which accounts for approximately on third of their total operating costs.

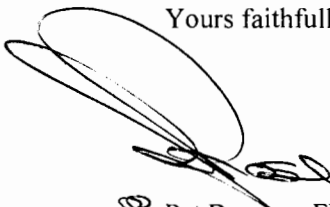
As you are aware Ofwat have recently completed a price control review for water companies. In the case of water companies, business rates has not been treated as a pass-through element and they will be incentivised to reduce their costs in this respect if possible. The position with regard to water companies is very similar to that of DNOs, where previously had their rateable values “prescribed” but from 1 April 2005 are subject to conventional rating assessment.

It is requested that Ofgem consider the above comments and advise whether a DNO will be able to retain any of the cost savings if it successfully obtains a reduction in the rateable value of its network assets.

It is also requested that Ofgem consider these representations in relation to the procedures to be adopted for the next periodic review.

We have written to Mr Carl Hetherington on the same topic some time ago and I am waiting for his response.

Yours faithfully



Pat Brennan FRICS