



**Southern Gas Networks further submission
to Ofgem under special condition E7
of GDPCR1 for additional costs
under the TMA Re-Opener
June 2013**

CONTENTS

EXECUTIVE SUMMARY

- 1.0 INTRODUCTION
- 2.0 NEW PERMIT AUTHORITY COSTS
- 3.0 INCREASED COSTS DUE TO S74 CHARGES
- 4.0 LANE RENTAL COSTS – TRANSPORT FOR LONDON
- 5.0 VACEX AND NEW TECHNOLOGY TO REDUCE OCCUPANCY TIMES ON THE HIGHWAY
- 6.0 NEW SIGNAGE – REQUIREMENTS FOR GREATER COMMUNICATION

APPENDIX A NEW PERMIT AUTHORITY COSTS

APPENDIX B 

APPENDIX C DESCRIPTIONS OF TMA TEMPLATED COSTS IN NEW PERMIT SCHEMES

APPENDIX D NOTES AND REFERENCES

EXECUTIVE SUMMARY

At the start of GDPCR1 Ofgem accepted that proposed new and enhanced Streetworks legislation could expose Network Operators to material increases in expenditure. To mitigate such events an uncertainty mechanism was incorporated into the Licence which, under limited circumstances, enabled GDNs to submit to Ofgem the justification for and quantification of an amendment to price control allowances. A successful Income Adjusting Event submission would result in the recovery of incremental costs on a historic and future forecast basis.

Three years into GDPCR1, 2011, our Network business had incurred a level of additional TMA expenditure which exceeded the materiality threshold and duly submitted a paper outlining the incremental costs incurred as a direct result of the new and enhanced TMA legislation. In their decision letter, 20th December 2011, Ofgem acknowledge the principles of the claim and based upon their assessment of efficient costs determined an income adjustment of £22.7m¹.

At this point Ofgem recognised that an expansion in the application of Streetworks legislation and enforcement to a wider geographic area could result in further incremental costs to the Network which it would be justified in seeking to recover. At such a time we would be required to make a second Income Adjusting Event application. For the period ending 2012/13 we believe significant additional costs have been incurred and that these are above and beyond those allowed for by Ofgem in their notice of decision letter dated the 20th December 2011.

Further more, these developments point towards continued increased expenditure which will impact network performance into the new price control period 2013-2021, RIIO-GD1. These costs were not allowed in the recent GD1 Final Proposals and we anticipate a future submission to Ofgem for the recovery of these and new Streetworks costs.

The additional costs identified and incurred in GDPCR1 amount to a total of **£1.81m¹**. While the exact quantum is not yet known it is anticipated the changes identified in this submission will generate material increased operating costs in GD1 over and above that incorporated within the price control Totex allowances. These new costs will include:

- New Permitting Authorities (e.g. Surrey and East Sussex)
- Lane rental schemes (e.g. Kent County Council)
- New legislation

As these are a matter for the RIIO-GD1 licence these are not included in this current submission to Ofgem. None of these costs formed any part of the business plan submissions for existing highway authorities on which Ofgem's final proposal allowances were based. They therefore represent an incremental cost increase.

Additional Costs for GDPCR1

There are five areas of costs related to TMA legislation that are additional and incremental to the Ofgem's TMA determination of December 2011. None of these costs were incorporated into the future forecast allowance adjustment and none are included in GD1 allowances. These are:-

1. New Permit Schemes Authority costs
2. Lane Rental costs – Transport for London
3. Increased costs due to the increase in s74 charges
4. Vac Ex - new technology to reduce costs
5. New signage - requirement for greater communication

These costs are summarised in the table below.

Section	Cost area	GDPCR1 £m
2	The total cost resulting from the introduction of new Permits schemes not included in the 2011 TMA income adjusting event	£0.02m
3	Costs incurred following the introduction of the Lane Rental Scheme by Transport for London in May 2012	£0.74m
4	Additional s74 charges incurred since 2012 as a result of the increase in charges above those allowed under GDPCR1	£0.23m
5	Investment in new technology to avoid significant cost increases resulting from drive by TfL and the London Mayors Office to reduce the occupancy times on the highway (Vac Ex Machines)	£0.67m
6	Complying with revised Code of Conduct to provide enhanced communication to road users through unique signs and banners	£0.14m
Total		£1.81m

1. INTRODUCTION – STREETWORKS LEGISLATION

The New Roads and Street Works Act 1991 (NRSWA) provides a legislative framework for street works carried out by Statutory Undertakers when working on the highway. Our Network business is one such Statutory Undertaker.

Various changes were brought about by the Traffic Management Act 2004 (TMA), which tightened the regulatory framework giving Highway / Permit Authorities more power to co-ordinate, control and direct works with the aim of minimising disruption to the road user from road works. The Traffic Management Act was enacted in April 2008.

The appointment of dedicated Traffic Managers by each Local Authority, as required by TMA, has resulted in step changes to the way that NRSWA requirements are administered by Authorities, thus significantly increasing our operating costs. In addition, the introduction of Permitted Schemes and further changes such as Lane Rental Schemes has further increased the operating costs of our Network.

The first gas distribution price control for 2008-2013 (GDPCR1) enabled gas network operators to apply to Ofgem to adjust their revenues to accommodate increased costs associated with the introduction of the Traffic Management Act. In June 2011, we submitted a paper detailing the costs associated with the TMA re-opener.

In Ofgem's decision letter dated 20 December 2011, we were allowed additional TMA costs for 2008-2013 of £22.7m. Ofgem also recognised the uncertainty over the number of Local Authorities that may implement new permit schemes within our network boundaries and allowed an opportunity for a further review.

Since the original paper, we have experienced further increases in costs due to the introduction of the new Permitted Schemes, the introduction of lane rental, increased rates under s74 and expansion of the London Mayor's Code of Conduct.

At the date of the first GDPCR1 TMA submission the additional costs for section 74A of New Roads and Street Works Act (NRSWA) 1991 (lane rental) and section 74 NRSWA 1991 (section 74 NRSWA daily charge rates) were uncertain. These were therefore not taken into consideration within our application by Ofgem.

This paper sets out the detail behind these additional costs.

2. NEW PERMIT AUTHORITY COSTS

Since the notice of decision letter by Ofgem of December 2011 and prior to the end of GDPCR1, an additional five Local Authorities have introduced Permit Schemes. These are all within our Network boundaries.

Four London Boroughs have introduced the London Common Permit Scheme and Hertfordshire County Council has introduced the East of England Common Permit Scheme. The commencement details of these schemes are as follows:

- Hertfordshire County Council (East of England Scheme) - November 2012

The following four London Boroughs have implemented the London Common Permit Scheme

- London Borough of Merton - 14th January 2013
- London Borough of Sutton - 14th January 2013
- London Borough of Bexley - 18th February 2013
- Royal Borough of Kingston - 4th March 2013

The total cost of new Permits schemes introduced, including operational costs and administration, in GDPCR1 is £23,000. The full break down in costs can be seen in Appendix A.

As some of the new schemes introduced by Authorities have only been in operation for very short periods prior to the end of GDPCR1 the gradual roll out and implementation has limited the size of the costs incurred in the relevant time frame. We anticipate that as these schemes mature the volume and associated costs of Permitry will increase further during GD1.

Our claim under GDPCR1 incorporates minimal admin and management incremental costs. As highlighted above we have been broadly able to accommodate the gradual roll out of the new schemes to date within our existing structures. However as these schemes impact our network further we believe the overhead burdens will increase. This will form part of our anticipated future claim under GD1.

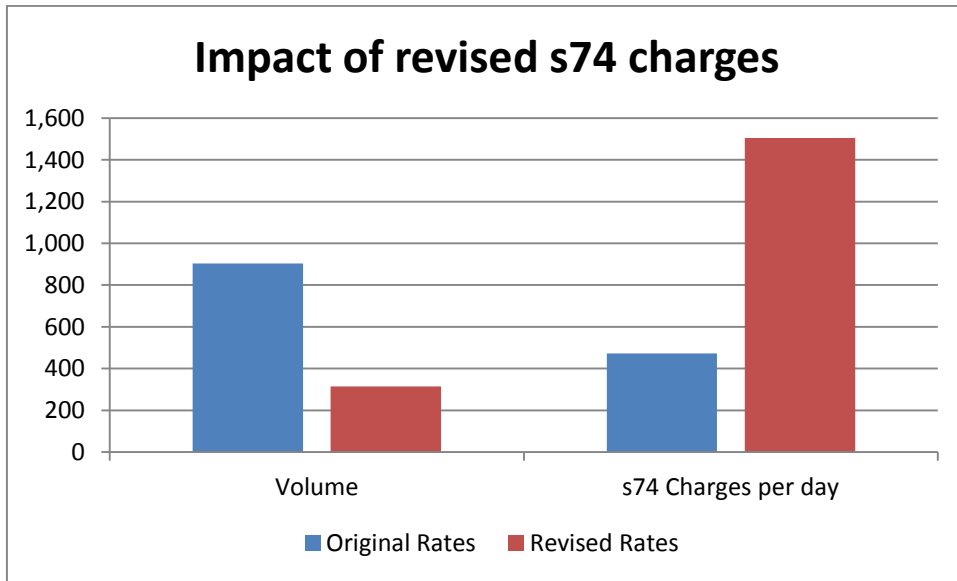
We are also aware of other Local Authorities (East Sussex County Council and Surrey County Council) planning to introduce Permit Schemes this year. The additional costs associated with these new schemes have not been included in this submission.

For reference, the elements which feed into the Permit Authority costs are shown in Appendix C. These are identified, captured, collated and verified in the same way as our previous submission in 2011. This section is included for reference and to demonstrate the alignment with previous submissions.

3. INCREASE COSTS DOES TO S74 CHARGES

The S74 charges were increased fourfold in October 2012 which resulted in additional cost of £232k being incurred by SGN during GDPCR1 which were not included in the original submission.

The quantum of these increased charges is included in our supporting templates to this income adjusting event submission. The impact of the increased rates per day is evident from the following graphic.



Derived from Streetworks template: June 2013

While as an undertaker we must comply with the charging regime in place we do and will continue to challenge the validity of each charge in order to ensure our business and ultimately our customers are only exposed to justifiable costs. Processes exist within our operational functions to ensure this approach is effective. They include:

- Depot and construction processes to confirm boards and barriers cleared, managing the notice period etc
- Revised duration challenges responding to Highway Authority requests for reduction in reasonable periods
- Duration extensions requested as soon as it is predicted work requirements will change on site

Recently we have identified and successfully challenge a number of large s74 charges received. They have resulted in reductions of over 10 times the original sum claimed.

4. LANE RENTAL COSTS – TRANSPORT FOR LONDON

4.1. DIRECT LANE RENTAL COSTS

The Department for Transport (DfT) stated that they will approve an initial three lane rental schemes to allow a period of time for review and to learn lessons before further scheme are introduced. These schemes are:

- The TfL scheme was approved and introduced on the 11th June 2012 (TLRS)
- The Kent Lane Rental Scheme was approved and implemented on the 28th May 2013
- The location of the third scheme has yet to be announced

The Transport for London Lane Rental Scheme (TLRS) is designed to minimise Streetworks in traffic-sensitive locations by applying a daily charge for each day that the street is occupied by the works. The daily charge does not apply or will be reduced if the works take place outside traffic sensitive times.

We are therefore incentivised by TLRS to change our operational practices and minimise occupation of streets at traffic- sensitive times and at the most traffic sensitive locations. This exposes our business to changes in:

- Working hours – deploying resources out of hours, incurring premium working time
- Management and control of resources – to avoid working within chargeable periods we must proactively manage planned and unplanned work to less disruptive periods
- Scheduling and balancing of resources – being able to release manpower and equipment in order to tackle necessary work in sensitive areas at the off peak periods

We experience additional costs incurred as follows:-

1. The Lane Rental charge – stipulated by legislation and dependent on duration and type of work
2. Additional depot costs (management, administration and dedicated industrial resources) avoiding the lane rental charges.

The Lane Rental Charges to the end March 2013 are £0.38m.

The TLRS applies to all activities that require a permit and to works in a carriageway or cycle track, plus works in a footway or verge which encroaches on a carriageway or cycle track. The TLRS does not apply to works that are carried out in a footway or verge of a lane rental chargeable road that do not involve any occupation of a carriageway or cycle track. Such occupation includes use by any associated plant, vehicles, or materials, or for any temporary arrangements for providing a walkway for pedestrians, as a result of or as part of the works. In the design of all our distribution projects and works we aim to

identify the potential for lane rental charges and where ever possible approach the implementation in order to avoid or minimise the final costs.

Charging commences on the day the works starts and continues until the works clear notice is sent. For immediate works the first 24 hours of the emergency are non chargeable. As shown in section 4.2 we have been proactive in managing and reducing the duration for which our unplanned activities affect lane rental areas.

The rates charged vary from £800 a day to £2,500 per day and Permit charges do not apply when Lane Rental charges are applied.

The total Lane Rental charges received in 2012_13 since the introduction of the scheme are £0.38m. Due to the Olympic embargo on Streetworks while the scheme became live in June 2012 the full impact was not felt until September 2012. The direct lane rental costs included in this submission reflect that delay.

To ensure we are only exposed to justifiable and efficient streetworks costs we proactively review and validate all Lane Rental Charges prior to the invoice being paid. Where appropriate we will dispute such charges in order to ensure the costs are incurred efficiently. [REDACTED]

Our claim submitted under GDPCR1 only relates to the London TRLS. While we are aware of plans to introduce the Kent County Council Scheme this had not commenced by the end of GDPCR1 and therefore we anticipate its inclusion in the first streetworks income adjusting event in GD1.

4.2. STRUCTURAL CHANGES

As noted above we have been proactive in managing and minimising Lane Rental costs. Since the introduction of the TfL Lane Rental scheme we have introduced significant changes in the way our operations functions manage day to day work activities. These cover the range of network functions, including both repair and new connections works, on all roads subject to lane rental charges in order to ensure lane rental charges are minimised.

A specialist team was established in each of the three depots affected by the scheme to take control of all work activities on lane rental roads. This includes a designated Team Manager and designated Repair Teams. Given the reactive nature of unplanned gas activity, primarily repair response, we have designated these resources as exclusive to lane rental response. This enables each of the three areas within the TfL scheme to respond quickly and complete works within the nil charge period or minimise over run into subsequent days.

Measures implemented by our depots to reduce or avoid lane rental charges include:-

Measure	Benefit	Incremental Cost
Carrying out work outside core lane rental times	Avoid charging period and subsequent lane rental costs	
Using new technology to increase production	Avoids over run of works into chargeable periods	Acquisition, running and maintenance costs of technology
Hiring specialist kit and operators for work in the highway	Targeted specialist equipment to reduce job times in specific locations	Cost of contract
Improved management controls to monitor on site activities	Efficient use of designated labour and reduction of job delays through work process scheduling, i.e. reinstatement	
Once a start date has been agreed we will work 24/7 until the work is complete	Minimises total time in chargeable carriageway	

These measures generate incremental costs and for the period 2012/13 these equate to £0.36m across the three depots affected by the scheme. We believe the investment in these resources are justifiable by the control of and reduction in potential lane rental charges as we undertake necessary work across our networks and deliver the outputs our Stakeholder require.

5. ADDITIONAL EXPENDITURE TO AVOID LANE RENTAL CHARGES/S74 CHARGES.

The London Mayors Office and TfL are active in using their powers under TMA to reduce the time that utilities are permitted to occupy the highway. This is viewed as a significant benefit to the road users in and around London through reduced traffic congestion. To achieve this outcome the available days utilities are allowed to occupy the highway are restricted under the permit scheme. This is coupled with a strong incentive under the Lane Rental legislation to minimise time working in the carriageway. Together they force road undertakings to seek out all options to minimise roadworks where ever commercially viable.

Whilst we continue to be exposed to pressure to reduce road work durations it should be noted that our required output levels, repairs and replacement activities, within Permit Scheme and TLRS areas have not reduced. To minimise the cost impact on our business we have actively pursued innovative solutions and developed new techniques to reduce occupancy times on the highway.

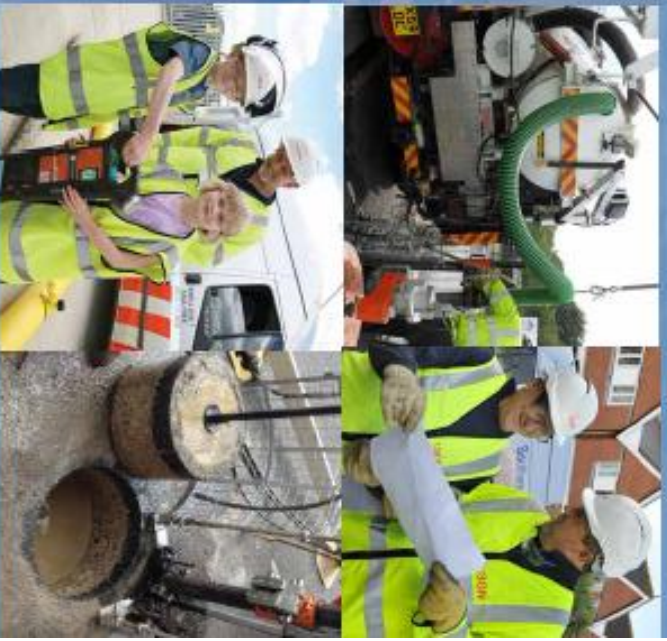
As a forward thinking network operator we are committed to continue this approach through GD1 and are actively pursuing exciting new opportunities to significantly reduce the impact our streetwork activities have on our Stakeholders. By the end of GDPCR1 we have successfully innovated and introduced the following to facilitate reduced times:

- Magnetometers – to enable accurate joint location
- Core and Vac machines - to enable rapid keyhole excavation
- Long Handled Tooling - to work on gas mains from the road surface

The development costs of this technology were funded through the IFI mechanism. To move this into operational production we have invested in four VAC EX coring and excavation machines at a total cost of £0.67m. These are targeted at use on first time permanent repair gas escapes within the carriageway. We will continue to develop use of these machines across our network and are continually learning and improving on their performance.

Keyhole technique... a gas repair in pictures

1. The coring device...
2. Taking out the core...
3. Vacuuming out the remaining excavation material
4. Neat hole left...
5. ...making the repair using long handled tooling
6. ...checking we meet the required standards
7. ...original core goes back in
8. ...clean almost invisible finish
9. ...you'd hardly know we were there



**Reducing inconvenience and
increasing efficiency**

Keyhole technology for gas mains repairs



6. NEW SIGNAGE - REQUIREMENT FOR GREATER COMMUNICATION

As a condition of the continuation of our streetworks within London we are a signatory to the London Code of Conduct. This was introduced in 2009 and has been revised on a number of occasions since. In September 2011 the code was revised to incorporate a range of pledges made by the Mayor of London. Within this revision was a commitment to provide bespoke signing on all our Streetworks in order to communicate information to road users and the travelling public about our activities on site.

While appropriate signage was already part of working in the highway this requirement is above and beyond the obligations contained in the Safety at Streetworks and Road Works Code of Practice (red book). The principles of the London Code of Conduct have subsequently been adopted by HAUC (UK) and rolled out across the country in 2012.

The revision to the code of conduct commits undertakings to the following:

'The signatories to this Code recognise the importance of adequate signage at all works and the value of providing clear and concise information to the public including details of the works, who is carrying out the works with relevant contact details, and their likely completion date. The Mayor's Code of Conduct will ensure that works promoters will provide this information to the public together with an update on the progress of works.'

'A good example of an information board should include:

- *The works promoter's name*
- *The contractor's name*
- *The associated permit number that the works are being carried out under*
- *A plain English description of the works that are being carried out*
- *The expected completion date of the works*
- *Contact numbers – for both non urgent and urgent enquires*
- *The working hours²*

Enhancing our signage to comply with best practice has and will continue to expose our business to additional costs. These include developing and purchasing the material (examples are shown below) and have resulted in additional costs in GDPRC1 of £0.14m.

These costs are ongoing and were not included in the RIIO submission.



APPENDIX A: NEW PERMIT AUTHORITY COSTS

Four London Boroughs have joined the Common London Permit Scheme and East of England permit scheme has been implemented since the Southern Gas Network TMA re-opener June 2011. While these were forecast within the submission in 2011 only existing authorities at that time were allowed for in Ofgem's determination. These therefore also are not part of the allowances granted under the final proposals for GD1. We anticipate subsequent TMA submissions within GD1 to recover the increasing costs for these and further Permit schemes.

- Hertfordshire County Council
- London Borough of Bexley
- London Borough of Sutton
- London Borough of Merton
- Royal Borough of Kingston Upon Thames

The following table identifies the actual permit costs of new schemes.

	Permit Costs (£)					Total (£)
	Immediate	Minor	Standard	Major/PAA	Variations	
Bexley	741	313	560	0	327	1,942
Sutton	2,724	2,056	1,161	104	93	6,137
Kingston	847	194	199	530	62	1,831
Merton	3,107	450	1,205	1,392	1,739	7,892
Hertfordshire	291	40	66	715	31	1,143
Total	£7,710	£3,054	£3,190	£2,740	£2,250	£18,944

The following table identifies the additional costs associated with the new permit authorities since their implementation.

New permit authorities	Total (£'000's)
Permit costs	18.9
TMA template costs	3.5
Admin costs	0.5
Totals	22.9

All prices 2009/10

APPENDIX B: [Redacted]

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APPENDIX C: DESCRIPTIONS OF TMA TEMPLATED COSTS IN NEW PERMIT SCHEMES

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C.3 Supervision – Pre-site Surveys

In order to meet the increasingly stringent planning & Opening Notice/Permitry requirements of Local Authorities it has been necessary to significantly improve the quality & quantity of information gathered whilst conducting pre-site surveys by both planning & operational staff.

Item one of the TMA templates captures the Construction Managers estimated costs of completing the improved pre-site surveys associated with each project.

C.4 Supervision – Site meetings

The step change in hours spent by our planning & operational staff attending co-ordination & multiple site meetings has increased significantly since the appointment of Traffic Managers by Local Authorities.

C.5 Other Items:-

C5.1 Special Signage

As part of most TM schemes, local authorities now request special Advanced Warning road signs to communicate forthcoming road works with the regular road users. Increasingly, TFL & other LA's are requesting the use of specialist electronic variable message (VMS) signs to be displayed on site – these are very expensive to hire or buy and they are very vulnerable to extensive vandalism.

The improved quality of Traffic Management schemes implemented as a result of the introduction of TMA now requires increasing numbers of special diversion & traffic direction signage which is non standard and often site specific. LA's also regularly request additional information signage for shoppers/local traders & businesses.



VMS Sign



Special Sign

C5.2 Parking Bay Suspensions

Many Local Authorities have now outsourced the administration of parking bays & parking meters; this has led to a significant increase in the charges imposed for suspension of parking bays and meters (Wandsworth are particularly vigorous with their charges). In the past LA's generally made an administration charge only for parking suspensions, now charges are made based on lost revenue as well as admin costs

C5.3 Temporary traffic orders

The use of formal Temporary Traffic Road Orders (TTRO) is now more common particularly for Road closures, Bus/Cycle lane closures, reversal of one way streets or banned left & right turns etc.



C5.5 Modifications to existing Traffic signals

TM schemes often overlap existing Traffic signals which need to be temporarily decommissioned or maintained with amended signal programming.

C5.6 Bus Stop Suspensions

In the past temporary suspension of Bus Stops simply required a request for a bus stop to be bagged by the local Bus Company and for them to supply a temporary bus stop to be placed at the nearest convenient location. Bus stop suspensions now require formal Traffic Orders.

C5.7 Other TMA Costs

Various infrequent costs not included within the above 'other operational costs'.

APPENDIX D: NOTES AND REFERENCES

- 1 All references to costs and expenditures within this paper, unless otherwise indicated, are in 2009/10 prices.
- 2 Mayor's Code of Conduct for Road Works

www.tfl.gov.uk/roadusers/reportastreetfault/934.aspx

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