

Decision

RIIO-2 NZASP Re-opener Final Determinations: NGN Birkshall Rationalisation and Relocation Works Project

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This document sets out our Final Determinations on Northern Gas Network's (NGN's) Birkshall Rationalisation and Relocation Works Project ('the Project') which was submitted under the Net Zero Pre-construction Work and Small Net Zero Projects (NZASP) re-opener mechanism (Special Condition (SpC) 3.9 of NGN's Gas Transporter Licence). This application was submitted by NGN on 16 August 2024. Our Final Determination is to reject NGN's NZASP application and to not award any additional allowances for the Project.

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Introduction

- 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 do not overpay for those investments.
- 1.2 The current price control model is known as RIIO (Revenue = Incentives + Innovation + Outputs). RIIO-2 is the second price control under the RIIO model for electricity transmission, gas transmission and gas distribution, and runs from 1 April 2021 until 31 March 2026. It includes a range of Uncertainty Mechanisms (UMs) that allow us to assess applications for additional funding during RIIO-2 as the need, cost or timing of proposed projects becomes clearer. This ensures that consumers fund projects only when there is clear evidence of benefit, and we have clarity on likely costs and cost efficiency. These mechanisms also ensure that the RIIO-2 price control has flexibility to adapt as the pathways to Net Zero become clearer.
- 1.3 Where possible, we have set automatic UMs, such as the Generation and Demand Connection Volume Drivers, which provide Electricity Transmission Owners with immediate funding when they are required to undertake new customer connection works. In other areas, where the degree of uncertainty is too great to allow for an automatic mechanism, we set 're-openers' which will allow us to assess proposals robustly once information with sufficient accuracy is made available.

What did we consult on?

- 1.4 NGN applied to Ofgem for additional RIIO-2 allowances under the NZASP re-opener mechanism (SpC 3.9).
- 1.5 Following submission, NGN also provided additional information to us through Supplementary Question (SQ) responses.

- 1.6 We considered the proposal and relevant justification for the funding requested in accordance with our principal objective and statutory duties. In line with the [Re-opener Guidance and Application Requirement Document](#), our assessment covered the following three areas:
- The needs case,
 - The options assessment and justification for the proposed project,
 - The efficient costs for the proposed project.
- 1.7 We combined this information to create our Draft Determinations on what additional allowances should be provided to undertake the project.
- 1.8 We issued a consultation on our Draft Determinations, between 27 January 2025 and 24 February 2025, and included a draft of the direction that would be used to implement the Draft Determination.
- 1.9 We received two responses to the consultation, one from NGN and one from another gas network that has asked to be anonymised. We have published NGN's response and a redacted version of the other gas network's response on our website alongside this document.

Purpose of this document

- 1.10 This document summarises the consultation responses received from stakeholders, and an explanation of the changes made to our Draft Determination position since the consultation. It also sets out our Final Determinations.

Related Publications

- 1.11 This document is intended to be read alongside:
- [Re-opener Guidance](#),
 - [Licence Special Conditions](#) – licenses available on the Electronic Public Register,
 - [NGN's re-opener application](#) on NGN's website,
 - [Our Draft Determinations](#).

Summary of our Final Determinations

- 1.1 We have decided to not accept NGN's NZASP application and we will not be providing any allowances for this project. **Table 1** below summarises our Draft and Final Determinations for NGN's NZASP application. Chapter 2 discusses these in greater detail.

Table 1: Summary of our Draft (DD) and Final Determinations (FD) for NGN's NZASP application (£m, 2018/19 prices)

	NGN submitted costs	Ofgem's DD allowances	Ofgem's adjustment DD to FD	Ofgem's FD allowances
Total	4.72	3.61*	-3.61	0.00

*During the consultation period, an error in our draft allowance calculation was highlighted by NGN. The correct draft allowance should have been £3.65m.

Table 1 reflects the draft allowances we consulted on.

2.Summary of our Draft Determinations, consultation responses and our Final Determinations

Needs case and optioneering assessment

Summary of our Draft Determinations

- 2.1 In our Draft Determinations, we considered that the Project was within scope of the NZASP re-opener mechanism in accordance with SpC 3.9 of NGN's Gas Transporter licence.
- 2.2 We agreed the Project was a key enabler for the [Bradford Low Carbon Hydrogen \(BLCH\) project](#), which is being delivered in partnership between [Hygen](#) and [N-Gen](#), and which has been awarded Government funding in the Hydrogen Allocation Round 1 (HAR1) of the Net Zero Hydrogen Fund (NZHF).
- 2.3 NGN's view is that for the BLCH facility to comply with engineering and safety standards, approximately 25% more space is required on the current Birkshall site than had been anticipated when the HAR1 funding application was made. NGN's re-opener funding request is to relocate assets to make the additional space needed for BLCH available. We agreed that the additional space is required at Birkshall to enable the BLCH project and therefore that there is a valid need for the proposed asset relocation works.
- 2.4 We were also satisfied that appropriate optioneering had been considered to address the needs case.

Responses to our Draft Determinations

- 2.5 NGN agreed with our assessment of the needs case and optioneering assessment.
- 2.6 The gas network respondent was supportive of the broader BLCH project, but asked for clarification on our rationale for approving the additional allowances, which would mean that the asset relocation works will be paid for by NGN's gas customers through their gas bills. The response highlighted that in other examples, such as asset relocation for wind farms or biomethane customers, the organisation requesting the site works, and benefitting from them, would pay directly for them, with consumers paying a portion of the costs only where there are additional associated wider consumer benefits.

Cost assessment

Summary of our Draft Determinations

2.7 **Table 2** below highlights what our proposed adjustments and draft allowances were:

Table 2: Summary of our Draft Determinations for NGN's NZASP application (£m, 2018/19 prices)

Cost category	NGN submitted costs	Ofgem adjustments	Draft allowances
Main works*	4.08	0.00	4.08
Risk allowance	0.47	-0.16	0.31
NGN direct costs	0.69	-0.49	0.20
Efficient Project Costs	5.24	-0.65	4.59
NGN contribution (10%)	-0.52	+0.06	-0.46
TIM impact adjustment	-	-0.52	-0.52
Total	4.72	-1.11	3.61**

* Includes £0.04m decommissioning costs originally omitted by NGN

**Note, our draft allowance included an error and should have been £3.65m.

2.8 Our Draft Determinations proposed the following:

- remove business as usual (BAU) costs as these are central business functions which we do not consider to be direct costs,
- reduce the risk allowance from 11.5% to 7.5% in line with average risk allowances across the RIIO-2 business plan portfolio,
- socialise costs across NGN's own customers rather than across all Great Britain (GB) consumers, given the BLCH project will primarily contribute to regional emissions reductions,
- a 10% company contribution rate in line with NGN's proposal, as per NZASP guidance,
- a Totex Incentive Mechanism (TIM) adjustment to protect this contribution.

2.9 We also consulted on proposed project deliverables which must be met as a condition of any awarded funding.

Responses to our Draft Determinations

2.10 The other gas network respondent did not comment on our cost assessment and proposed draft allowances. NGN disagreed with our cost assessment.

- 2.11 NGN disagreed with our assessment of direct costs and the removal of BAU activities as the project is in addition to delivering BAU with additional central activities required to deliver the project to time and scale. If these costs are not funded, NGN claims it could lead to pressure on project delivery and scope.
- 2.12 NGN disagreed with our risk allowance reduction, arguing that the non-operational IT workstream has a greater degree of certainty than asset relocation. The relocation would also interact with medium and high-pressure assets which naturally carries more risk. NGN also highlighted supply chain risk associated with ordering long lead items for the project and potential factors outside of NGN's control which could impact deliverability and lead to increased costs.
- 2.13 NGN agreed with the proposed 10% company contribution rate and did not object to the inclusion of the TIM adjustment. However, NGN made two points:
- i. that there was an error in our draft allowance. We consulted on £3.61m which should have been £3.65m, and
 - ii. that the BLCH project has since confirmed it would pay the 10% company contribution towards the project, not NGN, meaning the TIM adjustment methodology no longer works.
- 2.14 NGN broadly agreed with our proposed project deliverables and draft direction. It provided updated indicative deadline dates and requested that the corrected draft allowance be reflected in the project cost phasing.

Our Final Determinations

- 2.15 Given that the BLCH project is in receipt of government funding through the NZHF, we accept that BLCH is considered an important element of the UK strategy for meeting our net zero targets. On the basis that they are necessary to enable the BLCH project, we are therefore still of the view that there is a valid needs case for the proposed asset relocation works. However, this does not necessarily mean that consumers should pay the costs.
- 2.16 In light of the consultation response from the other gas network, we have considered whether there is a difference in circumstance between the proposed asset relocation works requested by BLCH, and other circumstances where a party requesting works and solely benefitting from them is required to pay for them (for example a wind farm connection or biomethane connection). Our view

now is that there is no clear reason to diverge from established charging practices for this project. In the case of the proposed asset relocation works, the direct benefit is to the BLCH project and, because the relocation works deliver no material system or asset health improvements, there are no direct benefits to consumers as a whole. Any broader benefits to consumers, such as its contribution to the UK net zero pathway, haven't been shown to be materially different from other projects that achieve emission reductions and that are subject to the standard charging principles. We therefore do not consider that there is a case for a different charging arrangement for the asset relocation costs for this project.

- 2.17 We have also further considered the appropriateness of providing additional funding through the NZASP re-opener mechanism for the asset relocations, when the project has already been allocated government support. The BLCH project will receive up to 20% of the project capital costs to support delivery of the project through the NZHF. Costs associated with site development and site remediation – the categories in which the costs associated with the asset relocation works would be classified – were eligible for inclusion in the developer's NZHF application. The total project capital costs also included risk allocation to budget for some additional costs associated with unexpected events or uncertain cost items. This re-opener application has been submitted because the developer did not include these site development and site remediation costs at the time that the developer submitted its NZHF Best and Final Offer (BaFO) in September 2023. We do not consider it appropriate in this instance for gas consumer funding to act as a further funding route in addition to the NZHF support where these costs were eligible.
- 2.18 The considerations above lead us to conclude that it would not be in energy consumers' interests to award additional funding for the proposed asset relocation works. Our Final Determination is therefore to award no additional allowances for the Project under the NZASP re-opener.

3.Next steps

- 3.1 As part of our Draft Determinations, we published a draft direction to give effect to the proposed allowances. As our Final Determination is to approve no additional allowances there is now no requirement to issue a direction. The re-opener application and approval process for this application is therefore concluded.