

# RIIO-2 DRAFT DETERMINATIONS

## Consultation Response

OGUK is the leading representative organisation for the UK offshore oil and gas industry. Our membership includes over 400 organisations with an interest in the UK's upstream oil and gas sector. As the champions of industry, we work on behalf of the sector and our members to inform understanding with facts and evidence, engage on a range of key issues and support the broader value of this industry in a changing energy landscape. From exploration through to decommissioning and located across the length and breadth of the UK, our members are critical to safely providing security of energy supply, while supporting around 270,000 jobs and contributing billions of pounds to the economy each year.

Natural gas will continue to be a core part of the UK energy supply in the decades to come, currently supplying 80% of UK households and with their heating requirements and a range of industrial applications that cannot easily be replicated with other technologies. Decarbonised gases, in the form of both hydrogen and biomethane will, over time, be likely substitutes for these needs. The requirement for a reliable and secure transmission and distribution system is therefore clear, during the RIIO-2 period and beyond. There is also a need for the capability of the network to deal with peak-days requirement, across a range of scenarios even where the total volume of natural gas supplied over the network may decline.

Our sector is currently working with government on a North Sea Transition Deal. This encompasses both the development of offshore electricity networks and the Hydrogen economy. This work is in line with the Energy Integration Project in which Ofgem participates, together with the OGA and other regulators, and which published its Phase 2 document recently. More than ever, regulators are going to need to work together to contribute to the net zero objective. This has not come through strongly enough in the documents. The risk of a siloed approach is that each regulator is perceived as a separate gateway for innovative projects and this will discourage the required investment.

With respect to the detail of the draft determination a key concern, particularly for transmission, is the large difference between the amounts allowed for the ongoing maintenance of asset health and reliability and those projected in companies' Business Plans. Ofgem's review of these sections has been comprehensive. However, it is not clear that Ofgem and companies are using the same underlying approach for their assessment, or whether these reflect the considerable engagement process with stakeholders during the initial phases of the RIIO-2 process. A higher degree of consensus is required over these baselines in order to form the basis for the projected outputs and expenditure requirements, and that users and consumers can continue to benefit from a reliable network service. The objective of both the regulator and NGC should be to largely resolve these outstanding issues before the Final Determinations.

Finally, although there is a case for wider scope for reopeners and Uncertainty mechanisms (UMs), there is equally some concern among our members relating to the stability of transmission charges and the wider passing of additional risk onto network users and consumers across the board.

The attached Annex sets out OGUK response to selected important questions in the draft determinations. Most of these relate to the NGGT draft determination proposals although some responses are also relevant to the other draft documents.

## RESPONSES TO SELECTED INDIVIDUAL QUESTIONS

### CORE QUESTIONS

#### Stakeholder Groups

*Q1. What role should Groups play during the price control period and what type of output should Groups be asked to deliver? Who should be the recipients of these outputs (companies, Ofgem and/or stakeholders)?*

In general, OGUK supports the continuation of the stakeholder groups. Given the trend towards a more continuous assessment of outputs and a wider variety of reopeners and UMs, the user groups can perform a useful role in monitoring performance and in reviewing the various adjustments to the regulated asset base.

*Q2. What role should Groups take with respect to scrutinising new investment proposals which are developed through the uncertainty mechanisms?*

UMs have a lighter process than the full determinations, without the possibility of appeal to the CMA. Given the lower materiality of the amounts concerned, the stakeholder groups should contribute to provide an agile process so that changes can be implemented in a timely fashion.

*Q3. What value would there be in asking Groups to publish a customer-centric annual report, reviewing the performance of the company on their business plan commitments?*

An annual report would assist with transparency and be a useful focus for the work of the various different groups. A consolidated report is a possibility. The report should also focus on network users and large consumers who are likely to be the most directly affected, especially for transmission.

*Q4. What value would there be in providing for continuity of Groups (albeit with refresh to membership as necessary) in light of Ofgem commencing preparations for RIIO-3 by 2023?*

It would be more sensible to keep the groups running (in a less intensive fashion) over the intervening period. One of the issues in RIIO-2 has been the lack of continuity between price control periods. It would not make much sense to abandon the existing groups and the restart. In addition, the groups also have an important role to play in assessing the early phases of delivery and reviewing baseline assumptions.

*Q8. Do you agree that the Groups could have an enduring role to work with the companies to monitor progress and ensure they deliver the commitments in their engagement strategies?*

To some degree this would be sensible. In addition, there is also a need to ensure expectations are clearer on the extent and coverage of engagement that is required with different groups.

## Digitalised system

*Q5. Will the combination of the two proposed Licence Obligations support the delivery of a digitalised energy system and maximise the value of data to consumers?*

*Q6. Do you agree with our proposed frequency for publication of updates to the digitalisation strategy and the digitalisation action plan, respectively?*

*Q7. What kinds of data do you think should comply with the data best practice guidance to maximise benefits to consumers through better use of data?*

Digitalisation will provide opportunities for increased efficiency, reduced carbon footprint and improved safety across the whole energy sector and will be crucial in the transition to a net zero future. As well as monitoring best practice and providing guidance, the regulatory regime also needs to maintain incentives on companies to deliver efficiencies through digitalisation.

Cross industry collaboration will be a key enabler, with the true potential of data being unlocked through a shared approach to industry challenges. Therefore, digitalisation is as much about culture as technology. Businesses will need to work together to share ideas, challenge themselves and combine expertise to deliver the necessary transformational change.

OGUK recently launched the UKCS Data and Digital Maturity Survey which provides some additional detail in this area.<sup>1</sup>

## General price control parameters

*Q9. Do you agree with our proposal to accept the proposals for an ODI-R for BCF and the other proposals set out above as EAP commitments and to require progress on them to be reported as part of the AER?*

In general, ODI-Rs, not being financial incentives, are effectively a requirement to collect and publish reliable data and to set a voluntary target. The oil and gas sector has recently itself adopted a target for emission reduction in the same vein and so the proposal for business carbon footprint. Such obligations are likely to become required in any case under the regulations on Streamlined Energy and Carbon Reporting and the governments expectation to adopt the recommendations of the Taskforce on climate-related financial disclosure (TCFD).

*Q10. Do you agree with our proposed RPEs allowances? Please specifically consider our proposed cost structures, assessment of materiality, and choice of indices in your answer.*

RPE allowances have a material impact on network charges. The expectation that construction prices will outpace CPI is probably realistic. However, the projections to be used and the annual truing up process would appear to be a sensible way to manage this issue, especially as the regime is shifting more towards a continuous assessment of the overall capital programmes.

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<sup>1</sup> <https://oilandgasuk.co.uk/product/ukcs-data-digital-maturity-survey-report-2020/>

*Q11. Do you agree with our proposed ongoing efficiency challenge and its scope?*

In the wake of the pandemic and the associated economic impact, all businesses will be required to focus on efficiency improvement. The ongoing efficiency objectives of 1.2% for capex and 1.4% for opex will feed through into NGC procurement strategies and provide an impetus to avoid cost escalation.

With respect to Ofgem's cost assessment model, please refer to later detailed comments on the NGGT document and NGGTQ22 in particular.

### **Reopeners**

*Q12. Do you agree with our proposed common approach for re-openers?*

The proposed approach overall is acceptable, and the move to a more continuous approach to capex makes sense given some uncertainties about future energy provision. However, there is concern that large amounts of expenditure being approved in UMs may lead to tariff volatility, especially as (under a revenue cap model) considerable volume risk already sits with network users.

On the other hand, the regime needs to be agile and respond quickly, especially with respect to anticipatory investments for zero technologies. Oil and gas businesses have particular interests in offshore electrification and hydrogen and would not wish to see the Ofgem regulatory process become an additional "gate" to realising these necessary investments (see response to net zero below).

*Q13. Do you agree with our proposals on a materiality threshold, a financial incentive, a 'foreseeable' criterion, and who should trigger and make the application?*

The proposals appear sensible although the process for application should be symmetrical for net zero issues (see Q23 below).

*Q14. Do you consider that two application windows, or annual application windows, are more appropriate, and should these be in January or May?*

Annual windows would be preferable. May rather than January might be better to avoid overlapping processes.

*Q20. Do you agree with our approach regarding legislation, policy and standards?*

Safety and legislative standards are potentially drivers for additional asset health expenditure. It may be advisable to reconsider this in the context of a wider Asset Health UM for gas transmission.

### **Cyber and security and resilience**

*Q16. Do you agree with our proposed re-opener windows for cyber resilience OT and IT, and our proposal to require all licensees to provide an updated Cyber Resilience OT and IT Plan at the beginning of RIIO-2?*

*Q17. What are your views on including the delivery of outputs such as: CAF outcome improvement; risk reduction; and cyber maturity improvement, along with projects-specific outputs?*

The determinations need to provide adequate allowance for regulated business to comply with all legislation and associated HSE guidance relating to cyber security including sites covered by COMAH requirements with respect to “all measures necessary”.<sup>2</sup>

*Q18. Do you agree with our proposal for the Non-operational IT and Telecoms capex re-opener?*

*Q19. Do you agree with our approach to using a re-opener mechanism for changes to government physical security policy?*

Please see response to NGGTQ30

## **Net Zero**

*Q21. Do you agree with our overall approach to meeting Net Zero at lowest cost to consumers? Specifically, do you agree with our approach to fund known and justified Net Zero investment needs in the baseline, and to use uncertainty mechanisms to provide funding in-period for Net Zero investment when the need becomes clearer?*

Overall, the proposed approach is sensible. However, the DD document overstates the scope for any regulatory body or agency, including Ofgem, to make an unambiguous judgement of what is “lowest cost”. In reality, the move to net zero will be an iterative process and there is uncertainty about the eventual mix of technologies and there will need to be scope for some experimentation, even if this leads to some element of sunk costs.

An over-restrictive and cautious approach will slow progress and create uncertainty. This, in itself will increase the overall cost of transition by delaying investment. Ofgem will need to be ready to rapidly approve anticipatory investment relating to electrification and the use of Hydrogen where the needs are, in fact, already relatively certain. Indeed, regulatory decisions can help reduce uncertainty about the pace of change so a “wait and see” approach can be counterproductive.

As already noted, the oil and gas sector is particularly interested in offshore electricity grids and hydrogen solutions being advanced more quickly as part of the North Sea Transition Deal being discussed with government. The joint BEIS\Ofgem review of offshore electricity transmission is welcome.

*Q22. Do you think the package of cross sector and sector-specific UMs provides the appropriate balance to ensure there is sufficient flexibility and coverage to facilitate the potential need for additional Net Zero funding during RIIO-2?*

The package of measures is welcome. However regulated businesses need to be proactive in coming forward with solutions to net zero or whole systems questions. The process outlined for net zero reopener will potentially discourage this and lead to a more reactive stance (see below).

*Q23. Do you have any views on our proposed approach to a Net Zero reopener?*

Ofgem should consider a symmetric approach whereby companies are also allowed to initiate a net zero reopener. This will encourage more proactive outcome and an agile system. Likewise, the roles and responsibilities of BEIS and Ofgem in advancing net zero may also need greater clarification. For example, the possibility for BEIS to issue a strategic steer to Ofgem under the existing Energy Act is not discussed. Likewise, coordination with other regulators is not mentioned and the DD document implies a rather siloed approach. This leads to concerns that a

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<sup>2</sup> <https://www.hse.gov.uk/eci/cyber-security.htm>

sequential will be followed involving several regulatory and policy “gateways”. This will slow progress significantly since each regulator has its own statutory duties and powers to consider.

## **Innovation**

*Q24. Do you agree with our proposals for the RIIO-2 Strategic Innovation Fund?*

*Q25. Do you have any comments on the additional issues that we seek to consider over the coming year ahead of introducing the Strategic Innovation Fund?*

OGUK supports the concept of a Strategic Innovation Fund. The innovation programme will be particularly important in RIIO-2 and future periods in view of the transformation required to achieve net zero. Research into decarbonisation of gas and hydrogen in particular will be central to achieving net zero in industrial and some commercial and domestic use. Innovation will be central to the success of this endeavour and there are certain elements of the R&D required that only networks are able to support.

That said, a higher degree of strategic oversight and collaboration with other funding agencies is necessary. The Oil and Gas Technology Centre (OGTC) would be a possible partner organisation to this element of the RIIO-2 programme. OGTC was established in 2017 as part of the Aberdeen City Region Deal and is focused on investing in technology that maximises the energy potential of the UK North Sea. The OGTC has co-invested £152M with industry to develop and deploy new technology, with >62% (£94.7M) match funded by industry. These partnerships are supported by a strong membership model across solution centres, with 137 members spanning operators, supply chain and technology developers. The strong external focus allowed the creation of important relationships which enabled an industry led launch of the Net Zero Solution Centre in September 2019 and the creation of a Net Zero roadmap, championed by industry.

## **Competition in Investment**

*Q32. Do you agree with our proposed position on late competition?*

“Late competition” is the most relevant to the gas transmission sector with the projects at St Fergus and Bacton being highlighted as potential candidates. In general, a more coordinated approach is preferred and the potential benefits from e.g. CATOs and SPVs are now smaller than previously. These are not supported for gas transmission projects in particular so a “competition proxy” model is probably the furthest this should be taken. The main issue with these projects is to deliver a reliable and cost-effective outcome rather than use these as an exercise in regulatory innovation.

## **Business Plan Incentive**

*Q35. Do you agree with our rationale for why NGET and NGGT should be considered to have failed Stage 1 of the BPI?*

In general, this is a matter between the companies concerned and Ofgem. However, NGGT did strongly engage with network users during the preparation of the Business Plan and the concepts and rationale behind the various sections of the plan were well understood. The main concern would be if the penalties somehow fed through into lower deliverables in RIIO-2 with respect to maintaining network performance.

## **NARMs questions**

*NARMQ1. Do you agree with our proposals on the scope of work within each of the NARM Funding Categories and on the associated funding arrangements?*

*NARMQ2. Do you agree the funding adjustment principles and our proposals for applying funding adjustments?*

*NARMQ3. Do you agree with our proposed approaches to calculating funding adjustments and to application of penalties?*

*NARMQ4. Do you agree with our proposals in regards to requirements for justification cases?*

A key concern is the disconnect between NGGTs and NGETs view of the NARMs baseline, as expressed in their Business Plans, and the outcome of the draft determination. Indeed, it is somewhat disturbing that the businesses and regulators have arrived at very different outcomes with the same approach. Likewise, the relationship between Ofgem's cost assessment process and the NARMs baseline is not clear.

This current situation does not provide a sound basis for the delivery of the NARMs requirements going forward into the RIIO-2 period. A sound mutually acceptable baseline in the Final Determinations is required to ensure that these outcomes can be met.

## **General Gas Transmission Questions**

*Q1. Do you agree with the outputs package that we are proposing for the GT sector?*

*Q2. Do you agree with our overall approach to cost assessment in the GT sector?*

The general context for the RIIO-2 period should reflect expectations for continued production and use of natural gas. The central forecasts of BEIS and the OGA suggest demand for natural gas in 2026 will be around 90% of 2019 levels, and that UKCS production will be some 75% of 2019 levels.<sup>3</sup>

With this in mind, there are concerns that the cost assessment process used means that risks are being passed to network users and consumers with respect to the reliability of the network. Likewise, reducing scope of outputs or delaying necessary maintenance to the RIIO-3 period or beyond is not something that has the support of network users. This is discussed in more detail in the following sections.

*Q3. Do you agree with the UM package that we are proposing for the GT sector?*

On balance, it is acceptable for more elements of expenditure to be dealt with via UM processes. However, this is a significant shift away from the original RIIO concept and moves in the direction of being an ex-post regulatory regime with an associated change to the incentive structure faced by NGGT. Significant and important projects such as those at Bacton and St Fergus are now covered by UMs, with a high degree of regulatory oversight. It is important that this adds value to network users and does not distort or delay outcomes.

The other key issue airing from a higher proportion of UM expenditure is the potential uncertainty around network charges. Network users are already facing an almost 40% change in tariffs for 2020-21 as a result of COVID related shifts in demand, with projected charges then falling back in 2021-22. Such major shifts need to be minimised.

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<sup>3</sup> <https://www.ogauthority.co.uk/data-centre/data-downloads-and-publications/production-projections/>

## National Grid Gas Transmission Questions

### ***Output delivery incentives***

*NGGTQ1. Do you agree with our proposals for the Customer Satisfaction ODI-F?*

The ODI appears somewhat subjective, being based on a /10 rating from, not yet determined, set of respondents. Ideally it could capture holistically the overall performance of NGC, but this is not really clear.

*NGGTQ2. Do you agree with our proposals for the Quality of Demand Forecasting incentive?*

No comments. The focus on D-1 forecasts is largely acceptable.

*NGGTQ3. Do you agree with our proposals for the Maintenance incentive?*

No comments

*NGGTQ4. Do you agree with our proposals for the CCM incentive?*

Do not agree. NGGT need to have stronger incentives to avoid constraints. The use of the costs during RIIO-1 as a reference point is a circular logic, since it is derived from a period where Ofgem has strong incentives to avoid buying back constraints that would be removed under the DD proposals. In general network users would favour the outcomes associated with the current regime (i.e. very limited buybacks) to continue even if this means a more “generous” incentive scheme.

*NGGTQ5. Do you agree with our proposals for the Residual Balancing incentive?*

Agree.

*NGGTQ6. Do you agree with our proposals for the GHG emissions incentive?*

No comment.

*NGGTQ7. Do you agree with our proposals for the NTS Shrinkage incentive?*

Our main concern is that the change to incentive structure on shrinkage will impact price formation in the balancing mechanism and distort cash out prices.

*NGGTQ8. Do you agree with our proposals on the bespoke ODIs? If no, please outline why.*

*NGGTQ9. Do you agree with our proposals for the Environmental incentive?*

Overall, the approach to constrain the quantity of ODIs is agreed as it adds complexity.

No comments on environmental incentive.

*NGGTQ10. Do you agree with our proposals for the proposed Stakeholder Satisfaction incentive?*

No comment

**Price control deliverables and licence obligations**

*NGGTQ11. Do you agree with our proposals on the PCDs? If no, please outline why.*

<b>Output name and description</b>	<b>Consultation position</b>
Decommissioning	<b>Accept:</b> Chapter 3 paragraph 3.341
Asset health – non-lead assets	<b>Accept:</b> Chapter 3 paragraph 3.294
Compressor emissions – Wormington	<b>Accept:</b> Chapter 3 paragraph 3.92
Compressor emissions – King’s Lynn	<b>Accept:</b> Chapter 3 paragraph 3.131
Compressor emissions - Peterborough	<b>Accept:</b> Chapter 3 paragraph 3.142
Compressor emissions – St Fergus	<b>Accept:</b> Chapter 3 paragraph 3.107
Bacton terminal site redevelopment	<b>Accept:</b> Chapter 3 paragraph 3.295
King’s Lynn subsidence	<b>Accept:</b> Chapter 3 paragraph 3.315
Network Asset Risk Metric (NARM)	<b>Accept:</b> NARM Annex
Cyber resilience IT	<b>Accept:</b> Confidential annex
Cyber resilience OT	<b>Accept:</b> Confidential annex
Physical resilience	<b>Accept:</b> Chapter 3 paragraph 3.397

PCDs are a new concept which will add a higher level of granularity to the requirements on network businesses. The main issue (as discussed in the NARMs section) is the potential disconnect between the asset specific PCDs and the overall NARMs indicator. This is unlikely to work well where there is disagreement around the baseline. In addition, the regulatory burden around monitoring individual asset health investment is likely to be considerable and is a move away from outcomes focused regulation.

However, the PCD deliverables identified are all important and if including these as specific outputs improves delivery then, in general, the approach is supported.

*NGGTQ12. Do you agree with our proposals for LO in relation to NCAM and ANCAR?*

*NGGTQ13. Do you agree with our proposal not to set network capability targets for RII02?*

Agree with annual process. These need to consider the full range of FES scenarios and other projections including OGA production forecasts and the potential of existing and future exploration licensing rounds.

*NGGTQ14. Do you agree with the proposal to reduce entry baseline capacity at St Fergus?*

Do not agree. Removal of capability should only be subject to a relatively high evidential hurdle. The analysis in the DD is not reflective of known projects relating to UKCS and Norwegian gas. Similarly, the analysis needs to reflect a wide range of scenarios and maximum and minimum peak day flows rather than being based on broad annual averages and extrapolated trends. Propose that this decision is postponed to 2021 and forms part of the first ANCAR process as a test case rather than being embedded and “lost” in the final determination decision

*NGGTQ15. Do you agree with the proposal to reduce entry baseline capacity at Theddlethorpe?*

Acceptable

## Baseline allowances

Cost category	NGGT Proposed Baseline (£m)	Ofgem Proposed Baseline (£m)
Load related expenditure	11.59	2.44
Non-load related	898.74	517.51
Other costs	545.80	230.31
Non-op Capex	296.50	68.40
Network operating costs	389.51	379.65
Indirect costs	518.24	411.10
Ongoing efficiency	-57.92	-50.50
<b>Total</b>	<b>2,602.45</b>	<b>1,558.91</b>

## Project specific Items

*NGGTQ20. Do you agree with our proposal to reject the Blackrod Reinforcement project?*

No comments

*NGGTQ21. Do you agree with our proposed allowances for Load Related Expenditure?*

No comments

*NGGTQ22. Do you agree with our proposed GT Project Assessment Process?*

In general, the approach taken by Ofgem is comprehensive and detailed. However, this has led to a significant divergence between NGGT's evaluation of the system and that of Ofgem which is concerning. This is likely to have consequence for the monitoring of delivery and process against PCDs as discussed above, and in particular the overall NARMs assessment.

Potential deterioration of the assets and their performance is not desirable as this is likely to pass risks and additional costs to network users and consumers. Likewise, postponing necessary expenditure to future periods is undesirable and may increase the cost of projects and again pass risk to users and consumers in the meantime.

The detailed evaluation sheets accompanying the DD appear to give scope for potentially subjective judgements about costs being justified or not. Similarly it is not clear the extent to which the evidence on declining serviceability of assets (faults and failures) has been taken into account, especially as allowed expenditure is lower than the amounts actual spent in asset maintenance in the RIIO-1 period.

These elementary issues need to be explored further in setting the final determinations. It is not really acceptable for Ofgem and NGGT to have fundamentally different views of asset condition, risk and deliverables. We would encourage companies to engage with Ofgem's invitation that the "consultation nevertheless provides a final opportunity for companies to provide better justification, and we will consider these carefully ahead of Final Determinations."

NGGTQ23. Do you agree with our proposal to provide baseline funding for Hatton subject to us conducting further volume and cost assessment prior to our Final Determination?

Agree

NGGTQ24. Do you agree with our proposal to accept the need for investment, provide baseline funding for development work and assess the full project costs during RIIO-GT2 for the compressor projects at Stage 1 - Needs Case Assessment (Wormington, St Fergus, King's Lynn and Peterborough and Huntingdon)?

Agree

NGGTQ25. Do you agree with our assessment approach to asset health work, including our proposal to use a combination of baseline funding, PCDs and an UM for the various cost sub-categories?

Project Theme (£m)	NGGT Proposed Baseline	Ofgem Proposed Baseline	Ofgem Proposed UM
Valves	63.15	50.83	No
Compressors	113.69	69.51	No
Pipelines	143.53	112.13	No
Plant & Equipment	156.44	82.28	Yes
Civils	79.54	39.97	No
Electrical	28.48	20.58	No
Cabs	31.29	14.38	Yes
<b>Total</b>	<b>616.11</b>	<b>389.68</b>	

Please see the comments in response to NGGTQ22 above. There is some concern regarding the large differences for compressors and pipelines in particular, and also for civils where there is a security or HSE element to consider. The draft determination does not appear to have considered all the evidence, in particular on asset performance during RIIO-2. Where there are elements of doubt, these should be dealt before the final determination and, where necessary these may also need to be addressed through the UM approach.

NGGTQ27. Do you agree with our proposed approach to approve the need for investment, provide development funding and assess the full project costs through a UM during RIIO-GT2, for the Bacton, St Fergus subsidence and King's Lynn subsidence projects?

Dealing with the above projects through an UM is acceptable. However, the uncertainty in these cases is around the cost and specification of the projects concerned. All the above projects are important, and which need to be undertaken during the RIIO-2 period. Entry capacity needs to deal with all scenarios including continued UKCS production beyond the mid-2030s with OGA\BEIS forecasts (see above) suggesting 170TWh of UK production in 2035. Some of this is likely to be in the central and southern North Sea which may well be landed at Bacton as there remains considerable prospect for gas resources in those locations. The most recent OGA licensing round included a number of exploration blocks in these regions of the North Sea.<sup>4</sup>

<sup>4</sup> <https://www.ogauthority.co.uk/licensing-consents/licensing-rounds/offshore-licensing-rounds/#tabs>

*NGGTQ28. Do you agree with our proposed baseline allowances for Stopples, GRAID and decommissioning of redundant assets and compressors?*

No comments

*NGGTQ29. Do you agree with our proposed assessment approach and baseline allowances for non-operational Capex costs, including IT&T, STEPm, property and vehicle fleet investment?*

The reductions in capex allowances are very significant. This is not an area that has direct implications for OGUK members but, especially on IT&T, there would be concern if the system owner and operator was obliged to use obsolete or incompatible equipment as a result.

*NGGTQ30. Do you agree with our proposed allowances for Physical Security Capex and Opex?*

NGGT need to have sufficient revenue to comply with legislation on security and health and safety matters. In this regard the substantial difference between their assessment and the Ofgem proposals is concerning and requires resolution.

*NGGTQ31. Do you agree with our assessment approach and baseline allowances for NGGT's Opex costs, including network operation costs, BSC, CAI and Quarry and Loss?*

The large reductions in CAI costs are noted although many of these would be covered by the opex escalator UM.

*NGGTQ32. Do you agree with our proposed approach to Pensions costs?*

No comment.

*NGGTQ33. Do you agree with our proposed approach to assessing risk?*

An overall cap of 10% of project costs appears a reasonable contingency level.

*NGGTQ34. Do you agree with our proposed UM for incremental capacity, specifically the timing and content of the Pre-Application Notification stage, the Needs Case and Cost Assessment timings, and the need for an exceptional events mechanism?*

Agree.

*NGGTQ35. Do you agree with our proposed UM, materiality threshold and trigger for pipeline diversion costs?*

Agree

*NGGTQ36. Do you agree with our decision to retain a UM for Quarry and Loss costs relating to loss of development and mineral sterilisation only, and do you agree with our proposed UM parameters?*

Agree

*NGGTQ37. Do you agree with our proposed asset health UM, specifically basing the UM on improved quality of cost data and volume measurement and assessing costs ex post?*

Please see response to NGGTQ26. Ofgem may wish to consider a wider Asset Health reopener covering all asset categories.

*NGGTQ38. Do you agree with our proposed GT Opex escalator adjustment mechanism?*

Agree.

*NGGTQ39. Do you agree with the level of proposed NIA funding for NGGT? If not, please outline why.*

See section on innovation (core document question Q24-31).

## **Finance**

*FQ22. Do you agree with our proposals, including the policy alignment for GT and GD, and to recover backlog depreciation for GT RAV additions (2002 to 2021) over 20 years from the start of RIIO-2?*

The rationale for the adjusted depreciation profile is understood and it makes sense for this to be harmonised between GD and GT. However, this increases costs to end users and therefore does not sit well with the proposed reductions in asset health expenditure and the possible associated increases in risk to end users.

Ofgem should therefore reconsider the interface between different regulatory decisions to ensure that network users continue to receive the degree of reliability implied by the overall outcome of determination. Currently the combination of the different elements of the draft determination around existing gas assets could be taken as implying an inferior service for a higher price.

## **Gas Distribution**

### *Iron Mains Replacement*

The Iron Mains Risk Reduction Programme (IMRRP) is a key strategic investment by GDNs to meet Health and Safety requirements and allow for the distribution of decarbonised gases. Ensuring that this work is carried out in an effective and timely fashion should be a priority in the RIIO-2 period.

### *Hydrogen*

*GDQ46. What are your views on our consultation position to address bespoke decarbonisation of heat re-openers through our proposed innovation stimulus, Net Zero and Heat Policy re-opener mechanisms?*

*GDQ47. What are your views on the questions set out in paragraph 4.57 of this document in relation to large hydrogen projects?*

Please see the above sections on reopeners and net zero.

OGUK is currently working with government on a North Sea Transition Deal which will set objectives around carbon capture and Hydrogen production. As part of this discussion industry has proposed a decarbonised gas strategy aiming at around 50TWh, as noted in response to the government's Future of heat consultation (attached).

Gas DNOs will be of central importance in allowing for switching industrial and other users to decarbonised gas. The reopener mechanisms need to accelerate this process rather than being an additional regulatory gateway. Regulators and government will need to work together in new and agile ways to make rapid progress on many areas relating to net zero including large hydrogen projects.