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1<sup>st</sup> September 2015.

Mick Watson  
Head of Gas Distribution  
Smarter Grids & Governance  
Ofgem  
9 Millbank  
London SW1P 3GE.

Dear Mick,

**Consultation on Ofgem's minded-to position for the determination of a proposed relevant adjustment associated with specified streetworks costs under the RIIO-GD1 price control review**

Thank you for the opportunity to respond to the above consultation. This is a non-confidential response on behalf of the Centrica Group, excluding Centrica Storage.

We do not believe that any additional revenue should be allowed at this stage, because:

- **Evidence required by Ofgem has not been provided.**
- **The evidence that is available does not provide assurance that costs relating to permits, administration and productivity are efficient.**
- **Insufficient independent and historic data exists in order to generate forecasts for the entire RIIO-GD1 price control.**
- **Resubmissions may be made during the 2018 reopener application window.**

Additionally, it is not clear to us how the timescales for this consultation process allow for stakeholder views to be fully taken into account.

***Evidence required by Ofgem has not been provided***

The consultation is clear that NGGD has not met the requirements in terms of providing evidence:

*“Prior to submission, we requested that the applications for relevant adjusted costs are forecast by HA, in line with previous streetworks reopeners. This is an important consideration as a number of GDNs highlighted differences between HAs as a significant*

*issue for them to manage. However, NGGD did not submit its proposed adjustment on this basis and said that the information was not available at this level of detail.”<sup>1</sup>*

The use of these HA data to generate expenditure forecasts would have provided stakeholders with comfort that the additional allowance requests robustly reflect costs likely to be incurred. Little explanation or justification is given for why this data was not provided. We find it difficult to understand how the GDNs could have generated robust forecasts without the ‘bottom-up’ data from the HAs which impose these costs and, if this is the case, we do not believe the additional allowance requests could be accepted to robustly reflect the costs likely to be incurred. The consultation does not seek to explain why submissions are being assessed without these requirements being met and such an approach would appear inconsistent with Ofgem’s draft decision to reject NGGT’s application for additional funding for RIIO-T1 Compressor Emissions costs primarily due to NGGT’s failure to fulfil the specific requirements set out for the re-opener submission.

### **Deficiencies in evidence submitted**

We are concerned about the proposal to make allowances available on the basis of efficiency as the consultation identifies significant concerns over the quality of the evidence that is provided. At RIIO-GD1 Final Proposals, the Authority set out the requirement for evidence of cost efficiency to accompany reopener applications and its intention to conduct efficiency assessments:

*“When a GDN makes a request for additional revenue it will need to provide evidence of the efficiency of the costs incurred, or expected to be incurred. The submissions will then be subjected to an efficiency assessment and we will undertake a consultation to allow all interested parties to comment.”<sup>2</sup>*

Further, in paragraph 8.48 of the same document (which relates specifically to the streetworks uncertainty mechanism):

*“Our March Strategy Document set out the costs that would be included as part of a reopener in this area. We have not made any changes to the type of costs that will be recoverable through this mechanism. In evaluating the efficiency of the costs incurred we intend to follow the same approach used in the current price control (GDPCR1) reopener assessment which was completed in December 2011. We expect GDNs to demonstrate the efficiency of the costs incurred.”*

We observe that concerns have been raised about the quality of the evidence submitted for three of the four cost categories discussed in the consultation. On page 5, deficiencies in the evidence relating to permit costs are mentioned:

*“Our consultant concluded that permit fees are proportionate to the work types and schemes, however there is insufficient supporting evidence to substantiate that the level of permit variations have been efficiently incurred and that the volume of variations in North West is exceptionally high.”*

On pages 5 and 6, deficiencies in the evidence relating to administration costs are mentioned:

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<sup>1</sup> Page 5 of the consultation document.

<sup>2</sup> RIIO-GD1: Final Proposals - Finance and uncertainty supporting document: Finance and uncertainty supporting document para 8.43

([https://www.ofgem.gov.uk/sites/default/files/docs/2012/12/3\\_riiogd1\\_fp\\_finance\\_and\\_uncertainty\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2012/12/3_riiogd1_fp_finance_and_uncertainty_0.pdf))

*“There was a large variation in unit costs per project across the three GDNs, which ranged from £207 in the North West, £480 in London and £2,169 in East of England. NGGD did not adequately explain or justify the differences across the GDNs...”*

AND

*“Our consultant reviewed administration costs at the lower level activity and concluded that there is a lack of evidence and clarity for some cost categories although overall costs appeared to be reasonable.”*

On page 6, concerns are deficiencies in the evidence relating to productivity costs are mentioned:

*“However, as NGGD were unable to submit their application at a detailed highway authority level we were unable to make a judgement on whether these costs were efficient or justified.”*

AND

*“Our consultant concluded that productivity costs are understandable but it is unclear whether the costs are a mathematical exercise multiplying the impact for all works, or whether the costs recorded, are additional costs incurred. In addition some of the costs may be mitigated in the future by innovative techniques.”*

We fail to understand how it can be concluded that any costs relating to permits, administration or productivity can be deemed efficient given the doubts about the robustness of the supporting evidence. The data presented in the consultation (and replicated in the table below) illustrates the fact that concerns have been raised about the quality of evidence submitted in support of about 82% of the total claim. We do not believe, therefore that sufficient assurance has been provided that the costs relating to permits, administration or productivity are efficient.

**Table 1: Claims Submitted**

Category	GDN Claim (£m)			Category Total (£m)	% of Total NGGD Claim	% of Total NGGD Claim
	EoE	London	NW			
Permits	2.5	2.8	4.6	9.9	31.6%	<b>82.4%</b>
Administration	1.6	1.2	0.9	3.7	11.8%	
Productivity	3.9	4.8	3.5	12.2	39.0%	
Lane Rental		5.5		5.5	17.6%	17.6%

### ***Insufficient independent and historic data***

We share concerns about forecasts generated from a single year’s worth of historic data to support claims for allowances over the entire price control. The fact that HAs’ forecasts were not submitted increases our concerns about allowance requests generated from a single year’s worth of historic data. We note also that these costs, for 2013/4, are then adjusted to reflect changes to permit schemes and so are fully representative of future costs. We welcome Ofgem’s proposal to reflect the potential for further cost savings through innovation but, given the concerns about insufficient historic data expressed in the consultation, we do not believe that it is sensible or necessary to provide additional allowances at this stage. There are other ‘check points’ later the current price control at which this could feasibly be revisited (such as the mid-period review and the 2018 reopener application window) when a better view on efficient costs would be available. NGGD may also be able to provide the information specified by RIIO GD1 Final Proposals by that point. It is

unclear what the advantages of settling at this stage, particularly for the entire period, are for customers.

### ***Resubmissions during the 2018 reopener application window***

We recommend that the reopener applications are not progressed at this stage given the concerns about the quality of the supporting evidence. The GDNs may be permitted to resubmit these applications for additional allowances during the 2018 reopener application window. In such a scenario, we expect the GDNs to submit evidence of sufficient quality that would facilitate cost efficiency assessments.

Alternatively, provisional allowances could be provided up until a 'check point' such as from start of the price control to the mid-point. These provisional allowances could be made available subject to:

- An efficiency assessment of the expenditure over this shorter period being conducted at the 'check point'.
- A requirement for the GDNs to fully satisfy the evidential requirements.
- The provisional allowances being returned to customers if the GDNs, again, do not fully satisfy the evidential requirements and cannot prove the expenditure over this shorter period was efficiently incurred.

### ***Insufficient opportunity for stakeholders' views to be taken into account***

Finally, we do not believe that sufficient time has been allowed for stakeholders' views to be taken into account during the assessment of the gas distribution networks operators' (GDNs') proposals. We recognise that special condition 3F.20 of the GDNs' licences stipulates adjustments will default to those proposed by the GDNs unless a decision is made within four months of the receipt of applications and so restricts the process:

*"If the Authority has not determined a relevant adjustment in relation to a proposal duly made by the Licensee under paragraph 3F.6 of this condition within four months after the close of the relevant application window (or in relation to Smart Metering Roll-out Costs within four months of the receipt of a relevant adjustment proposal), and the proposal has not been withdrawn, then the relevant adjustment, insofar as it relates to changes to allowed expenditure levels for the Licensee for the Formula Years specified in the proposal, will be deemed to have been made."*

Stakeholders have been invited to comment on the proposals for additional allowances no later than one month after this consultation was published, which was published two months after the close of the 2015 reopener application window<sup>3</sup>. We believe a consultation period of only month is insufficient for stakeholders other than GDNs to properly assess the proposals. We also believe that the remaining one month period before the assessment process must end places a significant constraint on the opportunity for any material issues highlighted by stakeholders to be properly considered. Given this, we believe all future GDNs' allowance requests should be published much earlier in order to give non-GDN stakeholders early sight in light of the short assessment window.

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<sup>3</sup> Special condition 3F.10 of the GDNs' licences states the application window closes on May 31, 2015.

We hope you find our comments helpful. Please do not hesitate to contact me if you have any questions.

Yours sincerely,

Andy Manning  
Head of Network Regulation, Forecasting and Settlements