

Clothilde Cantegreil
Ofgem
9 Millbank
London
SW1P 3GE

Date
19th January 2015

Dear Clothilde,

RIIO-ED1: statutory consultations for RIIO-ED1 – Charge Restriction Conditions, Standard Licence Conditions, Network Assets Workbook, PCFM and Price Control Financial Handbook

We welcome the opportunity to comment on the above consultations and to acknowledge the hard work across all DNOs and Ofgem. SPEN is supportive of the ENA consultation response.

We have and continue to correspond with Ofgem on a number of areas of error and material concern regarding the outcome of RIIO-ED1 including the Final Determination published on 28 November 2014 and this formal response should be considered by you alongside that separate correspondence.

Please note that this response should not be construed as acceptance of the output of RIIO-ED1 including the Final Determination and therefore the values contained in the proposed licence modifications.

In addition, SPEN has the following comments in the context of the consultations.

1. Licence Table Values

We have discovered various discrepancies within the licence table values. We believe the various licence term values as provided in Appendix 1 of this letter, to be inaccurate. We would be happy to work with Ofgem and to provide our workings in order to confirm that we have derived our expected values utilising ED1 policy.

One example is that Innovation Roll-out Mechanism materiality threshold has been uplifted by the efficiency incentive rate when this was not in the strategy decision.

In the March 2013 Strategy decision paper "Uncertainty Mechanisms" the decision in respect of the Innovation Roll-out Mechanism reopener states that the threshold will be "1% of average annual RIIO-ED1 base revenue" - there is no mention of "after the application of the efficiency incentive rate" as stated in other re-openers. Accordingly, we believe the

Ochil House, 10 Technology Avenue, Hamilton International Technology Park, Blantyre, G72 0HT

Telephone: 0141 614 0008

www.spenergynetworks.com

SP Transmission plc, Registered Office: 1 Atlantic Quay, Glasgow, G2 8SP Registered in Scotland No. 189126 Vat No. GB 659 3720 08
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thresholds should be adjusted downwards e.g. the thresholds for SPD and SPMW would become 3.45 and 3.11 respectively.

Moreover, various table values incentive licence conditions such as Time to Connect; Broader Measure of Customer Satisfaction and Incentive on Connections Engagement have transposed values between SPD and SPM.

For example, the maximum upside for supply interruptions in the Broader Measure of Customer Satisfaction should be calculated as follows:

- $0.3\% \times (\text{Base Revenue: ED1 Average } \pounds 345.3\text{m for SPD}) = 1$ (this is published as 0.9 in the table)
- $0.3\% \times (\text{Base Revenue: ED1 Average } \pounds 311\text{m for SPM}) = 0.9$ (this is published as 1 in the table)

Please see Appendix 1

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2. Outstanding Associated Documents

Many of the associated documents which are cross-referred to in the licence have not yet been published, therefore, we restrict the scope of our comments to those documents that have been published and reserve the right to make further comments once the additional documents are published. It is important that we fully understand the conditions applicable to us.

We have a further concern that such stringent timelines will affect the quality of the documentation produced and will not provide sufficient time for an adequate level of consultation.

These issues raise further concerns with regards to our internal corporate governance procedures and the ability of our Directors to accept the full RIIO-ED1 package without having had sight of the full suite of documentation.

Associated Document Name	Draft Released to DNOS	Consulted on	Near Completion/ Incomplete
Environmental Guidance	Yes	Initial draft	Near Completion
Incentive on Connections Engagement	Yes	Yes	Near Completion
Data Assurance Guidance	Yes	Yes	Near Completion
Stakeholder Engagement and Consumer Vulnerability Incentive Guidance	Yes	Yes	Near Completion
Losses Discretionary Reward Guidance	No	No	Incomplete
Business Plan Reporting Guidance	No	No	Incomplete
Regulatory Instructional Guidance	Not fully	No	Incomplete
NIA Governance	Yes	Consulted on proposed changes, not actual guidance docs	Near Completion
LCN Fund Governance Document (existing document brought forward)	Yes	No	Incomplete
NIC Governance Document	Yes	Consulted on proposed changes, not actual guidance docs	Near Completion
Time to Connect Guidance	Yes	No	Near Completion
Breakdown of RIG			
Cost and Volumes	No	No	Incomplete
Revenue and Financial Issues	No	No	Incomplete
Secondary Deliverables	No	No	Incomplete
Reinforcement	No	No	Incomplete
Interruptions	No	No	Incomplete
Connections	Yes	No	Near Completion
Customer Service	Yes	No	Near Completion
Pensions	No	No	Incomplete

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3. SLC 50 Business Plan Commitment Reporting

We note that SLC 50 was not amended as a result of DNO comments in the previous licence consultation. DNOs are still required to report against March 2014 plans. We do not believe that Ofgem has intended for DNOs to report against commitments made in superseded business plans.

This is not useful for stakeholders as some DNOs may no longer be capable of delivering particular commitments due to a reduction to allowed revenues.

4. DPCR4 Growth Term Licence Condition

We believe that the revenue term to correct the DPCR4 growth term following the close out of the DPCR4 losses incentive is not yet included in ED1 licence. Our understanding is that there is an up and coming consultation on this, therefore we assume that it is Ofgem's intention to make the necessary licence modifications to allow the adjustments to correct DPCR4 growth term for outcome of DPCR4 losses closeout.

5. CRC 2C – Impacts of a 2 year delay to funding

Consistent with CRC8.16 of the DPCR5 Licence, in order to reflect the 2 year delay in funding of the Broad Measure of Customer Service reward/penalty we believe that the formula in paragraph 2C.12 should be multiplied by $[(1 + It-2/100) \times (1 + It-1/100)]$.

6. CRC 2D - Incorrect values for ex-gratia payments per customer

The definition of SWPM quantifies ex-gratia payments for a severe weather event to be 'no more than a total of £300 of payments per customer'. The Electricity (Standards of Performance) Regulations 2010 have now been amended such that Guaranteed Standards payments for a severe weather event have a prescribed maximum of £700. The definition of SWPM therefore requires to be updated.

7. CRC 3F - Definition of Specified Street Works Costs

The definition of street works costs only references the costs associated with permits; however, it is our understanding that the Transport (Scotland) Act 2005 uses the Scottish 'Road Works Register' as opposed to 'permits'. We believe that 'Road Works Register' should be included in the definition of Specified Street Works Costs.

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8. Price Control Financial Model

a. Directly remunerated services (DRS9)

In the updated final determination price control financial model (PCFM) issued on 17th December 2014 reflecting Ofgem's correction email of the same date the PCFM now deducts DRS9 net revenues (row 41 of the DARTs tab). We also refer to point F01 in the Annex to the letter from Ofgem's dated 12th January which confirms Ofgem's approach to deduct forecast net miscellaneous revenues and consistency with CRC 5C. This approach is inconsistent with Licence Condition CRC5C.8: "Charges levied in respect of Directly Remunerated Services provided within categories DRS5 and DRS9 of Appendix 1 are to be set at a level that will allow the licensee to recover its reasonable costs and a reasonable margin in providing the service in question." The treatment adopted in the PCFM is inconsistent with the Licence because it deducts DRS9 net revenues and therefore does not allow the DNO to earn a reasonable margin. In the issues log we sent you on 12th December we pointed out that the costs are not part of our price control totex and are all incremental and therefore it is incorrect to make any adjustment to allowed price control revenue. The approach being adopted of deducting net margin from allowed revenue appears to be inconsistent with Maxine Frerk's letter dated 17th December which states: we allow DNOs to set charges with a reasonable margin of profit". To ensure consistency with the Licence and allow the DNO a reasonable margin we believe the PCFM "DARTs" tab row 58 should be amended by removing the deduction of row 41.

b. ED1 Established Pension Deficit funding

We refer to issue F02 we raised on 12th December 2014 and your response dated 12th January 2015, in relation to pension deficit being funded over 10 years, as opposed to the Ofgem proposal of 12 years.

We don't believe that the logic in the response is consistent with the approach set out in the Financial Handbook for updating the Pension Scheme Established Deficit revenue allowance through the Annual Iteration Process. Table 3.2 of the Financial Handbook (rows 4, 5, 6 & 7) confirms that established deficit funding from 2018/19 will reflect the 31 March 2016 deficit spread over 7 years; and table 3.3 (rows 4, 5, 6 & 7) confirms that established deficit funding from 2021/22 will reflect the March 2019 deficit spread over 4 years. It should be noted that the same approach is being applied in Electricity Transmission. So following these rules it would seem logical that the Established Deficit at 31st March 2013 should be funded over 10 years from 2015/16.

We were surprised at the 12 year proposal in the Final Determination in November as this was counter previous advice we had had from Ofgem on the same matter, in October 2014.

We received no subsequent correspondence from Ofgem prior to 28th November suggesting that the established deficit at 31st March should be funded over 12 years from 2015/16 instead of 10.

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The established pension deficit funding is set out in tab F7 of the FI tables issued on 28th November 2014 as part of the Final Determination. The following table shows the funding per annum in the Final Determination over 12 years and the corrected value over 10 years as modelled in tab F7 of the FI tables:

Established Deficit Funding	12 years p.a.	10 years p.a.	Variance p.a.
SPD	25.233	29.707	4.474
SPMW	23.880	28.115	4.235
Total	49.113	57.822	8.709

Therefore we believe the funding of the Pension Scheme Established Deficit in row 34 of the SPD and SPMW tabs of the PCFM should be changed to £32.570m p.a. and £31.905m p.a. respectively (this includes the additional funding in respect of the true up of the annual funding from previous price controls).

9. **Financial Handbook Tables 16.2 and 16.3**

The values stated for SPD and SPMW in table 16.3 for opening expenditure allowances for DPCR5 Workforce Renewal (WFR) do not agree to the final DPCR5 PCFM – IQI tab row 64. We believe the values should be:

WFR – DPCR5 expenditure allowances £m	2010/11	2011/12	2012/13	2013/14	2014/15
SPD – PCFM IQI tab row 64 (07/08 prices)	0.59	0.85	3.40	3.50	3.64
SPD – table 16.3 values (12/13 prices)	0.69	1.00	3.99	4.11	4.27
SPMW – PCFM IQI tab row 64 (07/08 prices)	0.78	1.06	4.19	4.09	4.16
SPMW – table 16.3 values (12/13 prices)	0.91	1.24	4.91	4.80	4.88

This has a consequential impact on the values for SPD and SPMW in table 16.2 for opening capex allowances adjusted for RRI. We believe the revised values should be:

WFR – opening capex allowances £m	2010/11	2011/12	2012/13	2013/14	2014/15
SPD – (12/13 prices)	127.96	135.71	138.69	146.94	142.78
SPMW – (12/13 prices)	173.90	168.17	179.95	173.22	174.92

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Please do not hesitate to contact me should you have any queries.

Yours sincerely,

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

Scott Mathieson
Regulation and Commercial Director

Ochil House, 10 Technology Avenue, Hamilton International Technology Park, Blantyre, G72 0HT

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APPENDIX 1

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Tables Name/No	Licence Term	Comments	Expected Value SPD	Expected Value SPM	Value in Licence SPD	Value in licence SPM
CRC 2C. Broad Measure of Customer Service Adjustment	CSAUt – Maximum upside supply interruptions	Values Transposed	1	0.9	0.9	1
	SIRIRt – Supply Interruptions Reward Incentive	Incentive rates not as expected	1.43	1.29	1.33	1.42
	CSBUt – Maximum upside connections term	Values Transposed	1.7	1.6	1.6	1.7
	CRIRt – Connections Reward Incentive Rate	Incentive rates not as expected	2.43	2.29	2.22	2.37
	CSCUt – Maximum upside general enquiries	Values Transposed	0.7	0.6	0.6	0.7
	GRIRt – General Enquiries Reward Incentive	Incentive rates not as expected	1	0.85	0.89	0.95
	CSADt – Maximum downside supply	Values Transposed	1	0.9	0.9	1
	SIPIRt – Supply Interruptions Penalty Incentive	Incentive rates not as expected	0.71	0.64	0.67	0.71
	UCPIRt – Unsuccessful Call Penalty Incentive	Values Transposed	0.07	0.06	0.06	0.07
	CSBDt – Maximum downside connections term	Values Transposed	1.7	1.6	1.6	1.7
	CPIRt – Connections Penalty Incentive Rate	Incentive rates not as expected	1.21	1.14	1.11	1.18
	CSCDt – Maximum downside general enquiries	Values Transposed	0.7	0.6	0.6	0.7
	GPIRt – General Enquiries Penalty Incentive	Incentive rates not as expected	0.5	0.43	0.44	0.47
	ARCMt – Complaints metric maximum penalty	Values Transposed	1.7	1.6	1.6	1.7
CRC 2E. Incentive on Connections Engagement	IRCMt – Complaints Metric Incentive Rate term	Incentive rates not as expected	0.26	0.25	0.24	0.25
	SEt – Maximum stakeholder engagement	Values Transposed	1.7	1.6	1.6	1.7
CRC 2F. Time to Connect Incentive	Maximum exposure to the Incentive on Connections Engagement	Values Transposed	3	2.8	2.8	3
	TQAIt – Incentive rate for the LVSSA Time to	Not in line with expectations	0.19	0.17	0.17	0.18
	TQBIt – Incentive rate for the LVSSB Time to	Values Transposed	0.21	0.19	0.19	0.21
	TCAIt – Incentive rate for the LVSSA Time to	Not in line with expectations	0.04	0.03	0.03	0.03
CRC 3D. The Innovation Roll-out mechanism	TCBIt – Incentive rate for the LVSSB Time to	Values Transposed	0.03	0.02	0.02	0.03
	Materiality threshold amount	We believe values should not be uplifted by incentive rate. This should be 1% of average ED1 base revenue only per strategy decision document	3.45	3.11	6.47	6.66
CRC 3F. Arrangements for the recovery of uncertain costs	The material amount for Specified Street Works Costs for each licensee (this amount is the amount we must spend before we can claim back any costs as a uncertain costs)	We believe values should not be uplifted by incentive rate. This should be 1% of average ED1 base revenue only per strategy decision document	6.32	5.69	6.47	6.66
	The material amount for Rail Electrification Costs for each licensee (This should be WPD/ENWL only, however, should we ever have rail elec this would be the amount we would have to get to before we could claim back)	We believe values should not be uplifted by incentive rate. This should be 1% of average ED1 base revenue only per strategy decision document	6.32	5.69	6.47	6.66
	The material amount for Link boxes for each licensee (Costs incurred or expected to be incurred by the licensee in efficiently managing the asset risk associated with Link Boxes, as may be further clarified in the RIGs- this amount	We believe values should not be uplifted by incentive rate. This should be 1% of average ED1 base revenue only per strategy decision document	6.32	5.69	6.47	6.66
CRC 3G. Revising the allowed level of Load Related Expenditure	Total Opening level of allowed expenditure and the material amount for application and notification windows for each licensee	We believe values should not be uplifted by incentive rate. This should be 1% of average ED1 base revenue only per strategy decision document	N/A	N/A	N/A	N/A
CRC 3H. Allowed expenditure on improving services to Worst Served Customers	Values for the Worst Served Customer Cap Per Customer (WSCCPC) by licensee	This is inconsistent with previous version (was £800/customer, now £1000).	800	800	1000	1000
	Worst Served Customer Required Performance Improvement	This is inconsistent with previous version (was 20%, now 25%).	20	20	25	25
CRC 5G. Net to gross adjustment for Load Related Expenditure	Baseline Specific Customer Funded Reinforcement	Specific Customer Funded Reinforcement (BSCFR) @ £4m can be greater than our Connections allowance which is only £3.9m	TBC by Ofgem	TBC by Ofgem	4	19.6

Please note that our response should not be taken to deem that we accept the output of the Final Determination; values from which the draft licence conditions will cross reference.

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