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28 November 2013

Dear Ian

Reasonableness review of energy network operators pension costs

Thank you for the opportunity to respond to the above consultation. This letter should be treated as a consolidated response on behalf of UK Power Networks' three distribution licence holding companies: Eastern Power Networks plc, London Power Networks plc, and South Eastern Power Networks plc.

We note and appreciate Ofgem's willingness to engage with pension scheme Trustees as a part of this process and understand that the Trustees of our principal scheme will be responding to the consultation separately. It is also worth noting that the ENA will be responding collectively on the detail of the consultation, however, UK Power Networks would specifically like to make the following observations:

- We welcome the two stage review process proposed and request that the supporting information required for the initial review is appropriate in its nature. We believe that the scheme dataset should be sufficient for the purpose of stage one but recognise that the data requirements for the second tier scrutiny will be more detailed. We would also like confirmation from Ofgem that the pension true up will still be available in sufficient time to be implemented in any price change on the 1 April 2015 for those NWOs who are not subject to the second stage review (due to the licence and DCUSA requirements we estimate this to be before the end of November 2014). For those companies that are subject to the second stage review we would like clarification from Ofgem what should be included in any price change to be implemented on 1 April 2015.
- We note that Ofgem are considering requesting the scheme actuary's neutral estimate from the trustees. We are concerned that this information is subjective in nature (as it is based upon one individual's views of best estimate) and has the potential to vary significantly between scheme actuaries. We would like to understand how Ofgem will use this information whilst acknowledging the subjectivity.
- A similar concern applies to the value at risk measure relating to the scheme assets. Our understanding (due to a recent investment advisor tender process) highlighted just how much the models used by different investment advisors can differ. Whilst we agree that

this is a key governance metric of pension schemes we would propose that this is a relative rather than a comparative measure and would suggest that disclosure of the movement in value at risk of each scheme is a more valuable metric.

- We accept that benchmarking of pension schemes outside the sector will provide a valuable insight into the wider pensions arena and can only be to the benefit of consumers. However, we would like to ensure that the consultants used in this exercise have a deep understanding of the restrictions that many regulated utilities face in relation to their pension costs. Therefore, we would like Ofgem's commitment that the appointed consultants are briefed on the limitations of the license conditions (for example the use of contingent assets) and also the Protected Persons Regulations that restrict the material changes of future accrual. As you know in excess of 90% of UK Power Networks' ESPS scheme membership are covered by these regulations.

I hope that you will find our response helpful. I can confirm that we look forward to attending your proposed workshop – our preferred date is 6 December. If you have any questions, please do not hesitate to contact me.

Yours faithfully

A handwritten signature in black ink, appearing to read 'K Hutton', with a stylized flourish at the end.

Keith Hutton
Head of Regulation
UK Power Networks

Copy: Paul Measday, Regulatory Returns & Compliance Manager, UK Power Networks
William McKenzie, Ofgem