

Guidance

Draft GD2/GD3 Crossover Guidance and Submission Requirements Document

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Contact: RIIO Future of Gas (Gas Distribution)

Email: RIIO3@ofgem.gov.uk

Overview

This document is directed at gas distribution network companies (for the purposes of this document ‘GDNs’ or ‘licensees’) as well as their stakeholders.

The purpose of this document is to set out the general principles, methodologies and processes that the Authority will use when assessing the need for, and the value of, any amendments to RIIO-GD2/RIIO-GD3 (‘GD2/GD3’) Crossover adjustments as set out in Special Condition 3.32 of the GDN licences. It also sets out requirements in relation to applications and other submissions by the Gas Distribution (GD) licensees that are required to support the Authority’s assessments.

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Contents

Overview	1
1. Introduction.....	4
2. Definitions and scope of coverage of adjustments to allowances	5
Definition of an GD2/GD3 Crossover Item.....	5
Scope of adjustments under the GD2/GD3 Crossover mechanism	6
3. General principles for GD2/GD3 Crossover adjustments	8
4. Approach to determining GD2/GD3 Crossover adjustments	9
5. Process for making adjustments under the GD2/GD3 crossover mechanism ...	12
Adjustments initiated by Ofgem	12
Adjustments initiated by GDNs	12
Assessment of applications and timing of decisions.....	14
Implementation of decisions	14

1. Introduction

- 1.1 This chapter sets out the background to the GD2/GD3 Crossover Submission Requirements and Guidance Document.
- 1.2 This document is issued by the Authority in accordance with Special Condition 3.32 of the GDN licences. This document applies exclusively to the GDN licensees.
- 1.3 As part of our decision to modify the licences held by the licensees to implement the RIIO-GD3 price controls we decided to create a GD2/GD3 Crossover mechanism through which we may adjust RIIO-GD3 allowances and, where appropriate, create new RIIO-GD3 outputs, for GD2/GD3 Crossover items, which are outputs, deliverables or activities that are funded in full or part by a RIIO-GD2 mechanism and where the GDN efficiently incurs expenditure in the RIIO-GD3 period.
- 1.4 This document sets out:
 - Definitions and scope of coverage of adjustments to allowances under the GD2/GD3 Crossover mechanism.
 - The general principles that the Authority will have regard to when making amendments to allowances under the GD2/GD3 Crossover adjustments mechanism.
 - the timing and format of requests by the licensee for an amendment to allowances under the mechanism.
 - the details of information required to be provided by the licensee to the Authority to support a request for amendment to allowances.
 - the Authority's process and timing for making amendments to any allowances.
- 1.5 This document is to be read in conjunction with the following documents:
 - Gas Distribution Special Conditions
 - RIIO-GD3 Price Control Financial Handbook
 - RIIO-GD3 Final Determinations
 - PCD Guidance
 - The Gas Act 1986, ('The Act')
- 1.6 In this Guidance, we use the terms 'Ofgem' and 'the Authority' as well as the terms 'we', 'us' and 'our' interchangeably. Ofgem is the Office of Gas and Electricity Markets. The Authority is the Gas and Electricity Markets Authority and is the governing body of Ofgem, consisting of executive and non-executive members.

2. Definitions and scope of coverage of adjustments to allowances

This chapter sets out the definitions and scope of coverage of adjustments to allowances under the GD2/GD3 Crossover mechanism.

2.1 Through our price control determinations, we set:

- outputs to reflect the attributes of network service quality that are of most value to current and future consumers; and
- price control allowances for the relevant price control period that reflect our view of the efficient cost of delivering those outputs.

2.2 Our RIIO-2 price controls covered the period from 1 April 2021 to 31 March 2026, and our RIIO-3 price controls will cover the period from 1 April 2026 to 31 March 2031.

2.3 We recognise that the periodic price control review process is not necessarily aligned with the way in which licensees undertake activities required to deliver their outputs. There are circumstances in which the delivery of price control outputs or deliverables set for one price control period may involve the GDNs efficiently incurring expenditure in the next period.

2.4 The purpose of the GD2/GD3 Crossover adjustments mechanism is to provide an explicit route for the Authority to provide funding to GDNs for efficiently incurred expenditure on GD2/GD3 Crossover Items as defined in Special Condition 3.32 GD2/GD3 Crossover Adjustments.

2.5 The provisions of the Special Condition 3.32 GD2/GD3 Crossover Adjustments are complementary to the process for closing out the RIIO-GD2 price control ('close out'), the methodology for which will be set out separately by Ofgem. The GD2/GD3 Crossover mechanism is intended to act as a backstop, providing a route for the Authority, where necessary and at its discretion, to remunerate efficiently incurred expenditure on qualifying items.

Definition of an GD2/GD3 Crossover Item

2.6 A GD2/GD3 Crossover Item is defined in Special Condition 3.32 of the RIIO-GD3 licences. This definition includes Outputs, Price Control Deliverables (PCDs) or activities that are funded in part or in full by a RIIO-GD2 mechanism and where the licensee has efficiently incurred (or will incur) expenditure in the RIIO-GD3 period.

2.7 This includes the following types of mechanisms:

- PCDs, both mechanistic and evaluative, for example the Cyber Resilience PCDs created under Special Condition 3.2 Cyber Resilience Re-opener and Price Control Deliverable (CROT_t and CROTRE_t).
- Use it or lose it (UIOLI) mechanisms, for example the mechanism created under Special Condition 3.5 Net Zero and Re-opener Development Fund use it or lose it allowance (RDF_t).

Scope of adjustments under the GD2/GD3 Crossover mechanism

2.8 Special Condition 3.32 of the RIIO-GD3 licence specifies two criteria (of which at least one must be met) for making adjustments to allowances.

2.9 The first is the part-funding criterion. We may make an adjustment to allowances under the GD2/GD3 mechanism if the funding provided by a RIIO-GD2 mechanism for a GD2/GD3 Crossover item was only intended to cover part of the efficient cost of delivering the item in full and there is no other mechanism in the licence as in force at the time of the amendment that could otherwise fund the remaining efficient cost of the GD2/GD2 Crossover Item.

2.10 For example, this might be the case where an output specified in GD2 was due to be delivered during the RIIO-GD3 period, with expenditure expected to be incurred in both the RIIO-GD2 and RIIO-GD3 periods, and funding provided by the relevant mechanism in the RIIO-GD2 licence only covered costs expected to be incurred in the RIIO-GD2 period. In such circumstances, we may use the GD2/GD3 Crossover mechanism to provide funding for efficient costs incurred or expected to be incurred in the RIIO-GD3 period.

2.11 The second is the RIIO-GD2 close out criterion. We may make an adjustment to allowances under the GD2/GD3 mechanism if adjustments to allowances made through the provisions specified under Special Condition 7.2 Legacy AIP Adjustment (LADJ_t) of the licence would result in (or are expected to result in) a negative adjustment to allowances for a GD2/GD3 Crossover item such that the efficient cost of delivering the item is no longer fully remunerated through the GD3 licence as originally intended.

2.12 For example, this might be the case where an evaluative PCD set as part of the RIIO-GD2 price control (with a delivery date in the GD2 period) is delayed and is now expected to be delivered in Year 3 of the RIIO-GD3 period. The assessment of PCD delivery, carried out in accordance with SpC 9.3 of the GD2 licence, might result in the PCD being assessed as not fully delivered, leading to a reduction in allowances to account for the non-delivery through the GD2 close out process. If the PCD is delivered in full after the close out process has been completed, and we consider that delivery of the PCD would still be beneficial to consumers, we may decide to reverse the reduction through a GD2/GD3 Crossover adjustment.

2.13 When making a decision on adjustments to allowances or outputs relating to a GD2/GD3 Crossover Item, we will consider whether there are alternative

mechanisms in the GD3 licence that could be instead of the GD2/GD3 Crossover adjustment mechanism. Where a suitable alternative mechanism is identified, we will consider the specific circumstances of the GD2/GD3 Crossover Item in making a decision on the appropriate mechanism to use.

- 2.14 We do not intend to use the GD2/GD3 Crossover adjustments mechanism to provide funding to remunerate GDNs for costs incurred in the GD2 period for outputs or PCDs that were not created during the GD2 period.
- 2.15 Notwithstanding the above, and for the avoidance of doubt, nothing in Special Condition 3.32 of the RIIO-GD3 licence restricts our ability to make changes to allowances specified in Appendix 1 or to introduce or amend outputs or deliverables in Appendix 2 in any event by modifying the licence using our powers under Section 23 of the Act if we consider such changes to be necessary.
- 2.16 We provide further information and guidance on our intended approach to the GD2/GD3 Crossover adjustment in Chapter 5.

3. General principles for GD2/GD3 Crossover adjustments

This chapter sets out the general principles that the Authority will have regard to when making adjustments to allowances under the GD2/GD3 Crossover mechanism.

3.1 When considering whether to make an adjustment to allowances, and the value of that adjustment, the Authority will have regard to the following principles.

- **Seamless transition.** We will aim to ensure that the transition from the RIIO-GD2 to RIIO-GD3 does not create unnecessary barriers to, or disincentives for, the efficient operation of the gas network or the efficient and timely delivery of outputs, deliverables or activities by the GDN.
- **Appropriate remuneration of efficient costs.** We will aim to ensure that any shortfalls in funding for efficient costs associated with an GD2/GD3 Crossover item created as a consequence of the transition from the RIIO-GD2 to RIIO-GD3 price control are appropriately remunerated.
- **No undue benefit to GDNs from delaying work into RIIO-GD3.** We will aim to ensure that GDNs do not unduly benefit from delaying delivery of GD2/GD3 Crossover items into RIIO-GD3. This may include re-profiling past or future allowances and the transfer of allowances from the RIIO-GD2 period to the RIIO-GD3 period, to better align with actual delivery dates.
- **Accountability for delivery.** GDNs will normally be held accountable for meeting outputs, deliverables, targets or delivery dates associated with GD2/GD3 Crossover items that are specified in the RIIO-GD2 licence. Where necessary, we will create new outputs, deliverables, targets and delivery dates in the RIIO-GD3 licence to support this. A decision by us to make adjustments under this mechanism does not imply our endorsement of any actions taken by the relevant GDN in relation to the GD2/GD3 Crossover item.
- **Negative adjustments and clawback of RIIO-GD2 allowances.** Where appropriate and in line with these principles, GD2/GD3 Crossover adjustments could be negative and could have the effect of clawing back allowances associated with the GD2/GD3 Crossover item.

4. Approach to determining GD2/GD3 Crossover adjustments

This chapter sets out further guidance on the approach that the Authority intends to take when making adjustments to allowances under the GD2/GD3 Crossover mechanism.

4.1 The table below provide further information and guidance on our intended approach to the GD2/GD3 Crossover adjustments.

Type of RIIO-GD2 mechanism	Intended approach to GD2/GD3 Crossover adjustments
Mechanistic PCDs	<p>Allowances for mechanistic PCDs will be Determined in line with the formulae set out in the relevant condition in the GD2 licence.</p> <p>Delayed delivery</p> <p>The delivery of RIIO-GD2 mechanistic PCDs may be delayed into the GD3 period.</p> <p>In such circumstances, the application of the formulae in the relevant GD2 licence condition may result in a downward funding adjustment in respect of mechanistic PCD volumes.</p> <p>If some of these mechanistic PCD volumes are subsequently delivered (after the close out assessment is complete) and the Authority considers that delivery is beneficial to consumers, the Authority may use the GD2/GD3 Crossover mechanism to provide appropriate funding to remunerate the licensee for efficient costs associated with the delivery of the delayed mechanistic output, taking account of the benefits delivered.</p> <p>If the adjustment to allowances is done on an anticipatory basis before the mechanistic PCD volumes are delivered, the Authority may introduce new outputs or PCDs in the GD3 licence to hold the GDN accountable for delivery.</p>
Evaluative PCDs and reopeners	<p>All GD2 evaluative PCDs will be assessed as part of the GD2 close out in line with Part A of SpC 9.3 of the GD2 licence.</p> <p>Delayed delivery</p> <p>In some circumstances, the delivery of some RIIO-GD2 evaluative PCDs may be delayed into the RIIO-GD3 period.</p>

Type of RIIO-GD2 mechanism	Intended approach to GD2/GD3 Crossover adjustments
	<p>In such circumstances, and depending on the extent of delay, the RIIO-GD2 evaluative PCD assessment process may result in a downward funding adjustment for non-delivery of the PCD.</p> <p>If part or all of the PCD is subsequently delivered (after the evaluative assessment is complete) and the Authority considers that delivery is beneficial to consumers, the Authority may use the GD2/GD3 Crossover mechanism to provide appropriate funding to remunerate the licensee for efficient costs associated with the delivery of the delayed evaluative PCD, taking account of the benefits delivered.</p> <p>If the adjustment to allowances is done on an anticipatory basis before the PCD is delivered, the Authority may introduce new outputs or PCDs in the RIIO-GD3 licence to hold the GDN accountable for delivery.</p> <p>Reopener submissions made before 31 March 2026</p> <p>A licensee may submit (or have submitted) a valid application for additional funding or adjustments to outputs under a reopener mechanism in the RIIO-GD2 licence.</p> <p>Provided a valid and complete application is made on or before 31 March 2026, Ofgem will assess these applications in accordance with the provisions contained in the relevant conditions at the time of application.</p> <p>If, following its assessment of the application, Ofgem decides to make adjustments to allowances, we will do so by making an adjustment to the relevant allowance term under the GD2/GD3 Crossover mechanism.</p> <p>If Ofgem decides to amend existing outputs or create new outputs, we will do so through a modification to the GD3 licence using our powers under Section 23.</p>
UIOLI	<p>Unused UIOLI allowances</p> <p>In some circumstances, GDNs may not have fully utilised allowances provided on a use it or lose it basis (UIOLI) in the RIIO-GD2 price control period. In these circumstances, there may be benefits in allowing GDNs to transfer the unused funding into the RIIO-GD3 period, though we consider this unlikely.</p>

Type of RIIO-GD2 mechanism	Intended approach to GD2/GD3 Crossover adjustments
	<p>If the Authority considers that there are benefits to transferring the unused funding to the GD3 period, we intend to use the GD2/GD3 Crossover mechanism to provide the funding for the GD3 period.</p> <p>The Authority may apply conditions to such GD3 allowances, including by setting outputs or price control deliverables, or a use it or lose it condition.</p>

5. Process for making adjustments under the GD2/GD3 crossover mechanism

- 5.1 As set out in Special Condition 3.32, we intend to make any amendments to allowances specified in Appendix 1 of the condition and, where appropriate, introduce new outputs or deliverables using our powers under Section 23 of the Act.
- 5.2 These adjustments are intended to be complementary to the GD2 close out process. Therefore, in most cases our expectation is that we would wait until the completion of the GD2 close out process before making an adjustment under the GD2/GD3 Crossover adjustments mechanism.
- 5.3 Where we are satisfied there are no material interactions between the GD2/GD3 Crossover item and the GD2 close out process, or that it is not necessary or appropriate to wait until the conclusion of the GD2 close out process, we may decide to make adjustments under the GD2/GD3 Crossover adjustments mechanism at any time.
- 5.4 Adjustments under the GD2/GD3 may be initiated by Ofgem or they could be made following an application by GDNs. The rest of this section sets out our intended process for making adjustments.

Adjustments initiated by Ofgem

- 5.5 Ofgem may initiate an adjustment under the GD2/GD3 Crossover adjustments mechanism at its discretion at any time during the price control period.
- 5.6 For instance, the GD2/GD3 Crossover adjustments mechanism might be used by Ofgem to give effect in GDNs' licences to a funding decision that it has already made where a suitable alternative mechanism is not available in the GD3 licence.
- 5.7 In such cases, there is no need for a formal application from GDNs. However, Ofgem may require GDNs to provide such information as may be necessary to ensure the amendments made under the mechanism are appropriate.

Adjustments initiated by GDNs

- 5.8 If a GDN considers that an adjustment to allowances or outputs under the GD2/GD3 Crossover adjustments mechanism is required, it must submit a request in writing to Ofgem. Such requests may be submitted at any time during the GD3 period.
- 5.9 Any requests for adjustments under the GD2/GD3 crossover mechanism must include the following:
 - A detailed explanation of the need for the requested adjustment to allowances specified in Appendix 1 of Special Condition 3.32, including as a minimum:

- An explanation of how the requested adjustment meets the definition of an GD2/GD3 Crossover Item as specified in Special Condition 3.32.
- Demonstration, along with supporting evidence, that without the requested adjustment, the licensee would not be adequately remunerated for the efficient cost of delivering the GD2/GD3 Crossover item.
- Demonstration, along with supporting evidence, that the requested adjustment is beneficial and in the interests of current and future consumers.
- A detailed explanation of the calculation of the requested adjustment to allowances specified in Appendix 1 of Special Condition 3.32, including as a minimum:
 - Demonstration, along with supporting evidence, that the costs intended to be remunerated by the requested adjustment are economic and efficient.
 - Where forecasts are relied upon, a demonstration with evidence that the forecasts are based on reasonable evidence and are robust under different scenarios.
 - Demonstration along with supporting evidence that the costs intended to be remunerated by the requested adjustment are not (and will not be) remunerated otherwise by a mechanism in the licence.
- A detailed explanation of how consumers' interests will be protected as a result of implementing the requested adjustment, including where appropriate:
 - Proposals for new outputs or deliverables that can be used to hold the licensee accountable for the intended benefits to consumers of the requested adjustment.

5.10 Licensees must provide high-quality information in applications to support our assessments of those applications. To this end, and as far as reasonably possible, applications from licensees must be accurate, unambiguous, complete, and concise.

5.11 All applications must be accompanied by written confirmation from a suitable senior person within the company that the application has been prepared and submitted, such that:

- it is accurate and robust, and that the requested adjustments are in the interests of consumers.
- there were quality assurance processes in place to ensure the licensee has provided high-quality information to enable Ofgem to make decisions which are in the interests of consumers.

- the application has been subject to internal governance arrangements and received sign off at an appropriate level within the licensee.

5.12 A point of contact must be provided for each application, including name, position, email, and phone number.

Assessment of applications and timing of decisions

5.13 Ofgem will assess applications from licensees under the GD2/GD3 Crossover adjustments mechanism in accordance with our principal objective and statutory duties. In doing so, we will also have regard to the general principles set out in Chapter 3 above.

5.14 We will aim to complete our assessment of applications and publish our decision in a timely manner. We recognise that unnecessary delays in reaching a decision could have detrimental impacts. However, the timeline for our decision on individual applications may vary and depends on several factors including the complexity of the issues raised, the quality and completeness of information provided in the application, the extent of interaction with the GD2 close out process and whether there are inter-related matters being concurrently assessed.

Implementation of decisions

5.15 If, following our assessment of an application under the GD2/GD3 Crossover condition, we decide to make an adjustment to allowances set out in Appendix 1 of the condition, we will seek to implement this as soon as practical afterwards through a modification to the licence using our powers under Section 23 of the Act.

5.16 Where necessary to protect the interests of consumers and to ensure licensees remain accountable for delivery of funded work, we may decide to create new outputs or PCDs using our powers under Section 23 of the Act.