

Decision

NGET's Bespoke Tower Steelwork and Foundations Re-opener Decision

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This document sets out our¹ decision on National Grid Electricity Transmission's (NGET's) Bespoke Tower Steelwork and Foundations Re-opener submission under Special Condition (SpC) 3.33 of NGET's Electricity Transmission Licence. We published a consultation on our initial assessment of this bespoke re-opener submission on 17 February 2023, and received one response. Following considerations and a review of this response, we have decided to maintain our consultation position and accept the needs case and optioneering put forward by NGET but will award no additional funding under this re-opener.

We have published the non-confidential response alongside this decision document.

¹ The terms 'we', 'us', 'our' refer to the Gas and Electricity Markets Authority (the Authority). Ofgem operates under the direction and governance of the Authority.

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1. Introduction

Section summary

This section introduces our decision document, outlining relevant context and related publications.

Context and related publications

- 1.1 Network companies are natural monopolies. Effective regulation of privatised for-profit monopolies is essential to ensure they cannot unfairly exercise their monopoly power to the detriment of their customers. This is particularly important in the case of essential utilities, such as energy, where consumers have no choice on whether or not to pay what they are charged. It is therefore crucial that an effective regulator protects energy consumers by controlling how much network companies can charge their customers. Ofgem does this through periodic price controls that are designed to ensure network companies are properly incentivised to deliver the best possible outcomes for current and future energy consumers. This includes ensuring that consumers only pay for investments that are needed and that they do not overpay for those investments.
- 1.2 The RIIO²-T2 price control period (which runs from 1 April 2021 to 31 March 2026) includes a range of Uncertainty Mechanisms (UMs) that will allow us to assess application for further funding during the RIIO-T2 period as the need, cost or timing of work becomes clearer.
- 1.3 At RIIO-2 Final Determinations (FD),³ NGET were awarded baseline funding of £20.089m. This comprised of £5.708m for tower steelwork and £14.381m for tower foundations. Only provisional baseline funding was provided for these asset categories because the results of surveys, which had not yet been completed, were required to determine the appropriate volume of steelwork and foundation interventions. This baseline funding allowed NGET to complete the survey works and to carry out immediately required interventions. A re-opener was created to facilitate extra funding, if necessary, once the surveys were available to inform more accurate intervention proposals.

² RIIO stands for Revenue = Incentives + Innovation + Outputs

³ https://www.ofgem.gov.uk/sites/default/files/docs/2021/02/final_determination_nget_annex_revised.pdf - Chapter 3

- 1.4 The Bespoke Tower Steelwork and Foundations Re-opener was created to allow NGET to request additional funding during the RIIO-2 price control period in relation to tower steelwork and foundation interventions as per their Licence SpC 3.33.⁴ This was subject to NGET performing condition assessments across a range of assets to ensure a clear picture of the network towers and foundations before any re-opener submission.
- 1.5 NGET submitted an application under the re-opener on 28 July 2022 and, following assessment of the application, we published our consultation on our draft proposals on 17 February 2023.⁵ NGET’s request equates to funding for an estimated [redacted] tonnes of steelwork and [redacted] foundation repairs. The consultation invited feedback on our initial views of the needs case, optioneering, and on the additional cost allowances. Our initial position was to approve the needs case and options, but we disagreed with some of the costs submitted. We considered the majority of costs submitted by NGET were reasonable. However, we proposed to remove a proportion of these costs as we considered some of the activities to be Closely Associated Indirect (CAI) activities and are therefore covered by the RIIO-2 Opex Escalator (OE) Mechanism.⁶ We proposed to remove CAI activity costs from the funding total and, as a result, our assessment of efficient costs was less than already provided for in baseline funding. We therefore proposed to not award NGET additional funding for this project.
- 1.6 This document sets out our consultation position, consultation response summary and our final decision.
- 1.7 This document is intended to be read alongside:
- NGET Bespoke Tower Steelwork and Foundations Re-opener submission;⁷
 - Consultation on Bespoke Tower Steelwork and Foundations Re-opener submission from National Grid Electricity Transmission;
 - RIIO-2 Re-opener Guidance and Application Requirements Document; and ⁸
 - NGET’s electricity transmission licence, Special Licence Conditions.⁹

⁴ <https://www.ofgem.gov.uk/industry-licensing/licences-and-licence-conditions>

⁵ <https://www.ofgem.gov.uk/publications/riio-2-bespoke-tower-steelwork-and-foundations-nget-re-opener-consultation>

⁶ https://www.ofgem.gov.uk/sites/default/files/docs/2021/02/final_determination_nget_annex_revised.pdf – As set out in SpC 3.36 of the ETO’s licence. Details of the use of OE is set out full under Chapter 4 of the ET sector annex.

⁷ <https://www.nationalgrid.com/electricity-transmission/who-we-are/riio2-business-plan>

⁸ <https://www.ofgem.gov.uk/publications/re-opener-guidance-and-application-requirements-document-0>

⁹ <https://www.ofgem.gov.uk/licences-and-licence-conditions>

2. Consultation response and our decisions

Section summary

This section summarises our consultation position, consultation response and our final decision on the needs case, optioneering and costs put forward by NGET in their re-opener submission.

General

- 2.1 We received one response to the consultation, from NGET, and have published this on our website.
- 2.2 We have summarised our consultation positions and our final decisions on each issue below, having considered the response we received.
- 2.3 Our decision is to maintain our consultation position and therefore to provide no additional funding under this re-opener application:

Table 1: Tower Steelwork and Foundations Re-opener funding decision, £m, 2018/19 prices

	NGET submitted costs	Ofgem Adjustments	Ofgem assessed efficient costs	Existing baseline allowances	Additional Allowances
	A	B	C = A + B	D	E = MAX(0, C - D)
Steelwork	17.704	-3.811	13.893	20.089	
Foundations	4.149	-1.289	2.860		
Pre-reopener submission surveys	1.910	-	1.910		
T3 climbing surveys	0.349	-	0.349		
Total	24.112	-5.100	19.012	20.089	-

Our consultation position, summary of responses and our final decisions

Needs case

Consultation position

- 2.4 We agreed with the needs case set out by NGET and considered there was sufficient justification for the tower interventions proposed in the re-opener submission.

Consultation response

- 2.5 NGET agreed with our assessment of the needs case.

Decision

- 2.6 We have decided to maintain our consultation position and consider that the needs case presented by NGET suitably demonstrates that the proposed tower interventions are required and in the best interests of consumers.

Options and justification for the proposed project

Consultation position

- 2.7 We were satisfied that NGET had considered an appropriate range of possible alternatives to address the needs case. We considered the most cost-effective solution for providing repair works in the interest of consumers was put forward. This was to replace all Grade 5 and 6 bars identified to be in poor condition, targeted whole tower section replacement, where a significant number of critical bars are in close proximity to other secondary corroded bars on earthwire peaks, and targeted foundation repairs.

Consultation response

- 2.8 NGET agreed with our optioneering assessment.

Decision

- 2.9 We have decided to maintain our consultation position and approve the preferred option selected by NGET.

Costs for the proposed project

Consultation position

- 2.10 We were satisfied with the majority of costs submitted. However, did not agree with NGET’s classification of certain costs (totalling £5.1m) as direct activity costs as they should have been correctly classified as CAI costs. CAI costs are not eligible for funding under this re-opener as they are funded through the OE mechanism.¹⁰ We therefore proposed to disallow these CAI costs.
- 2.11 Consequently, our cost assessment for this project was £19.012m. This is less than the baseline funding already awarded in RIIO-2 FD (£20.089m), and we therefore proposed to award no additional funding for this re-opener application.

Consultation response

- 2.12 NGET disagreed with our minded-to view of the re-opener costs for two main reasons:
- a. It disagreed with our application of the OE mechanism, arguing that contractor indirect costs should be treated as direct costs for these purposes, and therefore that we were wrong to disallow these costs; and
 - b. It argued that a portion of the works that it included within its application was additional to what it has been funded to deliver through baseline allowances, and that it should therefore be eligible for additional funding under this re-opener mechanism for these additional works.
- 2.13 In support of its view that its application included works that were unfunded in baseline (b. above), NGET submitted an alternative breakdown of its costs. This included a separation of the works that it claimed to be currently unfunded (NGET forecast cost: £4.115m) from the originally submitted full towers portfolio (NGET forecast cost: £24.112m). NGET claim the XM route, one of the original eight routes submitted, is unfunded and requires additional funding to refurbish.

Decision

- 2.14 Our position on the application of the OE mechanism (a. above), the reasons in support of that position including our response to NGET’s views are set out in detail in our decision on the licence modification associated with NGET’s 2022

¹⁰ See our decision on NGET’s 2022 Medium Sized Investment Project (MSIP) applications (Chapter 2) for explanation of the Opex Escalator Mechanism <https://www.ofgem.gov.uk/publications/decision-ngets-2022-msip-re-opener-applications>

MSIP applications.^{10,11} This decision, in so far as it relates to the OE, should be read in conjunction with those decisions.

2.15 We maintain the £5.1m classified by NGET as direct activity costs are CAI costs and are not eligible for funding under this re-opener as they are funded through the OE mechanism. Our cost assessment therefore remains £19.012m for this project as we have removed the incorrectly classified CAI costs from the cost total.

2.16 In coming to our decision, we also considered:

1. the workloads that NGET has been funded to deliver through baseline allowances; and also
2. whether NGET’s revised re-opener proposals are for a materially greater workload than was funded through baseline allowances.

Workloads funded through baseline allowances

2.17 Our FDs did not specify precise workloads or identify specific circuits or towers intended to be funded through baseline allowances. Our FDs simply state that baseline funding is provided “*to allow survey works and immediate interventions to continue*”.

2.18 NGET received £20.089m in direct activity baseline allowances. We have estimated that this would have been sufficient to carry out:

- [redacted] tonnes of tower steelwork replacement; and
- [redacted] tower foundation replacements.

These estimates are based on the requested workload volumes in NGET’s RIIO-ET2 business plan, and the percent of costs allowed at FDs. We have calculated what percentage of costs have been awarded in baseline allowances when compared to the original RIIO-2 business plan requests. We have then used this cost percentage to estimate the implied volumes of work, in steelwork tonnes and number of tower replacements, that would be sufficiently funded by the baseline allowance. It should be noted that these volumes assume no efficiency adjustments in NGET’s allowances, and therefore are likely to underestimate the volumes that could efficiently be delivered through baseline allowances. These calculations are presented in Appendix 1 Table 2 of this document.

¹¹ See our licence modifications to give effect to decision on NGET’s 2022 MSIP Applications (Chapter 2) for further explanation of the Opex Escalator Mechanism - <https://www.ofgem.gov.uk/publications/decision-modify-special-conditions-electricity-transmission-licence-held-national-grid-electricity-transmission-plc>

Additional re-opener workloads and allowances

- 2.19 The re-opener is intended to assess whether additional costs are required for tower steelwork and foundations. As per RIIO-2 FDs NGET Annex¹², the purpose of the re-opener is *“to allow NGET to seek funding for a range of steel and foundation works on overhead line route”* the benefit being that it *“ensures an appropriate level of funding is provided following receipt of sufficient levels of asset data from NGET.”*
- 2.20 Furthermore, in RIIO-2 FDs core document¹³ the purpose of default re-opener design parameters, was set out as *“re-openers allow network companies to receive additional allowances whenever there is more certainty about requirements. Where deemed necessary they also facilitate the adjustment of allowances by the Authority.”* Moreover, *“to decide, within the price control period, whether changes in allowance are needed.”*¹⁴ This design parameter allows us to look at the full picture of works and determine whether works have appropriate funding and ultimately protect consumers from unnecessary additional costs.
- 2.21 NGET’s application under this re-opener was to carry out the following total workload volumes over the RIIO-ET2 period:
- [redacted] tonnes of tower steelwork replacement, and
 - [redacted] tower foundation replacements.
- 2.22 Using unit cost weighted averages to compare the above requested workload volumes against our implied volumes calculations detailed in paragraph 2.18 above, indicates that NGET is now proposing approximately 4% more interventions than already funded through baseline allowances (28% more tower steelwork and 33% fewer tower foundations). Further explanation of our analysis and calculations can be found in Appendix 1.
- 2.23 Given the uncertainty around this estimate, including our assumption of no efficiency adjustment on baseline allowances, in our view, a 4% volume difference is likely to be well within the margin of error for this analysis.

¹² https://www.ofgem.gov.uk/sites/default/files/docs/2021/02/final_determination_nget_annex_revised.pdf - Chapter 4, page 87

¹³ https://www.ofgem.gov.uk/sites/default/files/docs/2020/12/final_determinations_-_core_document.pdf - Chapter 7, page 57

¹⁴ https://www.ofgem.gov.uk/sites/default/files/docs/2020/12/final_determinations_-_core_document.pdf - Chapter 7, page 56

- 2.24 This analysis further confirms our consultation position, i.e. that NGET has been sufficiently funded to carry out these works through baseline allowances.
- 2.25 NGET’s revised cost breakdown, submitted alongside its consultation response and discussed in paragraph 2.13 above, does not explain why the selected route put forward (£4.115m) is new work above what has already been awarded in baseline allowances. The baseline allowance given at FD was not assigned to specific routes or works at the time, and we therefore do not agree with NGET’s claim that one route within the entire portfolio is now unfunded.
- 2.26 We similarly do not agree with NGET’s identification of specific routes within the entire towers portfolio and the claim that these are currently unfunded pieces of work. Our analysis has shown the £20.089m NGET received in baseline funding at FDs is sufficient to carry out the entire portfolio of works forecast by NGET to be required during RIIO-ET2.
- 2.27 We have therefore decided that it would not be in the best interest of consumers to award any additional funding under this re-opener application as per our consultation position. As no additional funding is to be awarded, we do not need to make licence updates to the TSF_t term in accordance with SpC 3.33 of NGET’s licence.

Appendices

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Appendix 1 – Interventions volume assessment

A1.1 Intervention volumes that could be carried out through baseline funding have been estimated using RIIO-2 business plan data to estimate the unit costs.

A1.2 Additional intervention volumes have been estimated by calculating the difference between current total proposed work volume and baseline funded volumes (estimated as per paragraph A1.1 above).

A1.3 By applying the estimated unit costs, we have estimated the value or over/under-funding.

A1.4 The Unit Cost ratios have been used to calculate the Weighted volume increase.

A1.5 Our calculations are listed in Table 2 below.

Table 2: Intervention volume estimations

		Tower Steelwork (tonnes)	Tower Foundations (towers)	Total
RIIO-2 Business Plan	Costs (£m)	[redacted]	[redacted]	[redacted]
	Volumes (tonnes or towers)	[redacted]	[redacted]	-
Baseline allowances	Allowances (£m)	[redacted]	[redacted]	[redacted]
	% of funding request	27%	11%	19%
	Implied volumes	[redacted]	[redacted]	-
Reopener submission	Volumes requested	[redacted]	[redacted]	[redacted]
	Increase on baseline volumes	+28%	-33%	N/A
	Weighting (based on unit costs)	1.000	0.743	N/A
	Weighted volume increase	+28%	-24%	+4%