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Dear Joanna

**Re: Gas Distribution Price Control Review - Fourth Consultation Document**

SBGI wishes to submit a response to the above consultation document as follows:

**Chapter 3 Operating and Expenditure Analysis**

**Question 1** *How should we bring together the various consultants' analysis to establish an efficient cost benchmark and cost allowances? In light of our approach to setting a benchmark, what approach should we take to glidepaths?*

SBGI would urge caution in applying and combining the consultants' proposals. Further consideration should be given to understanding the material differences between networks, recognising specifically that the 'sold' networks are still in start-up mode and differing organisational models are in play.

There is a risk to the supply chain in applying inappropriate cuts because of wrong comparisons, coupled with possible cherry-picking of efficiencies at activity level.

We would support therefore Ofgem's approach that a top-down view for each GDN using supporting benchmark studies is the preferred approach to bringing together opex data, reflecting the potential limitations of comparative data.

**Question 2** *Is there a case for making adjustments to allowances for real price effects, specifically direct labour, contract labour or materials?*

A large proportion of investment programmes is delivered through the use of contractors, several of which are members of SBGI Network Engineering Group. Our view is that contractor inflation is expected to continue over the forthcoming price control period due to:

✎ Continuing high levels of demand being experienced in the construction industry

- ✍ Major infrastructure renewal programmes in both gas and water, with ongoing maintenance programmes to replace ageing equipment.
- ✍ Demographic profiles of the gas industry as a whole show that there is an ageing workforce with a high proportion of its field workers over 50 years of age. The cost of training and retaining staff, in particular at the engineering manager level, needs to be considered together with attracting suitable young entrants to the utility business.

As a result, it is important that allowances are reflective and appropriate to ensure that GDNs retain the flexibility to use contractors as and when required.

The forthcoming period coincides with a cyclical peak in plant renewal, as a large number of above-ground assets were installed in the 1970s, leading to an intense period of equipment purchase, on-going maintenance, and procurement activity. Appropriate funding is needed for all these activities.

**Question 3** *Is there a case for making adjustments to allowances for regional factors, and if so, what approach should be taken?*

SBGI agrees and supports an objective rather than anecdotal view of regional factors that may distort both contract/direct labour cost and back office functions.

Although not part of the formal response to questions, SBGI offers the following comments on Incentives and responses thereto in the 3<sup>rd</sup> Consultation, summarised in Appendix 5.

## **IFI**

SBGI refers to its response on IFI made during the 3<sup>rd</sup> Consultation, and reaffirms its support for a mechanism to encourage innovations beyond the time frame of the periodic review cycle, and in a comparable way to electricity distribution and energy transmission. Contrary to the view of the gas sector as a mature industry, and in pursuit of long term efficiency, opportunities exist for:

- ✍ Technology development to improve replacement techniques, buried asset location and condition, excavation protection systems
- ✍ Environmental development; gas quality impacts due to supply diversity, recycling technologies, hazardous waste reduction and vibration noise reduction; sustainable development.
- ✍ Asset management – optimising asset life, condition assessment, asset data capture and data quality assurance.

## **Network Extensions to the fuel poor**

SBGI supports the view that if network extensions are to make a real difference to fuel poverty, it is imperative that funding is made available to coordinate access to other government funding, ensuring maximum uptake in connecting to the mains and allowing for additional services such as the installation of central heating to be undertaken.

SBGI intends to play a lead role in facilitating dialogue across the industry in the forthcoming months.

Kind regards

Yours sincerely

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