

Consultation

SGN Non-operational IT Capex Re-opener Consultation			
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We are consulting on SGN's Non-operational Information Technology (IT) Capex Re-opener application. We would like views from people with an interest in electricity and gas transmission, distribution networks, and from other stakeholders and the public.

This document outlines the scope, purpose and questions of the consultation and how you can get involved. Once the consultation is closed, we will consider all responses. We want to be transparent in our consultations. We will publish the non-confidential responses we receive alongside a decision on next steps on our website at [Ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations). If you want your response – in whole or in part – to be considered confidential, please tell us in your response and explain why. Please clearly mark the parts of your response that you consider to be confidential, and if possible, put the confidential material in separate appendices to your response.

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Contents

1. Introduction	4
What are we consulting on?	4
Consultation approach	4
Context and related publications	5
Consultation stages	5
How to respond	6
Your response, data and confidentiality	6
General feedback	7
How to track the progress of the consultation	7
2. Assessment against Re-opener Requirements	9
3. Needs case for the proposed project	11
Overview of needs case	11
Demonstration of needs case	12
Our initial view of needs case	13
4. Assessment of options and justification for the proposed project	15
Consideration of project options and methodology	15
“Do nothing” considerations	15
Options for new telecommunications networks	16
Options for power provision	17
Summary of SGN preferred option	17
5. Cost assessment	19
Breakdown and justification of costs	20
Summary	26
6. Consultation proposal summary	27
7. Next Steps	29
Appendices	29
Appendix 1 – Consultation questions	30
Appendix 2 – Privacy notice on consultations	31

1. Introduction

What are we consulting on?

1.1. We are consulting on making adjustments to SGN Non-operational Information Technology (IT) Capex¹ outputs and allowances under the RIIO-2 Non-operational IT Capex Re-opener ("the Re-opener").

1.2. In accordance with Special Condition 3.7 ("Non-operational IT Capex Re-opener")², SGN submitted a Re-opener application for both its licensees, Southern Gas Networks and Scotland Gas Networks, to request approval of its proposed IT projects and associated allowances. SGN has provided evidence to justify its IT Plan through cost reports and supporting documentation.

1.3. Since its submission in April 2021, SGN has also provided additional information through a combination of meetings and Supplementary Question (SQ) responses. Throughout this document, all monetary figures are in 2018/19 prices except where otherwise stated.

Consultation approach

1.4. We are issuing this consultation in response to SGN's Re-opener application. The consultation sets out our assessment of that application and the adjustments we are proposing to make to SGN's licences (Southern Gas Network; Scotland Gas Network), including the addition of PCD outputs and adjustments to allowances. Currently SGN's licence condition for Non-operational IT capex Re-opener applications does not have a PCD component and does not allow for the addition of PCD outputs by way of direction. Therefore, we intend to implement our proposals from this consultation by way of a statutory licence modification process, which will allow us to adjust allowances and add PCD outputs at the same time. We expect to bring forward this statutory consultation later this year.

¹ Expenditure on new and replacement IT assets, including Hardware & Infrastructure and Application Software Development.

² <https://www.ofgem.gov.uk/publications/decision-proposed-modifications-riio-2-transmission-gas-distribution-and-electricity-system-operator-licence-conditions>

1.5. We reviewed the Re-opener application against the application criteria contained within the Non-operational IT Capex Annex in the RIIO-2 Re-opener Guidance and Application Requirements Document ("the Guidance").³

1.6. We considered the SGN's proposals and their justifications for the funding requested in accordance with our principal objective and statutory duties. In line with the Guidance, our assessment of SGN's proposals covers the three following areas:

- the needs case;
- the options assessment and the justification for the proposed project; and
- the efficient costs for the proposed project.

Context and related publications

1.7. The scope of this consultation is limited to SGN's Non-operational IT Capex Re-opener. This document is intended to be read alongside:

- the RIIO-2 Final Determinations – Core Document (REVISED)⁴,
- the RIIO-2 Draft Determinations – Core Document⁵,
- SGN's Licence Special conditions, and
- RIIO-2 Re-opener Guidance and Application Requirements Document.

Consultation stages

³ <https://www.ofgem.gov.uk/publications/re-opener-guidance-and-application-requirements-document-0>

⁴ https://www.ofgem.gov.uk/system/files/docs/2021/02/final_determinations_-_core_document_revised.pdf

⁵ https://www.ofgem.gov.uk/system/files/docs/2020/07/draft_determinations_-_core_document_redacted.pdf

1.8. This consultation will open on 01 September 2021 and close on 01 October 2021. We will review and publish the non-confidential responses after the consultation closes. We will endeavour to publish our decision by the end of October 2021.

How to respond

1.9. We want to hear from anyone interested in this consultation. Please send your response to the person or team named on this document's front page.

1.10. We've asked for your feedback in each of the questions throughout. Please respond to each one as fully as you can.

1.11. We will publish non-confidential responses on our website at www.ofgem.gov.uk/consultations.

Your response, data and confidentiality

1.12. You can ask us to keep your response, or parts of your response, confidential. We'll respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.

1.13. If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you *do* wish to be kept confidential and those that you *do not* wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published. We might ask for reasons why.

1.14. If the information you give in your response contains personal data under the General Data Protection Regulation 2016/379 (GDPR) and domestic legislation on data protection, the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 4.

1.15. If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

General feedback

1.16. We believe that consultation is at the heart of good policy development. We welcome any comments about how we've run this consultation. We'd also like to get your answers to these questions:

1. Do you have any comments about the overall process of this consultation?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Were its conclusions balanced?
5. Did it make reasoned recommendations for improvement?
6. Any further comments?

Please send any general feedback comments to stakeholders@ofgem.gov.uk

How to track the progress of the consultation

You can track the progress of a consultation from upcoming to decision status using the 'notify me' function on a consultation page when published on our website.

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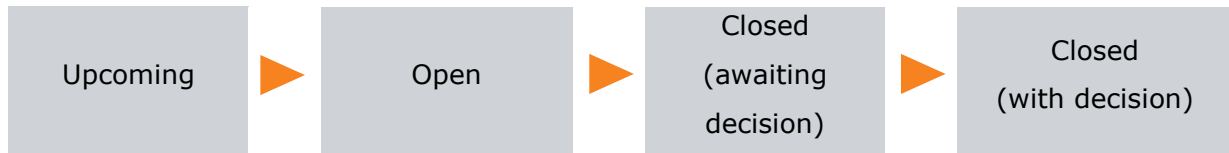
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Consultation - SGN - Wholesale Line Rental Phase-out (non-telemetry)

Once subscribed to the notifications for a particular consultation, you will receive an email to notify you when it has changed status. Our consultation stages are:



2. Assessment against Re-opener Requirements

2.1. This Chapter sets out Ofgem’s assessment of SGN’s application against both general requirements that apply to all Re-opener applications and specific requirements for the Non-operational IT Capex Re-opener application (see Table 1 below).

Table 1: Re-opener application requirements

Document	Requirement	Has the requirement been met?
Special Condition 3.7	To explain how the adjustment requested would improve its Non-operational IT Capex.	Y
	To explain the basis of the calculations for the adjustment requested to allowances.	Y
	To give details of anticipated business benefits derived from any risk reduction as a result of the proposed activities.	Y
	To provide such detailed supporting evidence as is reasonable in the circumstances, which must include: <ul style="list-style-type: none"> • delivery plans; • a prioritisation programme; • market and industry cost comparison; and • anticipated business benefits derived as a result of the proposed activities 	Y
Special Condition 9.4	To prepare applications for Re-openers in accordance with the Re-opener Guidance and Application Requirements Document.	Y
RIIO-2 Re-opener Guidance and Application Requirements Document	Assurance requirements: <ul style="list-style-type: none"> • To provide applications that are accurate, unambiguous, complete and concise • To provide written confirmation from a suitable senior person of the same • To provide a point of contact for each application. 	Y

	To publish applications within 5 working days of submitting it to Ofgem with only necessary redactions; unless this would pose a risk to national security.	Y
	To provide clear answers on: <ul style="list-style-type: none"> • Why an adjustment is justified • What that adjustment should be 	Y
Appendix 2: Non-operational IT (IT) Capex Re-opener Application Guidance	To provide information relating to the Needs Case of the adjustment requested, including: <ul style="list-style-type: none"> • Alignment with overall business strategy and commitments • Demonstration of needs case 	Y
	To provide information relating to the Options Selection of the adjustment requested, including: <ul style="list-style-type: none"> • Consideration of project options and methodology • Preferred option details 	Y
	To provide Cost information relating to the adjustment requested, including: <ul style="list-style-type: none"> • Consideration of options • Breakdown of costs of preferred option • Justification and efficiency of costs 	Y

2.2. In formulating its Re-opener submission, SGN has described the related circumstances in accordance with Special Condition 3.7 and these are covered in the following sections. In summary, we consider that SGN has looked to minimise additional Non-operational IT Capex, whilst seeking to address external changes which would increase business risk. SGN has provided a costed plan setting out the adjustment, underpinned by market data in order to address the external changes in a phased prioritised manner.

2.3. Ofgem has deemed that SGN's submission has met all the requirements set out in both the applicable Special Licence conditions and the detailed Re-opener application criteria set out in the Guidance as listed in the Table above. In the following Chapters we set out the assessment in more detail and our conclusion based on the evidence submitted by SGN.

3. Needs case for the proposed project

Consultation Question 1: Do you agree with our view of the validity of the needs case for the SGN Non-operational IT Capex Re-opener application for Wholesale Line Rental Phase-out (non-telemetry sites)?

3.1. In this Chapter we detail our assessment of the needs case for the project proposed in the Non-operational IT Capex Re-opener application.

3.2. The Guidance states that as part of the Re-opener application licensees must demonstrate alignment between their Non-operational IT Capex plans and their overall business strategy and commitments.⁶ We considered the information provided by SGN in its Re-opener application, as well as evidence gathered through SQs, to assess whether SGN has satisfactorily demonstrated the needs case for the proposed project.

Overview of needs case

3.3. This Re-opener submission identifies the need to transform the communications technology for SGN's gas profiler and logger systems, to ensure it can maintain its network in a safe and reliable manner and manage the network pressure appropriately.

3.4. At present the SGN's communications network uses a number of commercial off-the-shelf technologies that are connected to the Public Switched Telephone Network (PSTN) operated by Openreach. This Openreach network provides SGN with the infrastructure to relay information about pressure within the gas network and this is used to manage the network pressure. The current approach is suited to the PSTN since it has low bandwidth requirements (i.e. it does not need to continuously transmit large volumes of data) and the equipment has low power requirements. It is powered over the line from the local telephone exchange, negating the need for the installation of a separate supporting electricity supply. At

⁶ Appendix 2, para 1.1 – 1.4

present SGN utilises the Wholesale Line Rental (WLR) service from Openreach to provide this communications network.

3.5. Due to recent agreements between BT and Government via Ofcom on the national rollout of fibre-based broadband, Openreach (as a wholly owned subsidiary of BT Group) will no longer need to maintain both the PSTN and fibre-broadband networks in the medium term. PSTN related services based on the legacy copper line technologies will be decommissioned and the WLR services used by SGN will be withdrawn. When the legacy copper-line services are turned-off, unless SGN can put alternative communications equipment and associated power supplies in place, it will be unable to fulfil its license obligations to maintain the safety of its gas network by managing pressures remotely and providing periodic meter readings.

3.6. When SGN's RIIO-2 business plans were being prepared, Openreach's published position was that they did not intend to retire copper lines until it had switched off the PSTN in December 2025. However, this programme was then accelerated by Openreach with new dates proposed in September 2020 for a rolling quarterly program of exchanges being switched off beginning in 2022. Therefore, the Re-opener application intends to rectify this dependency on technology that will soon be withdrawn.

3.7. SGN proposes that if the Re-opener application proposals are implemented, its remote pressure monitoring systems will use the latest communication technology and not be reliant on WLR. It should be noted that there is no overlap between the deliverables set out in this Re-opener and the IT deliverables set out by SGN in its business plan submission at the end of 2019.

Demonstration of needs case

3.8. Openreach has set out a programme under which they will be turning-off all WLR services by 2025. In January 2021, Openreach published the first list of exchanges impacted with subsequent updates scheduled each quarter. The first of these 'stop-sell' notices⁷ for

⁷ The term 'stop sell' is used by Openreach to signify stopping the sale of certain Openreach products. This is different from product withdrawal, as under stop sell, any end customer who already has the product, will be able to continue using it (until it is withdrawn). If a product is impacted by stop sell, this limits the supply of new lines, but also restricts service changes such as working line takeovers, start of stopped lines, migrations, Communication Provider transfers, addition of broadband to copper voice lines, bandwidth modify, or addition of lines and channels to existing installations.

exchanges takes effect in June 2021. This will culminate in a national 'stop-sell' in 2023 and a removal of service 2 years later. For exchanges with a 'stop-sell' announced prior to 2023 there will be a removal of service 2 years after the 'stop-sell' was announced for that exchange.

3.9. The legacy copper-line network provides data connectivity to remote sites and also provides the electricity charge needed to power the telecommunication equipment / trickle-charge the battery. There is a need to identify alternative telecommunication technology to the copper-line services along with a suitable source of power to run alternative telecommunication equipment.

3.10. The consequences of the withdrawal of the WLR services by Openreach without SGN investment in new equipment are:

- an increase in the volume of gas lost related to any leaks. This "shrinkage" has both an environmental impact and a financial penalty on SGN.
- This "shrinkage" also represents a greater safety risk to the general public and SGN personnel.
- More rigorous procedures for SGN personnel in order to safely undertake routine (and emergency) maintenance activities resulting in potential inefficiencies.
- Additional operational costs due to SGN engineers attending sites to manually reset pressure monitoring equipment.

Our initial view of needs case

3.11. We consider that the needs case put forward by SGN has a genuine business impact that was not foreseeable at the time of the RIIO-2 business plan submissions and needs to be resolved.

3.12. We agree that to enable the operation of a safe and efficient network that SGN requires telecommunication services such as those previously procured through Openreach and that their subsequent withdrawal creates the need for an alternative solution and therefore a valid needs case exists. We agree at that time there was a reasonable expectation by SGN, supported by statements from Openreach, that the WLR services would remain in place until the PSTN was switched off at the end of 2025 and there remained a possibility that this could be further delayed.

3.13. SGN has considered several options to address the needs case. We set out in the following Chapter our view on the comparison of these options carried out by SGN.

4. Assessment of options and justification for the proposed project

Consultation Question 2: Do you agree with our technical assessment of the range of solutions to meet the needs case?

Consultation Question 3: Do you agree with our minded-to view of the solution proposed by SGN?

4.1. In this Chapter we detail our assessment of the options considered by SGN and its justification for the chosen project.

4.2. As set out in the Guidance,⁸ as part of the Re-opener application SGN was required to demonstrate consideration of project options and methodologies for its Non-operational IT Capex projects and to provide justification for its preferred option.

Consideration of project options and methodology

4.3. To address the needs case discussed in the previous chapter, SGN applied a stepped options process which consider the following in sequence:

- “Do nothing” considerations
- Options for new telecommunications networks
- Options for power provision.

“Do nothing” considerations

4.4. In taking a “Do nothing” approach SGN would not be able to meet its obligation of operating a safe and efficient network, which they did not consider to be a viable approach. As part of this option, they also considered mounting various challenges to the proposed

⁸ Appendix 2, para 1.5 – 1.11

changes to the status quo. This would however delay implementation starting and increases the risk of not completing site conversion in time, should the challenges be unsuccessful.

4.5. The needs case can also be met without installing alternative communications technology on SGN's network by increasing the pressure of the distribution network. The key consequences as set out in the previous Chapter include environmental impacts from gas leakage and operational inefficiencies.

4.6. We agree that "Do nothing" is not a viable option for the continued safe provision of a public service, due to the loss of visibility that SGN would have of the performance of the network and the negative consequences of mitigating actions they would have to undertake.

Options for new telecommunications networks

4.7. SGN then considered technical options to address the loss of telecommunications' capability. SGN was involved in the first Openreach trial of WLR withdrawal in the Salisbury area. SGN took the opportunity to use its Old Sarum site to better understand the impact of the withdrawal of legacy copper-line services, engaging a range of 3rd party solutions and services to ascertain viable alternatives following the withdrawal of WLR.

4.8. Based on this experience a limited set of pros and cons were developed by SGN in order to compare current mobile data, fibre and satellite technologies and combined with a high-level costing. This resulted in the recommended use of mobile data in preference to fibre or satellite as the default telecommunications mechanism.

4.9. We are minded to concur with SGN's technology assessment, though it could have been more expansive if SGN had included emerging technologies, such as 5G or micro-satellite that provide Internet of Things (IoT) networks at low cost. However, these do not yet have ubiquitous coverage to be considered as a full solution. We also note that Openreach has yet to publish any pricing guidance for low bandwidth applications and SGN has had to price against the current range of high performance bandwidth domestic packages which to them offer relatively poor value for money, and as a consequence this would currently appear overly expensive. It would be expected that over time, as fibre rollout progress, a number of lower cost providers will enter the market to provide cheaper products (though this may be constrained by Openreach wholesale pricing policy).

4.10. However, we are concerned that mobile data may not be suitable for all locations due to coverage issues, but also because Mobile Network Operators may start to phase out 2G GSM networks over the next decade as newer network are rolled out.

4.11. We raised these issues with SGN as part of the SQ process. In order to address the coverage issue SGN intends to use a blended technology approach and will deploy other, potentially more costly, technologies into areas with poor mobile coverage. With regard to network obsolescence, Ofcom has yet to announce any retirement dates, but SGN has had early discussions with equipment suppliers who have provided assurances that their current product roadmaps avoid having to replace equipment in the short to medium term.

Options for power provision

4.12. Having determined the recommended technology approach, SGN then considered mechanisms to power the equipment, within which there is the potential of mains or battery provision (supported either by a solar panel or monthly operational replacement of discharged batteries). The outcome of this analysis was heavily driven by the capex costs of deployment and consideration of ongoing additional operational costs.

4.13. We are minded to accept SGN's assessment of battery options. However, we are concerned that its preferred use of solar powered battery provision is not suitable for a number of locations.

4.14. We raised these concerns with SGN as part of bilateral discussions and it became clear that they consider the use of Mobile Data with solar powered batteries as their baseline design option. SGN intends to complete surveys of all sites in order to determine the use of secondary options (such as fibre and mains power) to be deployed where the use of the preferred option is not feasible. It is expected that this will be completed in time for the next Re-opener window in 2023. Therefore, where expected costs, as a result of changes in the equipment mix exceed the proposed 10% contingency budget, SGN has indicated they may seek further funding. We agree that it is appropriate that non-standard options which materially exceed the baseline design option be included in the January 2023 Re-opener window.

Summary of SGN preferred option

4.15. SGN's preferred option is the use of a Mobile Data solution with solar powered batteries, typically housed within an appropriately security rated enclosure or kiosk. Individual site surveys will determine the practicality of the preferred option and will use a number of templated designs to use alternate communications bearers (such as fibre), power provision (such as mains) and physical mounting arrangements where sites are constrained by either mobile coverage, solar coverage or site security.

Technical feasibility and consumer benefit

4.16. The proposed approach is building on established commercial off the shelf technologies and is relatively low risk. The installation of equipment at site will require a number of different civils designs and the extent of possible variations are covered within specific risk items within the project budget.

4.17. The migration from WLR technology does not provide any direct increased consumer benefits, it does however mitigate against a number of environmental and safety aspects which would indirectly impact the consumer.

4.18. Our view is that SGN has considered an appropriate range of options; although the range is not exhaustive, the conclusion is consistent with other industries which have implemented low cost, low bandwidth telecommunications solutions using standard technologies. The use of a subsequent Re-opener window affords SGN the ability to potentially change track if emerging technologies become viable in the intervening period. We therefore support the proposed solution.

5. Cost assessment

Consultation Question 4: Do you agree with our cost assessment of the SGN Non-operational IT Capex Re-opener for Wholesale Line Rental Phase-out (non-telemetry sites)?

5.1. This Chapter sets out our assessment of the submitted costs of the Non-operational IT Capex Re-opener application. The results represent our current view of an economic and efficient solution.

5.2. As set out in the Guidance⁹, SGN was required to provide a breakdown of the allowance requested in the Re-opener application, and to demonstrate that these costs are justified and efficient.

5.3. Having demonstrated the needs case and determined their preferred technical option, SGN then set out their programme of work to migrate to their proposed new telecommunications technology.

5.4. The proposed approach follows a sequential delivery model of initial design, procurement, site validation and a phased site migration. In addition to major project milestones, actual progress can be monitored through completion of site surveys and fitment.

5.5. Initially SGN will ensure enough information is available from field benchmark activities to design and implement the various types of installations and enable detailed planning of project execution. Completion of generic designs for various types of installations identified will be undertaken.

⁹ Appendix 2, para 1.12 – 1.20

5.6. Alongside the equipment procurement activity, SGN will survey each site to confirm communications coverage, installation type, design variance and any necessary permits to undertake change at the site.

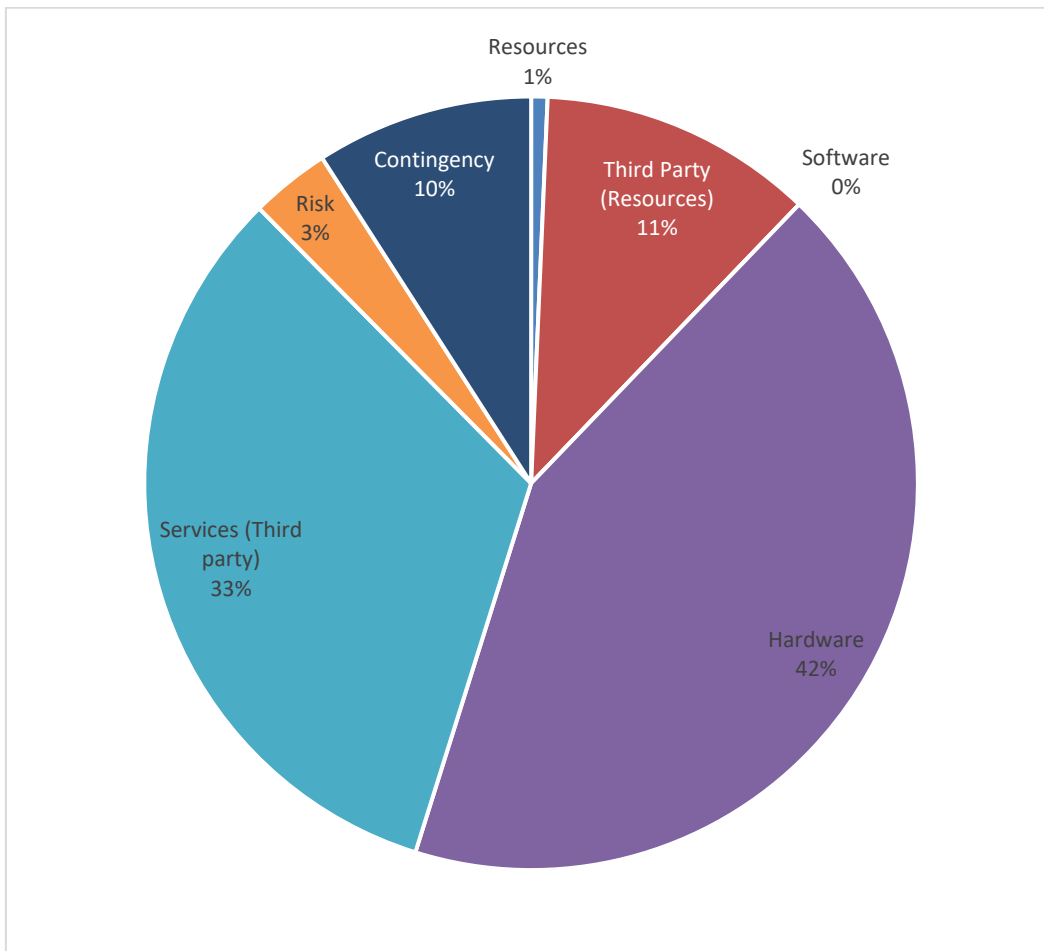
5.7. A phased deployment plan has been proposed – which will be aligned with the Openreach 'Stop sell' notices, initially with areas where there is adequate coverage of GSM network and only the modem unit needs changing being prioritised. A final phase will address remaining sites where GSM or alternative technology will be required to ensure completion of all sites impacted by the change including the scenarios where the modem unit cannot be replaced without changing out the entire profile unit.

Breakdown and justification of costs

5.8. SGN's submitted costs for this project were comprehensively broken down into a phased project approach, covering a logical stepped approach from initial design and benchmarks, through site surveys to the staged site installation. Costs for the project have been broken down into:

- Applicable Project Phase, covering the individual work packages:
 - WK1 - Initiation and Design & Field Benchmark Activities
 - WK2 - Tender / Procurement Process
 - WK3 - Validate PMAC Site inventory / Survey
 - WK4 - Pressure Mgmt Site Migration 1
 - WK5 - Pressure Mgmt Site Migration 2
 - WK6 - Pressure Mgmt Site Migration 3.
- Resources, covering SGN internal resources such as Programme Manager, Business Architect and Engineering Design Manager.
- Third Party resources from the contractor market, such as Network and Telecoms Architects, Engineering Design and Operations Engineers.
- Hardware, covering the proposed equipment and associated hardware for installation (e.g. Oscilloscopes, cables).
- Services such as procurement and civils.
- Risk, predominantly covering the need for additional civils related work at complex locations (assumed to be 15% of sites).

5.9. There are no defined software costs, though an element has been recorded as a risk if existing SGN's systems or applications are not suitable for recording the results of site surveys. A high-level breakdown of costs is shown in the figure below:



5.10. Within these categories, further breakdowns are provided at a granular level of spend. Costs are presented as average figures rather than ranges.

5.11. In considering costs, we have looked at both the supporting information provided as part of the Re-opener application, but also the information submitted in relation to other projects, from both SGN and the wider industry, assessed as part of the RIIO-2 Final Determination.

5.12. The proposal has a higher than average proportion of non-SGN staff. SGN has confirmed through the SQ process that this was driven by the project timing as the Re-opener was submitted outside of the usual staff planning process driven by the RIIO-2 Final

Determination. Where roles can be compared with the rate cards used at RIIO-2 for internal staff, the submitted costs represent an approximate 50% premium – but we understand and accept the need to use external staff for this work due to the timing issue identified.

5.13. The main area of concern within the resource profile is the approach to undertake the extensive set of site surveys, with them being undertaken as a separate activity rather than being incorporated into the regular site visit cycle to undertake annual maintenance checks. This introduces inefficiency through duplication of travel, site access arrangement and site familiarisation.

5.14. SGN has provided the following set of activities to be completed as part of the site survey activity in response to a SQ:

- Surveyors to be trained in:
 - (DSEAR¹⁰ – Haz3, Kiosk construction, street furniture construction, NRASWA¹¹ requirements – Civils, check land registry etc).
- Travel to and from site.
- Identify site layout, take photographs.
- Identify suitable location for communications cabinet and solar panel.
- Identify and record measurements of any required cable and ducting requirements.
- Identify and record measurements, locations of cabinet and solar panel, recording all civils and NRSWA requirements.
- Carryout a HAZ3 (DSEAR) assessment. (Need to ensure the site remains complaint with SR25¹²).
- Complete site plan for project.

5.15. Given that external resources will be used for undertaking site surveys and there are inefficiencies introduced by separating the task from the annual maintenance check process, our view is that end of day travel should be included within the contractual arrangements rather than charged on a time and material basis. This has the benefit of freeing up additional working time and allows an increase in the number of sites that can be surveyed (on average) per day. In addition, effort levels have been calculated by SGN on a nominal basis

¹⁰ Dangerous Substances and Explosive Atmospheres Regulations

¹¹ New Roads & Street Works Act 1991

¹² Security Rating

of 3,800 sites rather than the 3,733 sites to be converted, we see no justification for determining the effort level on a nominal figure of 3800 as opposed to the known sites.

5.16. The profile of the internal resources has been changed from that deployed within projects funded through the RIIO-2 Final Determination. The costs of internal staff have typically increased, with a greater emphasis on governance and experience of management of the supply chain. However, internal staff costs make up a very small proportion of the overall costs (<1%) and are not significant driver of expenditure. As a result, we have not made any adjustments for this figure.

5.17. In our view, the workplan's resource profile is appropriate, though costs have increased due to the use of external rather than internal resources, we understand and accept the need to use a different resource profile given the timing of the project being applied for under the re-opener in SGN's business cycle. There are however some areas where more efficient use of external resource could result in cost reductions.

5.18. SGN has proposed to install new enclosures in some locations rather than attempting to retrofit equipment. We agree that this is a sensible approach, in order to protect the integrity and relative security of the unit, failure of which would impinge consumer services and safety. It should also simplify site installation procedures during the later stage of the project. Although SGN has yet to commence procurement of additional equipment, they have sought to validate costs through quotes from their existing supplier base. These quotes are of a similar order of magnitude to other products on the market, although they do not include any volume related discounts.

5.19. As a result, we would expect the open procurement approach proposed by SGN to introduce an element of competition, especially given the large volumes required and drive these costs down. We therefore propose a reduction of £0.3m to reflect the potential cost benefit of open competition by SGN as this represents the volume discount achieved in similar 3rd party contract negotiations as confirmed by SGN through our SQ process.

5.20. SGN has a clear understanding of the number of sites that need to be converted, however it is hard to align these sites with their associated Openreach exchange due to a mix of historic record availability and Openreach business processes. At present Openreach has announced future 'stop-sell' dates at 300 sites nationwide of which 35 exchanges are within SGN's Scottish and Southern Regions.

5.21. SGN has proposed an aggressive site installation profile in lieu of there being a clear roadmap from Openreach for 'stop-sell' at each exchange, though this is countered by a hard 'stop-sell' nationally for WLR in 2023. Although 'stop-sell' incurs some inconvenience in SGN's operations, the major impact is when a threshold number of lines at each exchange has been migrated from legacy copper-line services that Openreach are permitted to close any remaining legacy services. Due to the infancy of Openreach's programme, the time taken to reach this point is unpredictable at present and SGN is being suitably prudent in their planning approach, with the activity to be completed by Openreach's target date of the end of 2025. It is expected that as the Openreach programme progresses, a more informed approach to the profile of site installations can be taken, with the peak of site conversion being smoothed over time.

Level of detail of cost information

5.22. SGN provided a detailed breakdown of roles per project phase, effort and day rates, along with assumed equipment prices based on low volume quotes from suppliers.

5.23. Risks related to site complexity and additional surveys, design work and installation costs have been considered, but are assumption based at present and will be realised once the site surveys have completed. The risk budget of £528k (18/19 prices) is just under 4% of the programme budget.

5.24. SGN has also applied a blanket 10% contingency to the project, which includes the costing for the Risk budget, cost of equipment through procurement and the final installation phase which is expected to be part of a subsequent Re-opener application to reflect use of alternate technologies. We therefore propose a further cost reduction to reflect that SGN will be using the subsequent Re-opener window once they have an understanding of the status of sites and evidence of discrepancies against their current assumptions.

5.25. We agree that the level of cost breakdown and information is proportionate to the stage of the project given the wider Openreach programme.

5.26. We have assessed the breakdown of costs and propose a funding reduction in relation to the following areas:

- the efficient use of external resources being used for site surveys, in that start and end of day travel times should be excluded from the cost calculation.

- the number of sites to be surveyed.
- cost savings through open competition in the equipment procurement and related discounts due to volume of equipment being procured.
- the blanket application of contingency to all elements of the projects, especially those areas which are subject to future re-opener windows or against quoted supplier rates for communications equipment and site visits.

Summary

5.27. The Table below details SGN's requested funding, our proposed reductions, and our proposed allowances against each of the components. Specifics of the work packages have been redacted for commercial sensitivity.

Table 2: SGN's requested funding and Ofgem's proposed allowances

Workstream	SGN requested allowance (£m)	Ofgem Proposed Adjustments (£m)				Ofgem Proposed Allowances (£m)
		Contingency reduction	Equipment procurement reduction	Site survey efficiency	Reductions arising from adjusting the number of site surveys	
WK1	0.544	0.001				0.543
WK2	0.139	0.000				0.139
WK3	1.678	0.044		0.165	0.012	1.457
WK4	6.837	0.318	0.147			6.373
WK5	4.734	0.229	0.114			4.391
WK6	1.391	0.126	0.032			1.233
	15.323	0.719	0.293	0.165	0.012	14.135

5.28. Allowances & any subsequent reductions have been split across SGN's two licences pro-rata on the number of sites within each geographical area.

6. Consultation proposal summary

6.1. We are proposing to add PCDs as a result of this Re-opener application given the specific nature of the investment proposed and the ability to measure the quantifiable outputs of sites surveyed and successfully converted. In addition, given the materiality of the Re-opener application it is important to ensure that the investment outcomes are achieved and ensure consumer value is protected. PCDs were not attached to the IT investments approved at Final Determination given the challenges of measuring and presenting quantifiable evidence of the applicable success criteria in a regulatory environment for a traditional IT project and the prevalence of agile delivery methods to deliver these programmes of work, these types of investment are often delivering additional capabilities or efficiencies upstream in the operating model and as such will be subject to other contributory factors. Subsequently the licence condition for Non-operational IT capex Re-opener applications did not have a PCD component and did not include within the consultation provisions direction making power for the ability to add PCD outputs.

6.2. We therefore propose to use the statutory licence modification process to give effect to our proposals in this consultation so that we can amend allowances and add PCD outputs for Re-opener applications at the same time. We expect to bring forward this statutory consultation later this year.

6.3. Table 3 below outlines our proposed adjustments to SGN's Re-opener allowance requests, while Table 4 outlines our PCD proposals. All values are in 18/19 prices.

Table 3: SGN's proposed allowances

Regulatory Year	21/22	22/23	23/24	24/25	25/26	All years
Scotland Gas Networks plc	£0.631	£2.040	£1.857	£1.105	£0.345	£5.978
Southern Gas Networks plc	£0.861	£2.783	£2.534	£1.508	£0.470	£8.156

Table 4: SGN's Non-operational IT (IT) Capex PCD Table

Output	Delivery Date	Measure	Allowance (£m) 18/19 prices
Scotland Site Surveys Completed	31/3/23	1,579 Scotland sites surveyed	0.62
Southern Site Surveys Completed	31/3/23	2,154 Southern sites surveyed	0.84
Scotland initial site fitment	31/3/24	790 Scotland sites converted	2.7
Southern initial site fitment	31/3/24	1077 Southern sites converted	3.68
Scotland site fitment completed	31/3/26	1,579 Scotland sites converted (789 additional sites converted from initial fitment)	2.38
Southern site fitment completed	31/3/26	2,154 Southern sites (1077 additional sites converted from initial fitment) converted	3.25
Total			13.47

7. Next Steps

7.1. We welcome your responses to this consultation, both generally, and in particular on the specific questions set out in Chapters 3, 4 and 5. Please send your response to: RIIO2@ofgem.gov.uk. The deadline for response is 01 October 2021.

7.2. We will conclude our assessment of SGN's Non-operational IT Capex Re-opener after receipt of the consultation responses and endeavour to publish our decision by the end of October 2021.

Appendices

Index

Appendix	Name of appendix	Page no.
1	Consultation questions	30
2	Privacy notice on consultations	31

Appendix 1 – Consultation questions

Question 1: Do you agree with our view of the validity of the needs case for the SGN Non-operational IT Capex Re-opener application for Wholesale Line Rental Phase-out (non-telemetry sites)?

Question 2: Do you agree with our technical assessment of the range of solutions to meet the needs case?

Question 3: Do you agree with our minded-to view of the solution proposed by SGN?

Question 4: Do you agree with our cost assessment of the SGN Non-operational IT Capex Re-opener for Wholesale Line Rental Phase-out (non-telemetry sites)?

Appendix 2 – Privacy notice on consultations

Personal data

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

1. The identity of the controller and contact details of our Data Protection Officer

The Gas and Electricity Markets Authority is the controller, (for ease of reference, "Ofgem"). The Data Protection Officer can be contacted at dpo@ofgem.gov.uk

2. Why we are collecting your personal data

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

3. With whom we will be sharing your personal data

(Include here all organisations outside Ofgem who will be given all or some of the data. There is no need to include organisations that will only receive anonymised data. If different organisations see different set of data then make this clear. Be as specific as possible.)

4. For how long we will keep your personal data, or criteria used to determine the retention period.

Your personal data will be held for (be as clear as possible but allow room for changes to programmes or policy. It is acceptable to give a relative time e.g. 'six months after the project is closed')

5. Your rights

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data
- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it
- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3rd parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

6. Your personal data will not be sent overseas (Note that this cannot be claimed if using Survey Monkey for the consultation as their servers are in the US. In that case use “the Data you provide directly will be stored by Survey Monkey on their servers in the United States. We have taken all necessary precautions to ensure that your rights in term of data protection will not be compromised by this”.

7. Your personal data will not be used for any automated decision making.

8. Your personal data will be stored in a secure government IT system. (If using a third party system such as Survey Monkey to gather the data, you will need to state clearly at which point the data will be moved from there to our internal systems.)

9. More information For more information on how Ofgem processes your data, click on the link to our “[Ofgem privacy promise](#)”.