

## **Cost survey *pro forma* – guidance for completion**

### **Purpose**

The Third Consultation document in the Transmission price Control Review (TPCR) process, due for publication in March 2006, will describe Ofgem's preferred option for enduring offtake arrangements from those described in the December 2005 consultation document. This decision will be informed by a quantified cost benefit analysis, evaluating the NPV impact of the different high-level options presented in the Second consultation document in December 2005<sup>1</sup> relative to the status quo (as defined by the transitional offtake arrangements).

In developing the March consultation document, Ofgem will therefore need to consider the costs that would be incurred should each of the alternative options be implemented. To this end, Ofgem has developed a pro forma through which relevant and detailed information regarding gas transporter (GT) and Agency costs can be provided to Ofgem.

This document:

- outlines the principles that have been applied in developing this pro forma;
- provides high-level guidance to ensure consistency of approach across submissions; and
- provides an overview of the information requested within the pro forma as well as more detailed completion guidance.

### **Principles**

The attached pro forma has been developed to enable Ofgem to gain an understanding of the implications of each of the high-level options for enduring offtake as outlined in the Second Consultation document in December 2005.

This pro forma has been developed to ensure high-level consistency across submissions, whilst also allowing some freedom in the format and disaggregation of detailed cost data and assumptions provided.

Ofgem recognises that in order to provide detailed and consistent cost estimates, respondents need to understand, at a high level, the implications of the specific arrangements proposed for their organisations. In order to do this, a separate assumptions document has been prepared (included as part of this set of documentation) that summarises the arrangements proposed under each of the options presented in the December 2005 consultation document. Ofgem considers this should provide sufficient information for respondents to provide an initial assessment of the cost implications of each of the proposed models for enduring offtake arrangements.

Ofgem recognises, however, that as the options for offtake arrangements are developed in more detail, further analysis will need to be undertaken to develop a more accurate view of the impact of the proposed arrangements. As such, Ofgem envisages that a further impact assessment will be performed as the detail of Ofgem's preferred option is further defined.

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<sup>1</sup> *Transmission Price Control Review Second Consultation*, Ofgem, December 2005, 277/05

## High-level guidance

When completing the *pro forma*, respondents should:

- consider the potential impact on ***their business alone*** – the costs incurred by other parties should not be estimated as part of this submission. Note that this means, for example, that GTs should not include any costs incurred by the Agency in their submissions;
- consider the potential impact in terms of the ***incremental costs of implementing*** the changes proposed only – please do not include a quantification of the expected change in your business's net financial position as a result of an expectation of changes to risks or charges faced as a result of the proposed reform;
- estimate the costs incurred ***relative to the transitional arrangements***, and as such 'net off' any benefits that may result from implementation of the proposed framework, for example, if the proposals require an additional 2 FTEs, yet replace a current process requiring 1 FTE, then the net impact is an additional 1 FTE. Furthermore, net benefits should be expressed as negative figures;
- ***where certain key decisions have yet to be made***, please provide an estimate of the costs imposed by the ***lowest cost solution***, with estimation of the additional costs that would be incurred, should a more costly solution be adopted, provided in the commentary;
- provide cost estimates that represent the ***most likely outcome*** i.e. base case / median estimates – any worst case scenarios and assessment of risks should form part of the detailed commentary provided;
- distinguish between ***implementation (one-off)*** and ***ongoing costs***;
- ensure that the costs of introducing new systems and processes are only included where the introduction of such measures is ***efficient and necessary***;
- submit costs in thousands of pounds (***£k***), specified in 2006 prices; and
- ***provide sufficient detail*** i.e. disaggregation of cost data / documentation of assumptions to allow an understanding of the derivation of high-level estimates, ideally providing:
  - cost drivers i.e. what causes costs to change; and
  - a break down by cost category as appropriate as well as a more detailed explanation of what the costs represent.

## Overview of *pro forma*

The *pro forma* has been structured into separate sections, relating to each of Options Ex2, Ex3, Ex3A and Ex4, as specified in the December 2005 Second Consultation.

The assumptions paper details the proposed arrangements in each of these areas, which should be assessed in relation to the transitional arrangements (Option Ex1).

Within each area, the *pro forma* requests information on:

- net up-front implementation costs – these costs should be one-off in nature and non-recurring; and
- the net ongoing annual costs of operating under the proposed framework once they have reached a steady state.

Both the up-front implementation costs and ongoing operations costs are further disaggregated into the following sub-categories:

- IT systems costs;
- staff costs; and
- other.

Where applicable, benefits should be expressed as negative figures.

Further data fields have been added to allow the estimation of staff costs to be more fully understood. The number of additional FTEs required should be provided. The spreadsheet will then automatically generate the average cost per FTE on the basis of the staff cost total and FTE numbers submitted. Please sense check the number generated.

In general, white cells within the *pro forma* indicate cells where formulae such as totals have been hard-coded into the spreadsheet to ensure that the numbers provided reconcile. We would ask that you check the numbers that are generated to ensure that they accurately represent your views. Cells requiring data entry have been colour coded in yellow.

### ***Detailed commentary***

The data fields on the *pro forma* have been kept to a small number to reflect the differing characteristics and estimation methodologies of each respondent. However, as a result, it is extremely important that there is sufficient documentation of the estimation methodologies and assumptions applied to allow Ofgem to understand the key cost drivers and any underlying differences in views between respondents.

We would therefore ask that the commentary provided is as detailed as possible. This can be provided either within the Excel *pro forma* or you may find Word attachments to be more appropriate.

Ofgem would expect to the commentary to detail the following:

- **IT systems:** the type of IT systems required, distinguishing between new systems and modifications to existing systems, the functionality of the systems changes, the factors driving this requirement, and the basis / source of the cost estimation. Note that systems costs should only reflect the minimum necessary given the proposals described;
- **Staff costs:** the number of additional staff required (broken down by staff type where appropriate), the factors driving this staff requirement and the skills required, the assumed annual cost of the staff required (by staff type where appropriate), and the basis for the cost estimation;
- **Other costs:** the nature of any other costs incurred, the factors driving these costs and the basis for the cost estimation;

- The **timing / phasing** of the costs proposed i.e. do the one-off implementation costs occur in year one or over a period of time? Do the ongoing costs increase over a number of years before reaching a steady state, and if so, how?
- The key **cost drivers** and breakdown of costs into key cost categories (e.g. customer service or overheads etc) wherever possible, explaining why such costs will be incurred;
- Where an important decision has yet to be reached which would have important implications for costs, an estimation of the **additional costs at risk** should be provided, assuming that the 'worst case' decision is made (specific guidance is provided in certain cases within the assumptions paper);
- **High and low case scenarios** may also be provided, reflecting the potential for variation of the numbers presented (both up and down) and the associated probabilities of these alternative scenarios.

### ***Queries***

Should you have any queries regarding the content of this *pro forma*, please contact Matteo Guarnerio on 0207 901 7493 ([matteo.guarnerio@ofgem.gov.uk](mailto:matteo.guarnerio@ofgem.gov.uk)).

### ***Submission deadline***

The information requested should be returned to Ofgem, by e-mail, by close of business on 9 February 2006. Please e-mail responses to [matteo.guarnerio@ofgem.gov.uk](mailto:matteo.guarnerio@ofgem.gov.uk).