Making a positive difference
**for energy consumers**

# RIIO-2 Gas Distribution Annual Report: 2023/24

## Executive Summary

The energy system's path to achieve the government's Clean Energy Superpower mission, including Clean Power by 2030 and accelerating to net zero by 2050, presents both significant challenges and opportunities for the sector.

While there will be a clear shift away from gas in any net zero pathway, over the short to medium term gas networks will still play a significant role in providing energy and must continue to do so safely and reliably.

To balance these complex short and long term needs, the current round of price controls (RIIO-2[1]) established a comprehensive investment and incentive package. We[2] designed the package to enable network companies to deliver a lowest cost, decarbonised energy system, while maintaining world-class levels of system reliability and customer service.

The scale of consumers' investments is substantial. Collectively, the gas distribution businesses expect that funding over the five-year price control period will reach £10.4 billion.

The RIIO-2 framework, being outcome-focused, is designed to assist companies in clearly coordinating the system consumers need in advance, minimising investor uncertainty, and ensuring that new infrastructure is built quickly and at a reasonable cost.

### Price Control Monitoring

As the sector progresses through the RIIO-2 period[3], it is crucial that we continuously monitor that companies are advancing as expected in delivering their agreed investment plans and outputs. Consumers have funded the network investments, and it is essential that these networks continue to provide reliable service and meet the diverse needs of network users.

It is encouraging to report that over the past three years, all GDNs have consistently surpassed their minimum targets for the complaints metric and consumer satisfaction survey. This gives us confidence that, overall, consumers are having a positive experience when interacting with their GDN. Additionally, we are seeing strong performance in emergency response, with most GDNs exceeding their targets.

[1] This is the second gas distribution price control using the Revenue = Incentives + Innovation + Outputs (RIIO) model.
[2] The terms 'we', 'us', 'our' refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.
[3] New price controls for gas and electricity transmission and gas distribution will be implemented from April 2026.

This report provides a comprehensive overview of how companies are delivering against the outcomes and metrics set for RIIO-2. It presents our key findings on the incentive delivery and performance of the four GB gas distribution network (GDN) businesses, with a particular focus on the position after the third reporting year. Additionally, the report provides an overview of the GDNs' current total cost (totex) expectations[4] across the five-year RIIO-2 price control period.

Looking ahead, we will use performance data to collaborate closely with stakeholders, learn lessons from RIIO-2, and develop the next set of network price controls.

**Key Messages**

**Output Delivery Incentives:** GDNs are generally performing well against their annual incentive targets. However, SGN did not meet unplanned interruption targets in its Southern region, while Cadent East of England (EoE) and West Midlands (WM) missed their period wide ODI targets in the third regulatory year. Consequently, both GDNs incurred financial penalties. All GDNs performed strongly against the Complaints Metric ODI, and outperformed target in each of the three years to date.

**Innovation:** Progress in innovation projects is accelerating. All GDNs have successfully secured funding through Ofgem's innovation mechanisms, supporting a number of initiatives. We are continuing to consider improvements to how networks report on their innovation work.

**Volume Drivers/PCDs:** The volume driver mechanisms are functioning as intended to ensure that consumers are only paying for the actual volume of activity. All GDNs are delivering lower volumes than forecast against their Domestic Connections Volume Driver. Mixed levels of delivery are being observed in Tier 2A, with some GDNs forecast to meet volumes as set out in the Final Determinations, and some lower than anticipated.

Good progress continues to be made in advancing a number of the Price Control Deliverables (PCDs). For example, almost all GDNs are forecasted to meet their Repex Tier 1 Mains PCD and all GDNs are performing well against Capital Projects PCD. However, SGN Southern is struggling to deliver against Tier 1 Mains targets.

**RIIO-2 Expenditure**: During the RIIO-2 period to date (2021-2024), three GDNs are operating below their allowances[5], while one is exceeding its allowance. All GDNs are expected to increase spending in the final two years of RIIO-2, with three projecting overspend and one underspending across the five-year period.

[4] Three-year actual costs incurred and a forecast of the costs to be incurred over the remaining two years of the RIIO-2 period.

[5] Allowances include adjustments for Reopeners, Price Control Deliverables (PCDs), Volume Drivers and Real Price Effects (RPEs)

## Structure of this report

- **Chapter One** provides summary information on the gas distribution network (GDN) businesses and the annual reporting process.

- **Chapter Two** explains how the GDNs have performed against their output commitments over the first three years of the RIIO-2 period. It also indicates the incentive payments earned.

- **Chapter Three** provides an overview of GDNs' actual and forecast activity related to two key volume drivers and one PCD mechanism across the RIIO-2 period.

- **Chapter Four** presents our summary of each company's five-year total cost performance against the price control obligations and incentives, using data and supporting information provided by each GDN.

All financial values in the report are in 2018-19 price base unless stated otherwise.

Information on our current assessment of the Return on Regulated Equity[6] was separately published in February 2025.[7]

Two subsidiary documents have been published along with this report.

- a document presenting further detail of the areas of GDNs' performance discussed in this report, and

- a supplementary datafile containing additional performance data.[8]

[6] The financial return achieved by shareholders in a licensee during a price control period from its outturn performance.
[7] This report does not provide any information on the Network Asset Risk Methodology outputs which is provided through a separate regulatory submission. This report is also separate to the 14 February 2025 publication which provides a view of regulatory financial performance (RFP): https://www.ofgem.gov.uk/publications/riio-2-regulatory-performance-data-2024.
[8] Please note that this report does not provide any information on the Network Asset Risk Methodology outputs which is provided through a separate regulatory submission.

# Chapter One: Introduction

GDNs are responsible for operating, maintaining the health, and the safety of the network whilst ensuring fair and competitive connections.

To ensure value for money for consumers, we regulate the GDNs through periodic price controls that limit the amount by which costs can rise, and that stipulate levels of performance.

There are mechanisms to adjust revenues year-on-year depending on GDNs' performance against pre-set targets. There are outputs associated with baseline revenues that GDNs must deliver either on an annual or on a five-year basis.

The four providers of gas distribution services are:

- Cadent which operates across four regions (East of England, London, North-West and the West Midlands).
- Northern Gas Networks (NGN) which operates in one region
- SGN which manages the network in Scotland and the South of England; and
- WWU which operates in one region comprising of Wales and the South West of England.

## RIIO-GD2

To establish our price controls, we use the RIIO (Revenue = Incentives + Innovation + Outputs) framework. The current Gas Distribution price control spans a five-year period from 1 April 2021 to 31 March 2026.

## Annual Reporting

GDNs are required to report on their performance in relation to their cost allowances and the outputs established under the RIIO-2 price control framework.[9] This includes an assessment of compliance with achieving minimum standards of performance, evaluation of progress towards pre-agreed targets, and indication of whether activities are on-track and on-time to achieve the anticipated delivery program across RIIO-2.

We analyse this information and examine any variations in GDNs' performance against their annual and five-year output targets, as well as the expected under and over-spend across specific activities and cost categories.  Additionally, we engage with each GDN to discuss the technical and financial aspects of their submissions. This process helps us gain a deeper understanding of the factors influencing the delivery of the RIIO-2 settlement and their perspectives on future performance.

[9] The Regulatory Instructions and Guidance (RIGs) requires Gas Distribution network owners to provide information to the Authority. The Authority used the information provided in the RIGs in preparation of this Annual Report.

# Chapter Two: Incentives

In this chapter, we examine outputs that are subject to incentives, including the value of rewards and penalties where applicable. It also provides a summary of performance against Output Delivery Incentives (ODIs), one of the GDNs Licence Obligations (LOs) and a Use-it-or-Lose-it (UIOLI) mechanism.

## Our assessment of GDN output delivery incentive (ODI) performance

As part of the RIIO-2 Price Control we implemented a number of ODIs for the network companies. Table 1 provides an overview of performance across all incentive areas in 2023/24

**Table 1**: Measure of performance (2023/24)

Green means 'Met': performance on target / ahead of target or above score.
Orange means 'Near': partially missing target / partially behind target or below score.
Red means 'Not met': performance substantially missing target / substantially behind target or below score.

| ODI | RIIO measure | Cadent | NGN | SGN | WWU |
|---|---|---|---|---|---|
| Customer Satisfaction Survey ODI | A measure of customer service performance covering; Connections, Planned and Unplanned work. | Met | Met | Met | Met |
| Complaints metric ODI | A measure of performance in the handling of complaints | Met | Met | Met | Met |
| Unplanned Interruption Mean Duration ODI | Measures the performance on the duration of unplanned interruptions | Met | Met | Not met | Met |
| Unplanned Interruption Mean Duration ODI [Cadent only] | Measures the performance on the duration of unplanned interruptions | Met | n/a | n/a | n/a |
| Shrinkage Management ODI | Reduction of shrinkage of gas from GDNs' pipe network | Near | Met | Met | Met |

Three years into the period, we observe that while the GDNs are rising to the challenge across the majority of incentive areas, there are incentive areas proving more problematic for some GDN's.

WWU and NGN have met or exceeded the annual targets set for all applicable ODI categories. Cadent is currently meeting or exceeding expected targets across the majority of its ODIs, but is currently falling short of expectations against its shrinkage management target. SGN is meeting or exceeding the annual targets set against all applicable ODI categories apart from its unplanned interruptions target for SGN Southern.

GDNs can be financially rewarded for good performance or penalised where they miss targets. Table 2 summarises the cumulative revenue rewards and penalties accrued by each GDN over the first three reporting years for each incentive area. In total, GDNs have received £36.29m in net rewards for their ODI performance.

**Table 2**: ODI-F indicative cumulative revenue rewards & penalties (£m, 2022-2024)

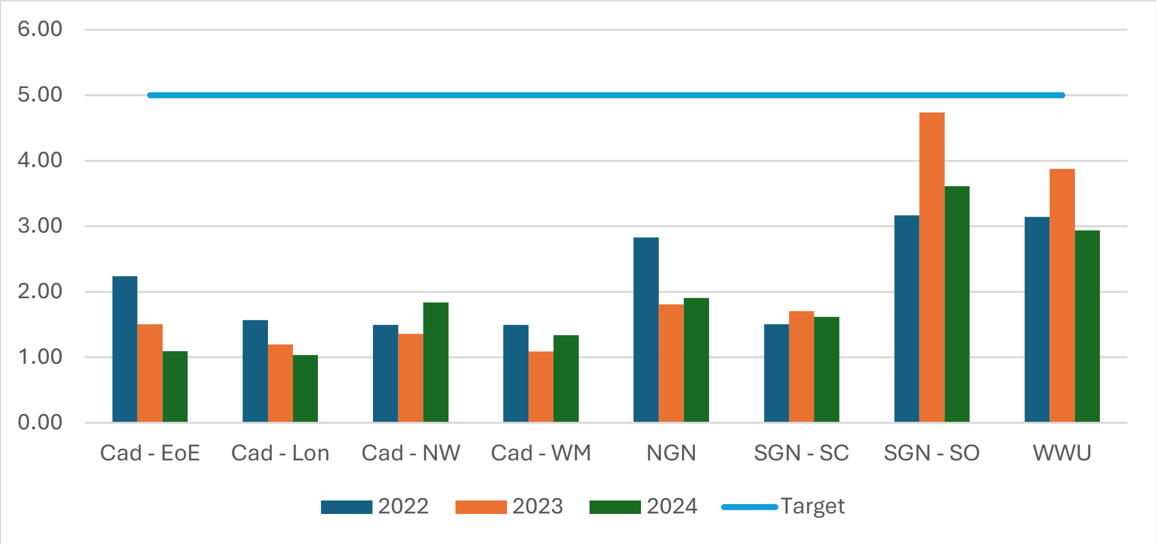
| ODI | Cadent | NGN | SGN | WWU | TOTAL |
|---|---|---|---|---|---|
| Customer Satisfaction Survey | £13.95 | £4.57 | £7.59 | £3.26 | **£29.37** |
| Complaints metric (penalty only) | £0 | £0 | £0 | £0 | £0 |
| Unplanned Interruption | n/a | £0 | -£3.06 | £0 | **-£3.06** |
| Unplanned Interruption [Cadent only] | £0 | n/a | n/a | n/a | **£0** |
| Shrinkage Management | £1.81 | £0.43 | £1.21 | £1.13 | **£4.58** |
| Collaborative streetworks[10] [Cadent Lon & EoE, SGN So only] | £3.2 | N/A | £3.66 | N/A | **£6.86** |
| **TOTAL (£m)** | **£18.95** | **£4.99** | **£9.41** | **£4.38** | **£36.29** |

## Complaints Metric

RIIO-2 supports the delivery of a high-quality complaints handling to all network users and consumers. It encourages GDNs to efficiently improve complaint handling by penalising them for achieving results below a minimum performance threshold.

[10] Collaborative streetworks – a bespoke ODI - is included within this table for completeness. It is not discussed further within this document as the focus is on performance across ODIs common across all GDNs and where a comparison can be drawn.

**Figure A1.4: Complaints Metric – performance against target (2023/24)**




**Our view:** Three years into the period, all GDNs are reporting strong levels of performance and surpassing their annual targets in handling complaints. Levels of customer service are being maintained, demonstrating that GDNs are effectively responding to the incentive design and continuing to prioritise the critical importance that consumers place on customer service.

## Customer Satisfaction Survey

The purpose of this incentive is to maintain good customer service. GDNs that deliver exceptional performance can be rewarded whilst any substandard provision will be penalised.

The incentive takes into account three elements, each with their own target scores:

- Connections: This relates to any request for, and the delivery of, any work to provide or modify a connection to the gas network.

- Planned work: Planned work is an interruption that occurs as a result of planned non-contractual work, other than those interruptions occurring as an inadvertent consequence of such work.

- Unplanned work: Unplanned work is a non-contractual interruption resulting from unplanned activities, or as an inadvertent consequence of planned work.

Across the third regulatory year (2023/24), all the GDNs achieved good performance and have been rewarded under the mechanism accordingly.

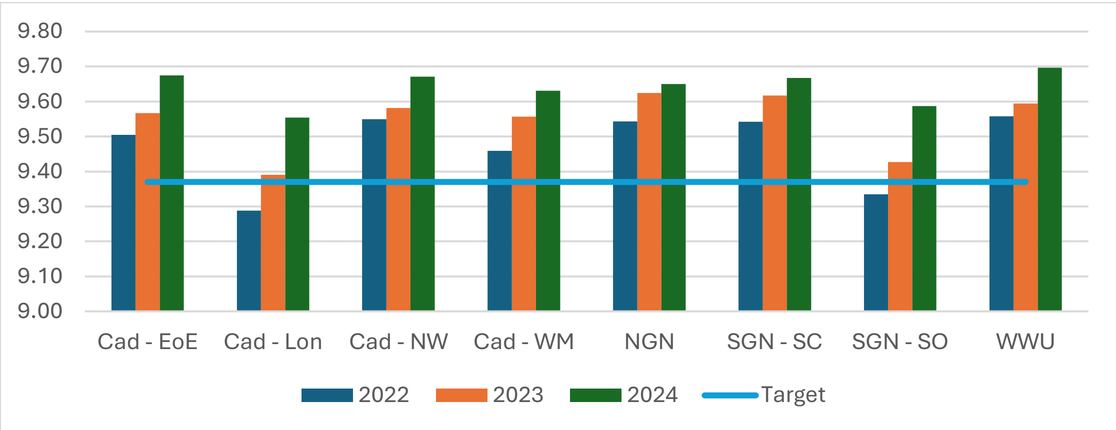
**Table 3:** Customer satisfaction Survey annual reward (23/24)

| ODI | Cadent | NGN | SGN | WWU | TOTAL |
|---|---|---|---|---|---|
| Customer Satisfaction Survey | £13.95 | £4.57 | £7.59 | £3.26 | £29.37 |

All GDNs have exceeded their target scores for customer satisfaction on planned works. However, performance for some licensees has been decreasing through the price control period. While scores remain above the target across all GDNs, and no penalties were applied, we will closely monitor this trend to address any further reductions in satisfaction scores observed.

Above target performance is also evident from all GDNs on customer satisfaction with respect to unplanned interruptions. We are encouraged that there are year-on-year improvements by all licensees to date. As a result no penalties were applied and those with stronger scores received a reward.

**Figure A1.3: Customer Satisfaction – Unplanned interruption performance against target (2023/24)**




**Our view:** A trend of improving scores has been observed across all GDNs throughout the price control period to date. The progress in this area since the start of RIIO-2 underscores the investment and focus companies have dedicated to this crucial area. This demonstrates that both our incentive mechanisms and the strategies of the licensees have been successful to date in improving customer satisfaction.

## Unplanned Interruptions ODI

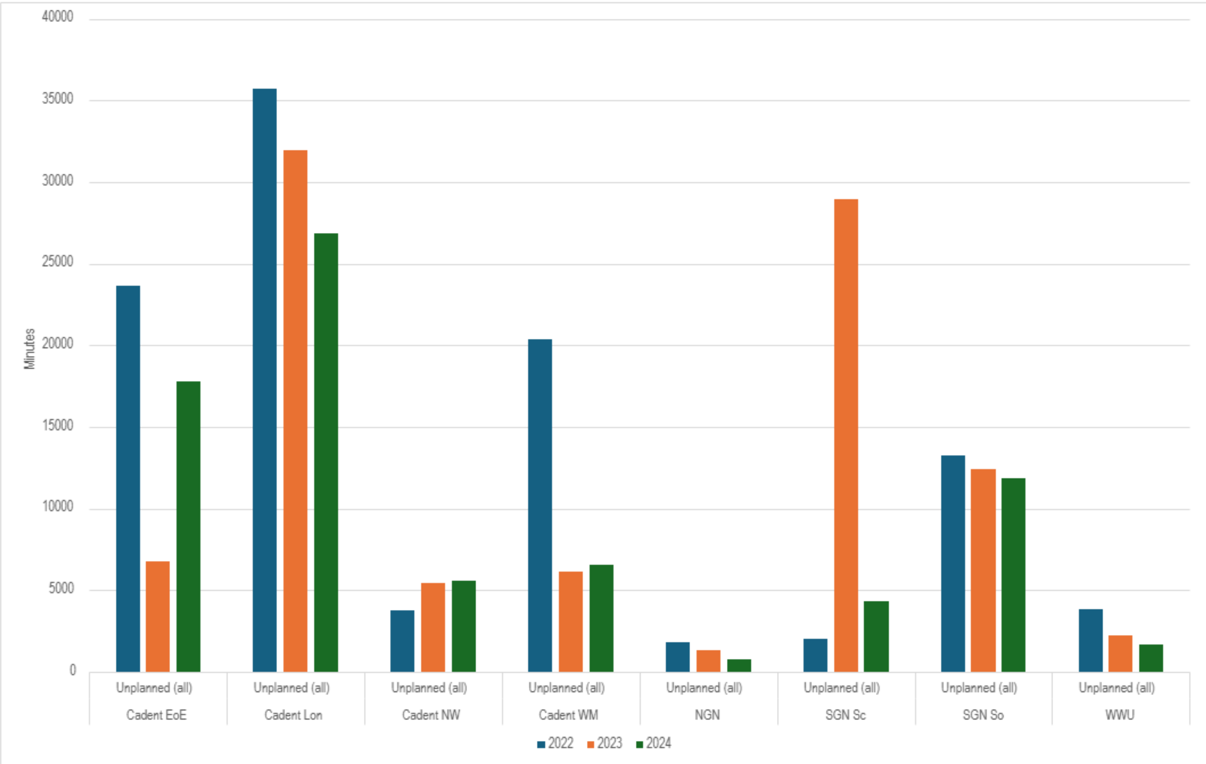
The purpose of the unplanned interruptions incentive is to ensure that GDNs manage the duration of these interruptions effectively and prevent performance deterioration. An unplanned interruption occurs when no prior notification is given to the customer.

For NGN, WWU and SGN performance is measured equally across all buildings connected to their network.

Cadent's incentive design differs from the other GDNs by incorporating two distinct measures for unplanned interruptions. The first measure focuses on Multiple Occupancy Buildings (MOBs), where a riser must be replaced or repaired before supply can be restored, due to the high number of MOBs (e.g. tower blocks) in Cadent's network. The second measure covers all other buildings (non-MOBs), offering a more accurate and detailed assessment of Cadent's performance.

Cadent, NGN, WWU and SGN Scotland all outperformed their targets in this output with improvements seen since RIIO-1 in their performances. However, SGN Southern exceeded their maximum penalty threshold with an average of 34.4 hours compared to a threshold of 33.5 hours, resulting in a £3.06m penalty. SGN explain that this was due to an interruption affecting a MOB and additional complexity in restoring supplies in such buildings. Additionally, SGN reports that a significant increase in repair workload in 2023/24 led to emergency gas escape work taking priority, causing reconnections to take longer than usual.

**Figure A1.4: Unplanned interruption, average interruption duration by GDN (2023/24)**




**Our View:** Though we have seen a decrease in the average time customers are off supply due to unplanned interruptions since the start of RIIO-GD2, there is still work to be done, especially in restoring supplies to MOBs.

## Other mechanisms

In addition to ODIs, the RIIO-2 framework includes other mechanisms to encourage desired behaviours, detailed below.

The **Emergency Response Licence Obligation** ensures GDNs respond to 97% of reported gas escapes within one hour for uncontrolled escapes and within two hours for controlled escapes.

All GDNs achieved their licence obligation to attend 97% of reported escapes within one hour for uncontrolled escapes and two hours for controlled escapes across the entirety of 2023-2024. We remain concerned, however, that some licensees did not achieve this performance consistently throughout the year with some failing to respond within an hour during the winter months. Ofgem continues to investigate these matters to ensure a consistent level of performance is provided to consumers.

The **Vulnerability and Carbon Monoxide Allowance** is a UIOLI for GDNs to fund activities addressing consumer vulnerability and Carbon Monoxide (CO) safety. The mechanism allows GDNs to provide bespoke services to support consumers in vulnerable situations and raise awareness of CO.

GDNs continue to deliver strong performance with their VCMA. We observe a number of collaborative projects being undertaken above the required percentage and a mixture of projects supporting consumers across the entire focus of this UIOLI allowance.

GDNs have targets in place to reduce their **Business Carbon Footprint** throughout the RIIO-GD2 period. This aims to ensure that GDNs take responsibility for their environmental impacts, excluding shrinkage.

At the time of our RIIO-2 FDs we did not have robust enough data to set target baselines for the GDNs regarding BCF reductions. The current differences between GDNs make direct comparisons challenging. Overall, we have observed mixed performance regarding BCF with some of this arising from complications regarding reporting requirements. We will continue to monitor this area and develop more robust procedures for future regulatory years.

Regarding **shrinkage management**, both WWU and SGN have consistently achieved rewards throughout RIIO-2 for their good performance in this area. NGN and Cadent have seen mixed results. NGN was initially penalised in the first year of RIIO-2 but has since stabilised its performance. Cadent whilst seeing overall shrinkage levels decreasing has seen mixed performance among individual licensees. Cadent London, previously penalised, achieved a reward this year. However, Cadent West Midlands and Cadent East of England received penalties for the first time in 2023/24.

# Chapter Three: Volume Drivers and Price Control Deliverables (PCDs)

In this chapter, we provide an overview of GDNs' actual and forecast activity related to two key volume drivers and one PCD mechanism across the RIIO-2 period. Volume driver mechanisms adjust a GDN's cost allowance to ensure that consumers only pay for the actual volume of activity that is delivered.[11]

## Domestic Connections volume driver

The Domestic Connections volume driver funds domestic service connections.

In each of the three years of the price control, all GDNs have delivered lower domestic connection volumes than the maximum allowed volumes set out in the licence. GDNs currently forecast that this will continue across the price control as a whole.

Demand for connections has decreased due to a decline in gas boiler demand, influenced by legislation phasing out their installation, rising energy costs, and growing climate change awareness prompting consumers to seek sustainable options.

Consequently, all GDNs forecast that domestic connections will remain well below the maximum allowed volumes over the five-year period. This position is summarised in Table four per GDN group and in Table 5 for each region.

**Table 4**: Domestic Connection Volume delivery as a % of allowed: GDN group

| | 3-Year Actual Position against the 3 year forecast | 5-Year Actual/Forecast Position against the 5 year forecast |
|---|---|---|
| **Cadent** | 62% | 54% |
| **NGN** | 54% | 54% |
| **SGN** | 48% | 44% |
| **WWU** | 60% | 51% |

**Table 5**: Domestic Connection Volume delivery as a % of allowed: Region

| | 3-Year Actual Position against the 3 year forecast | 5-Year Actual/Forecast Position against the 5 year forecast |
|---|---|---|
| **EoE** | 60% | 51% |
| **Lon** | 66% | 58% |
| **NW** | 65% | 59% |
| **WM** | 63% | 55% |
| **NGN** | 54% | 54% |
| **Sco** | 46% | 39% |
| **Sou** | 50% | 46% |
| **WWU** | 60% | 51% |

[11] A summary of the RIIO-2 volume driver mechanisms can be found in chapter three of: RIIO-2 Final Determinations – GD Sector Annex (REVISED)

The decline in demand is mirrored by a corresponding decline in allowances.

- Cadent: Allowances are expected to flex downward across the period from £116.5m to £68.8m.

- NGN: The current expectation is for NGN's five year allowance to reduce from £20.2m to £13.1m.

- SGN: The anticipated five year allowance of £61m is currently expected to be adjusted down to £25.6m.

- WWU: Allowances are expected to be revised downward across the five year period from £46.9m to £24.2m.

**Our View:** The connection landscape is evolving, with the demand for connections being substantially lower than initially assumed when the RIIO-2 settlement was being set. Consequently, over the five-year period, all GDNs currently expect a substantially lower trajectory of volumes to be delivered under the mechanism.

Overall, we currently hold the view that the observed movement in the delivery expectations throughout the price control period, and the resultant adjustments to allowance across the period, confirm that the volume driver mechanism is functioning as intended.

## Tier 2A mains replacement volume driver

The Tier 2a mains[12] replacement volume driver funds mains replacement for mandatory Tier 2A iron mains and associated services.

As of year 3, the anticipated volumes for Tier 2A Mains replacement have been below those set out in the Final Determinations. The cumulative position across the first three reporting years is summarised in Table 6 per GDN group. Table 7 demonstrates the current expectations for each GDN group across the five-year price control period.

**Table 6**: Tier 2A Mains Decommissioned, 2022-24

| | Actual (Km) | % of Forecast |
|---|---|---|
| Cadent | 6.3 | 27% |
| NGN | 5.6 | 56% |
| SGN | 0.0[13] | 0% |
| WWU | 2.8 | 85% |

[12] Tier 2A mains refers to a category of gas mains that require replacement due to their risk profile. These mains are identified based on factors such as age, material, and condition, which indicate a higher likelihood of failure or safety concerns.
[13] SGN have delivered no volumes of Tier 2A Mains to date. Please refer to the subsidiary document for more details.

**Table 7**: Tier 2A Mains Decommissioned, 2022-26

| | Actual (Km) | % of Forecast |
|---|---|---|
| Cadent | 27.7 | 118% |
| NGN | 8.2 | 81% |
| SGN | 3.2 | 40% |
| WWU | 2.8 | 85% |

**Our view:** It is important to acknowledge the challenges associated with accurately forecasting assets for replacement, which have led to significant variations in delivery compared to the levels anticipated in the final determination. These challenges underscore why we implemented a volume driver for Tier 2 Mains under the RIIO-2 price control. This mechanism ensures that consumers only pay for the actual volume of activity required, aligning costs with real-world needs and promoting efficiency.

Overall, the delivery expectations throughout the price control period confirm that the volume driver mechanism is functioning as intended.

## Delivery performance under the applicable PCDs

RIIO-2 includes Price Control Deliverables, where funding is linked to the delivery of outputs specified in the licence. This framework means the level and timing of allowances can be adjusted in the event the output is not delivered, not delivered to the specification required, or delivered late.

The iron mains replacement (Repex) programme is a long-term initiative focused on replacing old and deteriorating metal mains and services with plastic pipes. This effort is primarily executed through the Iron Mains Risk Reduction Programme (IMRRP), regulated by the Health and Safety Executive (HSE). Within the IMRRP, mains are categorised into different tiers based on diameter and risk measures.

RIIO-GD2 has two PCDs for Tier 1 mains and services[14], which are applicable to all GDNs. These PCDs are designed to fund decommissioning and replacement activities, while ensuring that consumer costs reflect actual delivery, and enabling GDNs to operate efficiently.

[14] Tier 1 mains refer to gas mains that are smaller in diameter (typically less than 8 inches) and are made of iron. These mains are considered higher risk due to their age and material, making them more prone to leaks and failures

Table 8 below shows the actual and forecast variance from the Tier 1 Mains replacement target in each year of the price control, and the projected variance across RIIO-2.

**Table 8:** Tier 1 Volume target variance (%, 2021- 2026)

| | **2022** | **2023** | **2024** | **2025** | **2026** | **Total** |
|---|---|---|---|---|---|---|
| **EOE** | -4.8% | 5.7% | 8.3% | 0.8% | -1.4% | **1.7%** |
| **LON** | -2.5% | -5.6% | -6.1% | 8.8% | 8.1% | **0.5%** |
| **NW** | 10.7% | 7.5% | -0.5% | 1.1% | -1.1% | **3.5%** |
| **WM** | -2.7% | 5.0% | 2.6% | -2.0% | -2.0% | **0.2%** |
| **NGN** | 2.1% | 0.4% | 9.5% | 3.1% | -5.1% | **2.0%** |
| **Sc** | 3.6% | 7.5% | -1.3% | -1.2% | -1.2% | **1.5%** |
| **So** | -2.3% | -15.0% | -21.7% | 0.0% | 2.5% | **-7.3%** |
| **WWU** | -10.0% | -0.3% | 7.5% | 1.4% | 1.5% | **0.0%** |

Performance across the GDNs varies for this PCD. The performance position of each GDN is briefly summarised below.

- Cadent's performance varies across regions. In London, Cadent is currently below the main replacement target but expects to exceed its linear target by 8.8% in year 4 and 8.1% in year 5. The remaining three Cadent regions are surpassing their targets, with forecasts indicating they will exceed price control targets throughout the RIIO-2 period. Ofgem acknowledges the challenges and will continue to monitor progress.

- NGN has consistently exceeded its linear target over the past three years and forecasts a 2% over-delivery for the entire period. This strong performance gives confidence that NGN will meet its target volumes across the full RIIO-2 period.

- SGN's performance differs between its two regions. Scotland has exceeded its three-year target and forecasts a 1.5% over-delivery across RIIO-2. However, the Southern region is significantly below target, with a 21.7% under-delivery in year 3. Challenges in attracting contractors and the complexity of work have increased costs and delayed completion. SGN forecasts a 7.3% under-delivery across RIIO-2 but has a recovery plan to improve performance in the final two years.

- WWU has reported below-target delivery in the first two years but increased volumes in year three, bringing it just below the three-year target. WWU forecasts slightly above-target delivery in the final years, and given the volumes achieved in year 3, this level of delivery is expected to be realised.

**Our View:** Due to initial delays at the start of the price control period and subsequent economic challenges, GDNs are facing significant obstacles in meeting the PCD targets. However, the companies have managed to recover from substantial under-delivery in the first two years by implementing efficiencies, such as bringing works in-house to mitigate contractor issues. Consequently, all regions, except SGN Southern, are currently on a trajectory that expects to meet or exceed the Tier 1 Mains replacement targets by the end of RIIO-2.

We are encouraged that the GDNs appear to be taking proactive measures to address early delays and improve performance. We look forward to seeing this strong commitment continue to ensure the successful completion of the Repex programme.

# Chapter Four: GDNs' cost and allowance performance

## Our assessment of totex performance

Table 9 summarises the GDNs' current view of totex against the adjusted totex allowance position through to the end of RIIO-2.

**Table 9:** GDN's current view of expenditure and adjusted allowance

| £ billion, 2018-19 prices | Cadent | NGN | SGN | WWU | TOTAL |
|---|---|---|---|---|---|
| a. Current forecast of GD2 expenditure (Controllable costs) | 5.42 | 1.20 | 2.96 | 1.36 | **10.94** |
| b. Current forecast of GD2 adjusted allowance | 5.09 | 1.25 | 2.79 | 1.28 | **10.41** |
| Performance (a-b) | **0.33 (6.5%)** | **- 0.05 (-3.8%)** | **0.17 (6.1%)** | **0.08 (6.3%)** | **0.53 (5.1%)** |

During the RIIO-GD2 period, all GDNs currently expect to exceed their five-year allowance except for NGN which expects to underspend. The table above illustrates that the deviations from the allocated budget range from +6.5% to -3.8% over the price control period.

For the three GDNs forecasting overspend, there is no common primary driver

- Cadent anticipates overspending across all three main cost categories (Capex, Opex, and Repex). The primary driver is Capex, forecasted to exceed the allowance by 12% due to material prices, supply chain issues, and work complexity. Opex overspending is attributed to inflationary pressures, increased repair work, and higher business support costs. Repex overspending is driven by a stretching settlement at final determination, exacerbated by inflationary pressures, a competitive labour market, and rising material costs. Additionally, the complexity of London's dense population and underground networks contributes to increased costs and delivery times.

- SGN, while expecting an underspend on Capex due to capital projects ramping up in the later years of RIIO-GD2, forecasts overspending in the other two areas. Opex is the main driver, projected to be 17% above the allowance due to investments in recruiting and retaining staff, as well as increased business support costs. Repex overspending is primarily in the Southern region, driven by difficulties in finding suitable contractors, whereas Scotland is not facing the same pressures, resulting in an underspend in this area.

- NGN is the only GDN that expects to underspend across all three categories. Opex underspending is due to the capitalisation of certain costs and a mild winter, which significantly reduced Publicly Reported Escapes (PREs). Capex underspending is attributed to delays in major projects like the TransPennine Electrification, economic conditions such as long lead times and contractor shortages, and increased resource demand across the utility sector. Repex spending is forecast to be largely in line with the allowance.

- WWU projects an underspend on Opex partly due to efficient staff utilisation and reduced reliance on external contractors. Capex is expected to underspend initially due to delayed projects and early underspending in areas like IT and vehicles but overspend later due to inflation and economic conditions. Repex is driving an 18% overspend, influenced by pandemic recovery, increased unit costs, supply chain issues, and local authority traffic management costs. WWU also cited insufficient Repex allowance, more work than forecasted, and increased labour costs due to staff turnover and contractor challenges.

**Our View:** GDNs have faced many challenges over the first three years to date. The COVID pandemic resulted in delays to carrying out work, and macroeconomic factors like high inflation resulted in an increased costs and resource challenges. However, where GDNs were able to, they have responded well to these challenges.

On delivery, there is a mixed picture across GDNs. The main area of under delivery, against what was agreed at FD, is Repex. Two GDNs are currently below their target for the Tier 1 mains PCD, and all GDNs are delivering lower volumes than set out in the FD against elements of the non-mandatory Repex. We do however note that for the non-mandatory element, GDNs have utilised the NARM risk trading framework, deviating from their original plans, in order to deliver against their Baseline Network Risk Outputs[15].

We will continue to work with the GDNs to monitor their progress in delivering what was agreed at final determination[16].

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15 RIIO-2 Final Determinations NARM Annex (REVISED

16 https://www.ofgem.gov.uk/sites/default/files/docs/2021/02/final_determinations_-_gd_annex_revised.pdf