

Decision

Decision to modify Special Condition 3.14 Asset health Re-opener of National Gas Transmission Plc's gas transporter licence

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This document sets out our decision and rationale to modify Special Condition (SpC) 3.14 Asset health Re-opener (Aht) and SpC 1.1 Interpretation and definitions of National Gas Transmission Plc's (NGT) gas transporter licence (the Licence).

This decision has been informed by the responses we received following publication of our statutory consultation on 25 March 2024. We are publishing the responses we received and the statutory notice to modify the Licence alongside this decision.

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1. Introduction

Context and related publications

1.1. This document sets out our decision and reasons to modify SpC 3.14 Asset health Re-opener (Aht) and SpC 1.1 Interpretation and definitions of the Licence granted to NGT. These modifications will permit NGT to seek additional funding for asset health interventions on "Valves" through the Asset health Re-opener for the St Fergus gas terminal. They also extend our ability to true-up costs related to Valves¹, Compressor Cabs² and Plant And Equipment³ for an additional year to cover the first three years of the price control period, 1 April 2021 to 31 March 2024.

1.2. This document follows up on the statutory consultation⁴ we published on 25 March 2024 setting out the proposed modifications, their reasons and effects. In this statutory notice we set our views of the issues raised in the single response received.

1.3. NGT have submitted two applications⁵ seeking adjustments to allowances for interventions on Valves, Compressor Cabs and Plant And Equipment at the St Fergus gas terminal. Following publication of this statutory notice we will consult on our minded to position with respect to both these applications.

Our decision-making process

1.4. We published a statutory consultation proposing modifications to NGT's Licence on 25 March 2024. Following publication of this statutory notice to modify SpC 3.14 and 1.1

¹ Valves means the valves and related systems, including actuators, seals and vents, that control and isolate the flow of gas at the St Fergus gas terminal.

² Defined in SpC 1.15 as "means the enclosures, air circulation, exhaust and fire suppression systems necessary for the protection and safe functioning of the compressor fleet."

³ Defined in SpC 1.15 as "means the pipework at compressor stations and above ground installations, coated as a means of primary protection and protected by cathodic protection as a secondary means where it is below ground as well as the equipment associated with maintaining gas quality and pressure."

⁴ [Modification of Special Condition 3.14 Asset Health Re-opener of National Gas Transmission Plc's gas transporter licence | Ofgem](#)

⁵ January 2023 and June 2023

there will be a period of 56 days before the modified conditions become effective on 4 July 2024. We set out below the various stages in the statutory modification process.

Statutory Modification stages

Date	Stage description
25/03/2024	Stage 1: Statutory consultation and notice of proposed licence modification issued
22/04/2024	Stage 2: Consultation closed
08/05/2024	Stage 3: Statutory modification decision issued
04/07/2024	Stage 4: Modification comes into effect

General feedback

1.5. We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this report. We’d also like to get your answers to these questions:

- 1. Do you have any comments about the overall quality of this document?
- 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. Are its conclusions balanced?
- 5. Did it make reasoned recommendations?
- 6. Any further comments

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

2. Proposed modification of Special Condition 3.14 and Special Condition 1.1 – Reasons and Effects

Section summary

This Chapter gives an overview of the Asset health Re-opener mechanism, our reasons for the modification and the effect it will have.

Overview of the Asset health Re-Opener mechanism

2.1. The gas transmission network in Great Britain is owned and operated by NGT. Economic regulation of the network follows the RIIO (Revenue = Incentives + Innovation + Outputs) price control framework. The current RIIO-T2 price control period will last five years from 1 April 2021 to 31 March 2026. Prior to commencement of the price control period, we set out our policy on the economic regulation of the network during the period in the Final Determination (FD).⁶ These policy decisions were given effect by new SpCs in Part C of the Licence, which came into force on 1 April 2021.⁷

2.2. Asset health interventions are interventions on existing assets or groups of assets in response to defects that negatively impact the level of risk associated with the operation of the asset. Such interventions do not result in a material increase in network capacity.

2.3. At our FD⁸, asset health interventions were split into seven broad project themes with allowances granted on the bases of these themes:

- Compressor Cabs
- Plant and Equipment
- Valves

⁶ [RIIO-2 Final Determinations - NGGT Annex \(REVISED\) \(ofgem.gov.uk\)](#)

⁷ The SpCs as made on 3 February 2021 can be found in [Decision on the proposed modifications to the RIIO-2 Transmission, Gas Distribution and Electricity System Operator licences | Ofgem](#) and the current version of the SpCs is [National Gas Transmission Plc - NTS - Consolidated Special Conditions - Current Version.pdf \(ofgem.gov.uk\)](#)

⁸ Table 12 at page 60-61 of [RIIO- 2 Final Determinations NGGT Annex \(Revised\)](#)

- Pipelines
- Compressors
- Electrical
- Civils

2.4. At FD, baseline allowances were provided for each project theme for several projects. However, due to uncertainty with respect to either unit costs and / or the volume of interventions, we decided that an Asset health Re-opener should be established to adjust allowances during the price control period for certain project themes. These were:

- Compressor Cabs
- Plant and Equipment
- Valves⁹

2.5. In our RIIO-T2 FD, we introduced an asset health uncertainty mechanism to adjust NGT's allowances during the price control period. SpC 3.14 Asset health Re-opener of the Licence establishes the mechanism to adjust by direction, where the adjustment to the value of any term relates to asset health interventions on Compressor Cabs or Plant and Equipment, the following Price Control Financial Model¹⁰ terms:

- AHt¹¹ (SpC 3.14 Asset health Re-opener);
- NARMAHot¹² (SpC 3.1 Baseline Network Risk Outputs); and
- NLAHot¹³ (SpC 3.15 Asset health non-lead assets Price Control Deliverable).

⁹ Specifically remediation of defects on actuating gas ring main at St Fergus gas terminal, at paragraphs 3.115, 3.119 and 4.29.

¹⁰ The Price Control Financial Model is the template used to calculate the Allowed Revenue of National Gas Transmission. This template is updated annually in accordance with Special Condition 8.2 Annual Iteration Process for the GT2 Price Control Financial Model

¹¹ Contributes to the calculation of the UMTerm, which is used to calculate the opex escalator term under SpC 3.18. It has the value zero unless directed otherwise in accordance with Special Condition 3.14 (Asset health Re-opener).

¹² Contributes to the calculation of NARM asset health Re-opener term (NARMAHt) under SpC 3.1.5. In accordance with SpC 3.1.5 means the sum of allowances directed by the Authority in accordance with paragraphs 3.14.4(b), 3.14.8(b) and 3.14.9(b) of Special Condition 3.14 (Asset health Re-opener).

¹³ Contributes to the calculation of the asset health – non-lead assets Re-opener term (NLAHt), under SpC 3.15.5. In accordance with SpC 3.15.5, means the sum of allowances directed by the Authority under paragraphs 3.14.4(c), 3.14.8(c) and 3.14.9(c) of Special Condition 3.14 (Asset health Re-opener).

2.6. As such, the current scope of SpC 3.14 does not provide for funding to be granted for Valves.

2.7. One of the projects that we decided not to provide baseline funding for, but which we noted at FD could subsequently be funded through this Asset health Re-opener, was the work required at St Fergus's gas terminal to repair the terminal's actuating gas main ring. NGT have submitted two applications for funding works at St Fergus under SpC 3.14. Some of the funding required is for Valves which is currently outside the scope of SpC 3.14, this brought to our attention the unintended disconnect between the policy decision set out in the FDs and the subsequent licence modifications to give effect to that decision which inadvertently did not include reference to Valves. We are therefore now looking to remedy this and amend SpC 3.14 to bring it in line with our FD.

2.8. Further, at FD we provided baseline funding for those asset health project themes included in SpC 3.14 for only the first three years of the price control period.¹⁴ We decided that those allowances should be subject to an ex-post adjustment mechanism as there was some uncertainty regarding them.¹⁵ We provided a true-up mechanism in SpC 3.14.9 which allows Ofgem to align allowances with efficiently incurred costs and work volumes during this period. However, the current drafting of SpC 3.14.9 only allows us to adjust baseline allowances for the first two years of the price control period.

Proposed modifications reasons and effects

2.9. The reason for the proposed modifications to SpC 3.14 Asset health Re-opener and SpC 1.1 Interpretation and definitions is to align the Licence with the policy intention as stated in FD, so that Ofgem can direct adjustments to NGT's allowances under SpC 3.14 for Valves, Compressor Cabs and Plant and Equipment.

2.10. We proposed to introduce a new defined term "Valves" into SpC 3.14, so that funding for Valves can be allocated alongside funding for Compressor Cabs and Plant and Equipment. We also proposed to extend by one year the period subject to the ex-post true-

¹⁴See paragraph 4.28 of [RIIO-2 Final Determinations - NGGT Annex \(REVISED\) \(ofgem.gov.uk\)](#).

¹⁵See paragraphs 4.28 and 3.117 of [RIIO-2 Final Determinations - NGGT Annex \(REVISED\) \(ofgem.gov.uk\)](#)

up mechanism set out in SpC 3.14.9 to cover the first three years of the RIIO-T2 price control.

Valves

2.11. These modifications are necessary as the current drafting of SpC 3.14 permits Ofgem to direct adjustments to NGT's allowances for asset health interventions relating to the Compressor Cabs and Plant and Equipment project themes only, which cover:

- Compressor Cabs - the enclosures, air circulation, exhaust and fire suppression systems necessary for the protection and safe functioning of the compressor fleet; and
- Plant and Equipment - the pipework at compressor stations and above ground installations, coated as a means of primary protection and protected by cathodic protection as a secondary means where it is below ground as well as the equipment associated with maintaining gas quality and pressure.

2.12. This does not make provision for adjustments to allowances for asset health interventions relating to the Valves project theme, which covers valves and related systems, including actuators, seals and vents, that control and isolate the flow of gas. As explained under Overview of the Asset health Re-Opener mechanism above, Valves were also identified at FD as requiring funding under the Asset health Re-opener mechanism in SpC 3.14 for works required to remediate defects on the actuating gas ring main at St Fergus' gas terminal. This had to be provided for under SpC 3.14 due to the level of uncertainty around both unit cost and volume at FD, which meant it was not possible to set a baseline allowance for the entire price control period.

2.13. This modification will allow Ofgem to allocate funding to NGT for Valves under SpC 3.14, so that the works related to Valves to remediate defects on the actuating gas ring main at St Fergus gas terminal can be funded.

True-up Mechanism

2.14. At FD we provided baseline allowances for the first three years of the price control for Valves, Compressor Cabs and Plant and Equipment. Further, we stated that the Asset

health Re-opener mechanism would allow us to adjust allowances for those first three years based on an ex-post assessment.¹⁶

2.15. The current drafting of SpC 3.14.9 allows us to adjust allowances for actual efficient costs and work volumes for only the first two years of the price control (2021/22 and 22/23). As such, we proposed to modify SpC 3.14.9 so that we can also adjust allowances for the third financial year of the price control (2023/24), to bring the Licence in line with our FD.

2.16. This proposed modification will permit the application of the ex-post true -up mechanism to a greater proportion of baseline allowances reducing risk for both NGT and gas consumers.

¹⁶ See paragraphs 3.117 and 4.28 of [RIIO-2 Final Determinations - NGGT Annex \(REVISED\)](#) ([ofgem.gov.uk](https://www.ofgem.gov.uk))

3. Summary of responses and our view

Section summary

This section contains a summary of the responses we received and our views on the various issues raised.

Responses to specific questions

Question 1: Do respondents agree with our proposed modifications to Special Conditions 1.1 and 3.14 of NGT’s gas transporter license?

3.1. The single respondent (NGT) agreed with our proposal to modify both SpC 1.1 and SpC 3.14 to align the scope of the Asset health Re-opener mechanism with our policy decisions as set out in FD. In particular:

- To extend the scope of the Asset health Re-opener mechanism to include asset health innovations under the Valves project theme, in addition to Compressor Cabs and Plant And Equipment.
- To extend the scope of the Asset health Re-opener true-up mechanism by one year to include the first three years of the price control period from 1 April 2021 to 31 March 2024.

Our View

3.2. We welcome this support for our modifications.

Question 2: Do respondents propose any changes to the proposed licence modification?

3.1. The single respondent (NGT) raised three issues with respect to the detailed drafting of the modification.

- The proposed definition of Valves in SpC 1.1 is limited to those at St Fergus gas terminal. This would seem to be more restrictive than the definition of Compressor Cabs and Plant And Equipment which is not geographically restricted.
- The extension of the ex-post true-up mechanism to the first three years of the price control would seem to imply that there should be a reciprocal reduction in the period covered by the ex-ante mechanism within the Asset health Re-opener, from the final three to the final two years of the price control.
- The direction issued by Ofgem on 1 August 2022¹⁷ creating two additional Re-opener windows (June 2023 and January 2024) has not been reflected in SpC 3.14.5.

Our View

3.3. For the reasons set out below we have decided not to amend the proposed modifications set out in the statutory consultation.

- The definition of Valves reflects our policy decision as set out in FD. In Chapter 4 of FD we described the purpose of the Asset health Re-opener as being, to adjust NGT revenues associated with above ground Plant & Equipment and Compressor Cab infrastructure assets and the remediation of defects on the actuating gas ring main at St Fergus. Further, at paragraphs 3.115, 3.119 and 4.29, we also noted that the Valves intervention under SpC 3.14 was intended to be for St Fergus actuating gas ring main. As such, it is appropriate for us to depart from the approach to Plant And Equipment and Compressor Cabs and restrict funding for Valves under the Re-opener mechanism to St Fergus.
- The extension of the ex-post true-up mechanism does not require a reciprocal reduction in the period covered by the ex-ante mechanism. These are separate mechanisms such that a change in one does not require a change in the other. The original Re-opener window was set for January 2023 at the end of the second year of the price control, this was so that allowances could be provided for asset health interventions in the final three years of the price control.
- The direction issued by Ofgem on 1 August 2022 did not modify the Licence. Although it is possible for Ofgem to modify the Licence as prescribed in the licence conditions (a process known as self-modification and provided for under s. 7B(7) of

¹⁷ [Direction under SpC 3.14.5 \(1 August 2022\)](#)

the Gas Act 1986), SpC 3.14.5 only provides for Ofgem to direct that NGT may submit an application under 3.14.4 at a date later than 25 January 2023 to 31 January 2023.

4. Conclusion

Our decision

4.1. In reaching our decision, we have considered the responses received following publication on 25 March 2024 of the statutory consultation setting out the reasons and effects of the proposed modification.

4.2. We have decided to issue on 8 May 2024 the statutory notice modifying SpC 3.14 Asset health Re-opener (AH_t) and SpC 1.1 Interpretation and definitions of the Licence granted to NGT. This modification will take effect on 4 July 2024, 56 days after the Statutory Notice has been issued.

4.3. The modifications to SpC 1.1 are found in Appendix 1 to this document, and the modifications to SpC 3.14 are in Appendix 2. Additions are marked in double underlined text and deletions in strikethrough.

Appendix 1 – Modifications to Special Condition 1.1
Interpretation and definitions

Insert into the table at paragraph 1.1.15 the following definition, between the definitions of “User” and “Valve Operations”:

<u>Valves</u>	<u>means the valves and related systems, including actuators, seals and vents, that control and isolate the flow of gas at the St Fergus gas terminal.</u>
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Appendix 2 – Modifications to Special Condition 3.14 Asset health Re-opener AHt

Special Condition 3.14 Asset health Re-opener (AHt)

Introduction

- 3.14.1 The purpose of this condition is to calculate the term AH_t (the asset health term). This contributes to the calculation of the Totex Allowance.
- 3.14.2 The effect of this condition is to:
- (a) establish a Re-opener triggered by either the licensee or the Authority to adjust allowances for Valves, Compressor Cabs and Plant And Equipment for Regulatory Years commencing on 1 April 2023 to 1 April 2025; and
 - (b) provide for the true up of costs incurred in Regulatory Years starting on 1 April 2021, 1 April 2022 and 1 April 2023.
- 3.14.3 This condition also explains the process the Authority will follow when directing any changes as a result of the Re-opener.

Part A: What is the scope of this Re-opener?

- 3.14.4 The licensee may apply to the Authority for a direction:
- (a) adjusting the value of the AH_t term;
 - (b) adjusting the value of the $NARMAHO_t$ term; or
 - (c) amending the outputs, delivery dates and allowances in the Asset Health Non-Lead Assets PCD Tables
- where it is seeking allowances for work relating to Valves, Compressor Cabs or Plant And Equipment in Regulatory Years commencing on 1 April 2023 to 1 April 2025.

Part B: When to make an application

- 3.14.5 The licensee may only apply to the Authority for an adjustment under paragraph 3.14.4 Between 25 January 2023 and 31 January 2023, or during such later periods as the Authority may direct.

Part C: How to make an application

- 3.14.6 An application under paragraph 3.14.4 must be made in writing to the Authority and include:
- (a) the changes the licensee is requesting to:

- i. the value of the AH_t term and the Regulatory Years to which that adjustment relates;
 - ii. the value of the $NARMAHO_t$ term and the Regulatory Years to which that adjustment relates; and
 - iii. the Asset Health Non-Lead Assets PCD Tables;
- (b) the basis of the calculation for the proposed adjustments to any allowances; and
- (c) such detailed supporting evidence, including justification of unit costs and volumes of work based on historical outturn data, benchmarking, actual condition information, cost benefit analysis, and updated engineering justification papers, as is reasonable in the circumstances.

3.14.7 An application under paragraph 3.14.4 must:

- (a) relate to changes to the licensee's investment plan that have developed since the licensee submitted its GT Asset Health Plan to the Authority in December 2019;
- (b) relate to costs incurred or expected to be incurred that exceed the Materiality Threshold; and
- (c) be confined to costs incurred or expected to be incurred on or after 1 April 2021.

Part D: Authority triggered Re-opener

3.14.8 The Authority will also consider directing:

- (a) an adjustment to the value of the AH_t term;
- (b) an adjustment to the value of the $NARMAHO_t$ term; and
- (c) an amendment to the outputs, delivery dates and allowances in the Asset Health Non-Lead Assets PCD Tables

without an application being made under paragraph 3.14.4, in relation to costs incurred or expected to be incurred relating to Valves, Compressor Cabs or Plant And Equipment Between 1 April 2023 and 31 March 2026 that exceed the Materiality Threshold.

Part E: Assessment of Years ~~1 and 2~~, 2 and 3

3.14.9 After the Regulatory Year starting on 1 April 2022~~3~~, the Authority will assess costs relating to Valves, Compressor Cabs and Plant And Equipment for Regulatory Years commencing on 1 April 2021, 1 April 2022 and 1 April 2022~~3~~ and direct:

- (a) an adjustment to the value of the AH_t term;
- (b) an adjustment to the value of the $NARMAHO_t$ term; and
- (c) an amendment to the outputs, delivery dates and allowances in the Asset Health Non-Lead Assets PCD Tables

to reflect actual efficient costs and work volumes.

Part F: What process will the Authority follow in making a direction?

3.14.10 Before making a direction under paragraph 3.14.4, 3.14.8 or 3.14.9 the Authority will publish on the Authority's Website:

- (a) the text of the proposed direction;
- (b) the reasons for the proposed direction; and
- (c) a period during which representations may be made on the proposed direction, which will not be less than 28 days.

3.14.11 A direction under paragraph 3.14.4, 3.14.8 and 3.14.9:

- (a) will set out any adjustments to the value of the AH_t term and the Regulatory Years to which that adjustment relates;
- (b) will set out any adjustments to the value of the $NARMAHO_t$ term and the Regulatory Years to which that adjustment relates; and
- (c) where any amendments are being made to the outputs, delivery dates or allowances in the Asset Health Non-Lead Assets PCD Tables, will replace the text in Appendix 2 to Special Condition 3.15 (Asset health – non-lead assets Price Control Deliverable).