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Thomas Mackenzie
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Ofgem
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Our ref	*Your ref*	*Date*
-		28 February 2014

Dear Tom

RIIO-ED1: Informal consultations on licence drafting –Financial Handbook and Charge Restriction Conditions (Part 2)

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 response to the above consultations published on 31 January 2014.

> Question 1: Do you have any views on the proposed changes to the CRCs?
>
> Question 2: Do you have any views on the reasons and effects for the licence changes?
>
> Question 3: Do you have any comments on the draft of Section 1 of the ED1 Price Control Financial Handbook?

The ENA LDWG has submitted detailed drafting comments on the remaining CRCs and Part A of the Financial Handbook, together with an updated issues log. We look forward to further discussions with Ofgem on the Financial Handbook.

This response therefore addresses issues specific to WPD. An updated log of issues from WPD is attached. This takes account of feedback from Ofgem on issues previously raised.

<u>Appendix 1 – CRC Issues Log</u>

<u>2A Provision for the £5 Rebate</u>

The 2 year delay on the 14/15 k factor under recovery caused by the voluntary £5 reduction in charges for domestic customers means that WPD will be voluntarily artificially under recovered in the East Midlands region for 8 years. In the interest of transparency for stakeholders notably suppliers, we request a separate k factor to identify the £5 rebate

2M - Losses – Whilst it is Ofgem's intention to make minimal changes to this CRC, the changes to the definition of PPLt have a significant impact. The drafting now reads as if all of PPLt is to be recovered during ED1. For WPD this is not the case. We refer to Ofgem's Decision on Q9 and Q12 of the DPCR5 losses consultation dated 24/08/2012, and the decision letter published on 24 July 2012 in respect of Q9 and Q12 of the DPCR5 losses consultation. The decision letter stated that "DNOs should use the estimations they made in the May DCP066 reports for the value of PPL in their forthcoming DCUSA forecasts". In August 2012, Ofgem clarified that DNOs were expected to be using the estimations they made in May of the value of PPL in their indicative and final tariffs for 2013-14. As a result WPD's 13-14 tariffs already include a PPLt amount.

Therefore Ofgem's Determination of PPLt, needs to recognise monies recovered prior to April 2015.

We have raised this issue with Ofgem separately, and been advised that this matter will be recognised in the forthcoming PPL Decision Document and Determination, prior to the ED1 Licence taking effect.

For the avoidance of doubt, the correct values that prices were adjusted by in 2013/14 Regulatory Year are set out below and we would expect these to be used in Ofgem's Final Determination of the PPL. These are in 13/14 prices as 2013/14 was the year that the adjustments were made.

ADJ1
WPD South West = -£4.55m
WPD South Wales = -£3.39m
WPD Mid West = -£11.21m
WPD Mid East = -£44.52

Ofgem's Final Determination (FD) will therefore be:

FD = PPL1 - ADJ1

Where PPL1 is the value from the DPCR4 close out formula and
ADJ1 are the adjustments in the table above.

Appendix 2 – Financial Handbook

Rail Electrification

The formula contained in para 12A.10 of the Financial Handbook is not consistent with Ofgem's intention, as the formula can clawback values in excess of the allowed rail electrification costs.

WPD's Business Plan BPDT included costs for both wayleaves terminations and diversions of assets in highways for specified rail electrification projects. The existing wayleaves are covered by a Master Wayleave Agreement and WPD has assumed that all the costs associated with the termination of these wayleaves will be funded by WPD. The costs of diversions in highways are informed by the New Roads and Street Works Act which requires that 18% of the costs of diversions are funded by WPD. For diversions in highways WPD's has included 18% of the costs, assuming that Network Rail will contribute 82%.

There is no expected change to the rules on works in highways, but the government could decide to require Network Rail to contribute to the costs of wayleave terminations.

Therefore Licence condition CRC 3K and Financial Handbook section 12A should be clear that adjustments for rail electrification expenditure relate to wayleaves covered by the Master Wayleave Agreement.

If WPD is accepted for fast-tracking, the full cost of wayleaves diversions associated with the specified rail electrification projects will be included in the Opening Base Revenue Calculation.

In CRC 3K.3 the adjustment term RE for the licensee for a particular Regulatory Year represents the total reduction in the licensee's allowed Totex expenditure (expressed in 2012/13 prices) with respect to Recoverable Diversion Costs, for that Regulatory Year. "Recoverable Diversion Costs" are defined as costs associated with the diversion of electric lines or electrical plant to facilitate rail electrification projects that were included in the calculation of the licensee's Opening Base Revenue Allowances, but which have since become recoverable from a third party. Financial Handbook 12A.10 refers to "expected diversion costs will be met by additional contributions".

The current proposal for adjustments calculates a revenue reduction equivalent to the amount of additional contributions. The formula in para 12A.10 of the Financial Handbook claws back an unlimited amount of contributions through the revised RE value = (-1 x aggregate amount of additional contributions))

We propose that the amount of the reduction derived from the formula should be capped at the expenditure that WPD has been allowed (for wayleave terminations). We propose that the adjustment term (RE) should be the minimum of the contribution or the allowed expenditure for wayleave terminations associated with specified rail electrification projects.

So if contributions are lower than allowed expenditure, the amount clawed back is the value of contributions.

If contributions are greater than allowed expenditure, the amount clawed back is the full value of allowed expenditure.

We suggest that this formula is inserted after 3K.3 and amended in 12.10 of the Financial Handbook.

RE shall be calculated as :

Revised RE value = -1 x (min(AARE, TRE))

where:

AARE is the aggregate amount of additional contributions for specified rail electrification projects

TRE is the total amount of allowed expenditure for wayleave terminations for specified rail electrification projects (as detailed in appendix 1).

Together with an Appendix giving the allowed expenditure amounts.

APPENDIX 1

Values for the TREterm (expressed in £ millions, 2012/13 prices) by licensee

(see Part A)

Licensee	TRE
WMID	16.8
EMID	16.0
SWALES	38.0
SWEST	17.3

In addition it would be helpful for the Handbook to contain additional explanation about contribution assumptions. A marked up version of Chapter 12A is attached including additional explanation and comments set out above on the formula for calculating RE.

We look forward to further discussions with Ofgem to address the issues that we have identified.

Yours sincerely

NATASHA RICHARDSON
Regulatory Compliance Manager