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Anna Rossington
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Our ref

Your ref

Date

23 April 2014

Dear Anna

Application for relief from the consequences of under-recovery because of the removal of the Fifth Distribution Price Control Review (DPCR5) losses incentive mechanism

Further to Ofgem's Direction of PPLt issued 21 March 2014, I am writing on behalf of Western Power Distribution (East Midlands) plc to request relief from the impact of CRC14.2 for the 2013-14 and 2014/15 regulatory years.

With reference to paragraphs 2.198 to 2.202 of the March 2014 Losses Decision Document, Ofgem states that current over or under recovery position of DNOs will be affected and that any adverse impact or penalty arising from the anticipation of the PPLt term will be dealt with on a case by case basis.

WPD made Ofgem aware of this issue during the ED1 licence drafting discussions and requested that Ofgem set the PPLt term net of any amounts already returned to customers. Ofgem's decision to require DNOs to "recover" PPL amounts from April 2015 onwards, means that WPD East Midlands SLC47 Revenue Return will now show a significant under-recovery position.

CRC14 in WPD's current Special Condition provides that the rate of interest adjustment (PR_t) applicable on an under-recovery should be zero, where the Distribution Network Operator's (DNO's) revenue is less than 97 per cent of the allowed revenue. WPD forecasts that for WPD East Midlands, Ofgem's decision to disallow PPL estimations will mean that its revenue for 2013-14 and 2014-15 will recover less than 97 per cent of its allowed revenue.

WPD requests a modification to CRC14.2 for WPD East Midlands to set the interest rate at 1.5% for 2013/14 and 2014/15.

In addition we are likely to need to apply for a consent under CRC 2A (Restriction of Allowed Distribution Network Revenue) for the same reasons, in respect of all four of the WPD licensed areas. Whilst the impact on the other three WPD licensees areas is smaller, when combined with the unwinding of the £5 rebate, the effect is likely to be material.

Reasons

We were asked in 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" to enter the same value in the 2013/14 for the PPL, for setting Indicatives and Finals, as used in the May DCP066 reports.

The Decision Letter of July 2012 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 included a PPLt amount. We were not asked by Ofgem to remove this from the 13/14 allowed revenue and set up an under recovery position and therefore did not remove it. Consequently both our Template B forecast and DCP66A included a PPLt amount for 2013/14.

In the case of WPD East Midlands, a negative amount of £44.52m for PPLt was included in the 2013/14 published prices.

We highlighted this to Ofgem during discussions on Licence drafting and asked Ofgem to set our PPL terms net of the PPL values already included in 2013/14 prices.

As the Decision Document reverses Ofgem's original instruction and sets a PPL term that includes the amounts already recovered in 2013/14 prices – i.e. £44.52m for WPD East Midlands, we will have under recovered by over 97% of allowed revenue under CRC14.2 and be subject to an adverse interest rate.

Request for Licence modification

I am hereby formally requesting that the Authority modifies CRC 14 paragraph 2, for Western Power Distribution (East Midlands) plc to remove the adverse interest rate for under recovery.

Part A: Interest adjustment for over and under recoveries of revenue

14.2 For the purposes of Part D of CRC 3 (Restriction of Distribution Charges: Use of System Charges), the value of the interest rate adjustment PRt is to be treated as follows:

(a) if, in respect of Regulatory Year t-1, Regulated Combined Distribution Network Revenue exceeds 103 per cent of Combined Allowed Distribution Network Revenue, PRt must have the value of 3;

~~(b) if, in respect of Regulatory Year t-1, Regulated Combined Distribution Network Revenue is less than 97 per cent of Combined Allowed Distribution Network Revenue, PRt must have the value of zero;~~

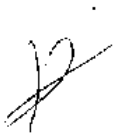
and in all other cases:

(be) PRt must have the value of 1.5.

As WPD needs to submit its SLC47 Revenue Return for 2013/14 by 31 July 2014, we request that WPD East Midlands licence is amended by 31 July 2014.

If you have any queries regarding this request, please contact Natasha Richardson, Regulatory Compliance 0117 9332382 or Dave Wornell, Income and Connections on 0117 9332032.

Yours sincerely

A handwritten signature in black ink, appearing to be 'AS', written over a horizontal line.

ALISON SLEIGHTHOLM
Regulatory & Government Affairs Manager