

**Legal & Regulatory**

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25 February 2011

Dear Rachel

**Regulatory asset lives for electricity distribution assets**

Thank you for the opportunity to comment on Ofgem's proposed changes to the regulatory asset lives for electricity distribution assets. We agree that it makes sense to review this issue at the present time, to coincide with the assessment of asset lives for transmission and gas distribution assets under the RIIO-T1 and RIIO-GD1 price controls.

Our views on the appropriate regulatory asset lives for electricity distribution assets are in line with the position we set out in our response to Ofgem's recent strategy consultation for RIIO-T1 and GD1. To reiterate, we fully support the proposal to set depreciation allowances based on the estimated economic life of network assets. This will ensure that investment costs are shared equitably between current and future consumers. As you note in your letter, it is also consistent with the accounting depreciation policies already in use by the networks themselves.

Based on the analysis undertaken by Ofgem's consultants (CEPA, SKM and GL Noble Denton), it is clear that the useful economic life of electricity distribution assets is considerably longer than the current regulatory life of 20 years. The proposal to move to an asset life of 45-55 years appears to be reasonable, although we believe that the consultants' report supports the use of a figure at the top end of this range. This reflects the fact that there is less uncertainty regarding the future usage of electricity distribution assets than there is for either gas distribution or electricity transmission.

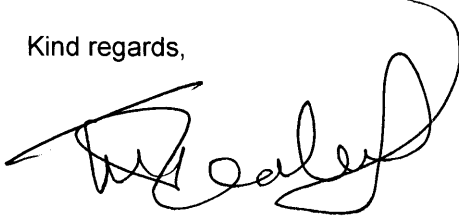
We also agree with the proposal to retain the current straight-line depreciation profile for electricity distribution assets. There is no obvious rationale for moving away from this profile, given that utilisation of these assets is expected to be high throughout their economic life. Recent analysis such as that undertaken by Redpoint Energy on behalf of the Energy Networks Association (ENA) reinforces the view that peak demand on the electricity distribution network is likely to grow steadily, even in scenarios with relatively low levels of electrification of heating and transport.

The one area of concern we have with Ofgem's proposals is in relation to the potential need for transitional arrangements. In line with the RIIO principles on financing, we strongly believe that networks should manage such issues using market-based mechanisms unless they can present compelling evidence to the contrary. Analysis undertaken for us by CEPA as part of our submission on the RIIO strategy consultation indicates that electricity transmission companies should be fully capable of managing the cashflow impacts of changes to asset lives through tools such as raising new equity. The case for transitional arrangements is arguably even weaker in the case of electricity distribution, given the higher level of certainty over the future use of these assets, and the additional lead time available until the next price control takes effect in 2015.

The CEPA report contains a number of worked examples of the financial impact of changes to depreciation policies, in support of the points set out above. We refer you to our RIIO strategy response for more details.

We hope that the comments set out in this response have been helpful, and we would be happy to discuss them in more detail if you would find this useful.

Kind regards,

A handwritten signature in black ink, appearing to read 'Tim Dewhurst', with a large, sweeping flourish extending upwards and to the right.

Tim Dewhurst  
Interim Director of Regulatory Affairs  
British Gas