

## Note of a staff meeting between Ofgem and the CC, 11 am, 20<sup>th</sup> November 2013

1. Ofgem explained that it was in the process of deciding RIIO-ED1 fast-track applications and would be publishing preliminary decisions on Friday 22 November. The cost of capital proposed by the distribution companies was a factor that Ofgem had taken account of in making these decisions. It would take final decisions in February 2014. Ofgem was considering the relevance of the CC's provisional determination on the NIE price control (the NIE PD) to its own decision making process on the cost of capital. For that reason Ofgem was seeking clarification on some of the issues raised in the provisional determination.
2. In the light of the CC's provisional determination on NIE, Ofgem was proposing to consult on its methodology for assessing the equity market return.
3. CC staff said the CC had not changed its approach to assessing the expected return on the market in the NIE PD. The CC had considered the same types of evidence on the market return and its components in its NIE PD as it had done in coming to its last price control decision on the cost of capital in Bristol Water (2010). However, the CC had taken into account the latest evidence in its NIE PD. This had led the CC to provisionally decide to reduce the upper end of the range for the market return to 6.5 per cent (previously 7 per cent).
4. CC staff clarified that the CC was not advocating a move away from the established approach of estimating the market return and its components taking into account a long run of historical data. However the CC saw merit in moving away from the upper limit suggested by historical realised returns. The CC had continued to take a range of evidence into account, including on historic realised returns and on historic and current expectations of returns. The CC used the term "forward looking" in this context to mean any approach, including those based on 113 years of data, which attempted to estimate investors' ex-ante expectations of returns.
5. On the cost of debt, CC staff said that the CC proposals were weighted towards NIE's embedded debt costs. The CC had assumed a real cost of new debt of 2.7 per cent.
6. On the asset beta, CC staff said that the CC had considered the confidence interval for the betas of the listed GB comparators together with evidence on the comparative risk profile of NIE. The CC considered that NIE was less well understood by investors and had therefore estimated a range for the asset beta towards the upper end of the confidence interval based on the comparator set.