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Re: RIIO-T1 reopener consultation: Enhanced Physical Site Security Costs

Dear Kiran,

This response is submitted by National Grid Gas Transmission (NGGT). We operate and own the gas transmission assets in Great Britain.

We disagree with Ofgem's initial views on the Enhanced Physical Site Security Costs assessment. The main points we would like to make are:

- Shared site complexity: Our 2018 submission consists of a number of shared sites for which the costs are higher than the 2015 benchmark due to the additional complexity associated with undertaking activities on a site owned by another operator. In addition, increasingly challenging market conditions, such as a 47% increase in steel prices since July 2015 are reflected in the slightly higher unit costs. These costs should be funded accordingly.
- Cost allocations: Ofgem's approach of assessing individual elements which span the Main Works Contractor (MWC) and the client has a number of shortcomings, when there are not pre set definitions for these particular line items. Looking at the overall costs and accounting for the additional complexity introduced through shared sites and increasing cost of steel, our submission is consistent with efficient levels set for NGGT in 2015. We have provided a chart showing the unit costs relative to the main cost driver, the site perimeter, in a confidential appendix to this letter. We disagree with the methodology of applying a high-level percentage reductions to individual cost categories when each company and contractor structure and define these cost categories differently. We believe a more appropriate assessment would be against the total cost of delivering the works on a suitable unit cost basis, taking into account extenuating factors such as those outlined in our submission and this response. This would avoid the potential misalignment of activities and costs.
- Project risk: In their consultation Ofgem introduced an assessment of project risk across the MWC and client, for both NGGT and Wales and West Utilities (WWU). This assessment does not take account of the current stage of project delivery as NGGT is at an early stage of project development whereas the WWU sites, as far as we are aware are largely delivered. Therefore, using a similar benchmark for both operators is inappropriate.

- Minor works: In terms of the disallowance of the Minor Costs of £0.6m relating to telecommunication costs we provided clarification as part of the submission supplementary questions and we provide further evidence below to substantiate that this work is driven by the Physical Site Security Upgrade Programme (PSUP) requirement and therefore should be funded.
- Outputs: NGGT has included an output relevant to the development works we would undertake on sites not being delivered within T1. We therefore do not understand Ofgem's statement 'we propose not to allow this request as it is not clear what this work will deliver and why it is needed'.

Specifically, with regards to Ofgem's two questions please see our responses below:

Question 1: Do you agree with our assessment approach?

As part of your response please consider:

- **Our approach to Project Management costs**
- **Our approach to Risk costs**

No, we do not agree with the assessment approach. Ofgem deemed an efficient level of delivering NGGT sites in 2015, and the current Ofgem consultation is not consistent with that assessment.

Applying benchmarks for line items such as client project management and general items and preliminaries is not an effective method for assessing the overall efficient cost of the works. The interaction between client and MWC project management is dependent on the project scale and complexity (which is different for NGGT compared to WWU). NGGT has implemented a number of measures to reduce its client side project management and our contracting strategy ensures all other costs are set through a competitive award process.

The risk costs presented in the submission are a function of the stage of development of the project and Ofgem's assessment does not take account of that fact and needs to be revisited. The reference made by Ofgem to "a minor civil works project" is not aligned with our view of the scheme. 'Minor works' within the construction industry typically relate to small relatively straight-forward projects less than circa £0.5m. The value and complexity associated with these works in delivering the interface between the technology, the civil works and the Alarm Receiving Centre (ARC) results in inherent risks which need to be identified, quantified and controlled through the use of the risk management process. It is unclear from Ofgem's consultation which specific risks they are disallowing to arrive at the overall 9% total and where Ofgem have suggested that risk can be removed through mitigation, it is not clear how this has been reflected in the base works estimate.

With reference to the shared sites, NGGT is mitigating risks through early engagement with the relevant Gas Distribution Network (GDN). However, there are still residual risks involved with working on shared sites where NGGT do not own the site fully. This requires additional planning and interface management to ensure coordinated access for the uninterrupted delivery of the security enhancement scheme.

Question 2: Do you agree with the outcome of our assessment?

As part of your response please consider:

- **Our proposed adjustment on specific work costs**

- **Our proposed adjustment for NGGT development costs**
- **The application of the materiality threshold**

We do not agree with the outcome of the assessment. For minor works, the activities undertaken in this category of costs are not a duplication of existing telecommunications infrastructure. Each site is required to have two separate communication links, whose sole function is to connect the site to the NGGT ARC and both site connections are required to be dedicated for the use of the site security only. These minor works costs therefore should be included in the allowed costs.

In addition, the General Items and Preliminaries will be higher due to the need to complete works at shared sites that require engagement and operational liaison with the site owner. The application of the materiality threshold is appropriate however it should be reviewed in light of the comments above. We believe making the adjustment in line with Ofgem's 2015 assessment which would result in NGGT exceeding the materiality threshold.

We hope you find this response helpful. If you would like to discuss any of the above please do not hesitate to contact me.

Yours Sincerely

A handwritten signature in black ink, appearing to read 'A. T. Nixon', with a stylized flourish at the end.

Tony Nixon
Head of Gas Transmission, Regulation

Appendix 1 Cost Assessment

<CONFIDENTIAL>