RIIO-ED1 Reopener Decision – Specified Street Works Costs

Publication date:	18 October 2019	**Contact:**	RIIO-ED Team
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Context

The RIIO-ED1 price control sets the outputs that the electricity distribution network companies need to deliver for consumers and the associated revenues that they are allowed to collect for the eight-year period from 1 April 2015 until 31 March 2023.

For cost categories where there was a significant degree of uncertainty about expenditure requirements at the time of setting allowances, the price controls include a "reopener" mechanism. The mechanism allows network companies to propose adjustments to baseline expenditure allowances for these costs when there is more certainty. The reopener mechanism specifies a window in May 2019, during which adjustments to allowances may be proposed.

We have received reopener submissions in the following cost categories:

- High Value Project Costs
- Rail Electrification Costs
- Enhanced Physical Site Security Costs
- Specified Street Works Costs

This document sets out our decision on applications received under the "Specified Street Works" category of uncertain costs.

Associated documents

Informal consultation on RIIO-ED1 price control reopeners (May 2019)

Consultation on RIIO-ED1 price control reopeners (August 2019)

RIIO-ED1 Price Control Financial Handbooks (fast-track and slow-track licensees)

Contents

1. Executive summary

1.1 In the May 2019 reopener application window, we received submissions from five Distribution Network Operators (DNOs) across eight licensees, requesting an adjustment to their expenditure allowances in relation to Specified Street Works Costs (SSWC). The eight licensees were:

- Electricity North West Limited (ENWL)
- Northern Powergrid (Northeast) Limited (NPgN), which is part of Northern Powergrid (NPg)
- Northern Powergrid (Yorkshire) plc (NPgY), which is part of NPg
- Scottish Power Manweb (SPMW), which is part of Scottish Power Energy Networks (SPEN)
- Eastern Power Networks plc (EPN), which is part of UK Power Networks (UKPN)
- Western Power Distribution West Midlands (WMID), which is part of Western Power Distribution (WPD)
- Western Power Distribution East Midlands (EMID), which is part of WPD
- Western Power Distribution South West (SWEST), which is part of WPD

1.2 On 2 August 2019, we published a consultation document setting out our initial views on the submissions received in the May 2019 window and sought views from stakeholders on our minded-to position. We received eight responses to this consultation. We reviewed the consultation responses and have taken these into account in our decision.

1.3 As part of our consultation, we set out that we would consider submissions by licensees for logged-up SSWC and, subject to consultation and review by us, determine any revision to the RIIO-ED2 Price Control Financial Model (PCFM). In their consultation responses, some respondents requested clarity on the position regarding the logging-up of SSWC for the remainder of the RIIO-ED1 price control. This is set out in more detail in Appendix 2.

Summary of decision

1.4 Table 1.1 sets out the level of additional funding requested by each licensee, each licensee's materiality threshold (as set out in Appendix 3 to CRC 3F), along with the amount of funding we have decided to allow (if any). Our detailed analysis can be found in Appendix 1.

Table 1.1: Requested and allowed funding by licensee (£m, 2012-13 prices[1])[2]

Licensee	Materiality Threshold	Funding requested	Minded-to allowance	Decision allowance	Difference from request (£m, %)	
ENWL	6.2	10.3	9.0	**9.7**	(0.6)	-6%
NPgN[1]	4.5	5.2	-	**-**	(5.2)	-100%
NPgY[1]	5.9	9.3	-	**8.9**	(0.4)	-4%
SPMW	5.8	21.3	8.0	**8.2**	(13.1)	-61%
EPN	9.7	10.2	-	**9.9**	(0.3)	-3%
WMID	5.7	24.5	-	**-**	(24.5)	-100%
EMID	5.7	20.7	7.6	**7.9**	(12.8)	-62%
SWEST	4.2	11.0	-	**-**	(11.0)	-100%
Total		**112.5**	**24.6**	**44.7**	**(67.8)**	**-60%**

[1] NPg's funding request is based on their May 2019 reopener submission. In response to SQs, NPg identified errors in its submission and provided additional information that allowed us to disaggregate its data to produce specific unit costs. We have considered this additional information in our assessment.

1.5 This document summarises the responses to the consultation we received, sets out our updated view of the submissions and provides our overall decision.

Next steps

1.6 Our decision will be implemented through the 2019 Annual Iteration Process, which means that adjustments to DNOs' allowed revenues will take place from 2020-21 onwards.

[1] Unless otherwise stated, all values are in a 2012-13 price base.
[2] Please note that where the sums do not match the overall total, this is due to rounding.

2. Summary of approach and our minded-to positions

Background to Specified Street Works Costs

2.1 DNOs are sometimes required to work in the highways to access their assets; this is referred to as street works. When DNOs carry out street works, they must comply with the relevant legislation. In England, this includes the Traffic Management Act (TMA) 2004, and in Scotland, the Transport (Scotland) Act 2005.

2.2 DNOs need to obtain permission to work in the highway from the relevant Highway Authority (HA). HAs can adopt different ways of allowing DNOs to work on their roads. These include:

- **A noticing scheme**, where a DNO needs to let the relevant HA know that it will be working in the road
- **A permit scheme**, where a DNO needs to request a permit for time to work on the road. This allows the HA to place specific conditions on the DNO (eg how traffic should be managed, relevant diversions that need to be in place, and the agreed working hours). HAs charge a fee for these permits to cover the cost of coordinating various activities on the roads. Additional charges can apply, for example, if permits need to be varied (ie permit variation costs) or if a DNO exceeds its permitted time for working in the road (ie a penalty charge)
- **A lane rental scheme**, where a HA can charge a DNO for its time in the road. These charges are focussed on the busiest streets at the busiest times, and are currently capped at £2,500 per day.

2.3 We allowed efficient costs for street works as part of the RIIO-ED1 price control where permit schemes had already been implemented and 12 months of cost data was available. However, we included a reopener within the price control in order to provide funding in the event of increased uptake of these schemes and other areas of street works legislation.

2.4 The RIIO-ED1 Strategy Decision[3] set out that the street works reopener mechanism would cover DNOs' additional costs that were not included as part of the ex ante allowance.

2.5 In May 2019, we received submissions from eight licensees (across five DNOs) seeking an adjustment to their allowed expenditure for Specified Street Works Costs (SSWC).

Summary of approach used in our minded-to decision

2.6 We undertook our assessment of the submissions in accordance with the requirements of Charge Restriction Condition (CRC) 3F (Arrangements for the recovery of uncertain costs) of the DNOs' special licence conditions, and Chapter 7 of the RIIO-ED1 Price Control Financial Handbook (the Handbook).[4] These detailed requirements are set out in our consultation, but a high-level summary is as follows:

- The proposed adjustment must be based on auditable information and justification about the actual or forecast level of efficient expenditure that was either unavailable or did not qualify for inclusion when the licensee's Opening Base Revenue Allowance was derived and relate to costs that have been incurred, or are expected to be incurred, after 1 April 2015

- The proposed adjustment must constitute a material amount, must take into account any relevant adjustments that have been previously determined under CRC 3F and must constitute an adjustment that cannot be made under any other condition of the licence

- The proposal must include statements that set out the uncertain cost activities that it relates to, the associated changes to allowed expenditure, as well as the basis for the calculation that the DNO has used to generate the expected costs.

[3] Uncertainty Mechanisms supplementary annex, page 13: https://www.ofgem.gov.uk/sites/default/files/docs/2013/02/riioed1decuncertaintymechanisms_0.pdf
[4] Please see 7.40 (ii) b. and c. of ED1 Price Control Financial Handbook (slow track): https://www.ofgem.gov.uk/system/files/docs/2017/08/ed1_handbook_v3_slowtrack_0.pdf; and 7.42 (ii) b. and c. of the ED1 Price Control Financial Handbook (fast track): https://www.ofgem.gov.uk/system/files/docs/2017/08/ed1_handboook_v4_fasttrack_0.pdf

2.7 We undertook a cost efficiency assessment for each of the cost categories that make up SSWC.[5] More detail on our overall approach is provided in our minded-to consultation document, but a high-level summary of the building blocks of our approach was as follows:

- The **use of a benchmark** to assess whether unit costs were efficient
- To inform the calculation of the benchmark, we determined which **cost categories** we would consider in our unit cost assessment and which costs we would consider on a case-by-case basis
- The **application of an efficiency adjustment** on forecast costs
- A **methodology to forecast permit volumes**.

Use of a benchmark

2.8 To establish a benchmark of efficient costs, we derived an average from the data submitted to us by the DNOs. To do so, we cleansed the unit cost data provided in the submissions and corresponding 2018-19 Cost and Volumes Regulatory Reporting Pack (RRP), removing inconsistencies where they were clear and significant outliers, which would lead to an artificially distorted result. This provided a benchmarked unit cost, which we compared to each licensee's unit cost.

2.9 We used this benchmarked unit cost as a reference point. In assessing unit costs, we considered factors provided in the DNOs' submissions that justified any differences between our view and the DNO's submitted costs. Unless justified in the DNO's submission, we applied the lower of the licensee's submitted costs and our benchmarked costs when setting proposed allowances for each of the remaining Regulatory Years in the RIIO-ED1 period.

2.10 We did not consider that the information provided by NPg in its submission to be of sufficient quality to include within the benchmarking exercise. This was mainly due to the variability in its costs compared with other licensees over time and our lack of confidence in the information provided for its administration and permit

[5] These are: permit fee costs; administration costs arising from the introduction of permit schemes and lane rental schemes (or their equivalents); costs arising from the introduction of permit conditions and lane rental schemes (or their equivalents) and one-off set up costs.

condition costs. We therefore assessed the costs submitted by NPg separately in our initial assessment.

Cost categories

2.11 In our assessment of unit costs, and in establishing a benchmarked unit cost, we only included costs associated with obtaining a permit (ie permit fee,[6] permit condition and administration costs). We did not include the following costs in our unit cost assessment:

- **Lane rental costs**: as there is continued uncertainty over the future implementation of lane rental schemes, and as licensees were not able to provide the required 12 months of cost data, we did not carry out a unit cost assessment of these costs

- **One-off set-up costs**: as we received only one request for funding under this cost category and it is a one-off cost item, this was considered on a case-by-case basis

- **Penalty charges**: the charges for any penalties incurred as a result of non-compliance with permit conditions or for failing to obtain appropriate permits are an element of street works activities that we believe are within the control of the DNO to avoid. We considered these are an inefficient cost that should not be borne by customers and did not believe that these fall within the definition of SSWC.

Application of an efficiency adjustment

2.12 In our consultation, we set out that there are opportunities for DNOs to improve their performance and reduce costs by, for example, reducing the number of permit variations, working closely with HAs to reduce the impact of street works, and by using innovative solutions.

[6] Permit fee costs include costs associated with varying a permit. These costs, known as permit variation costs, are incurred by DNOs when they make a change to a permit to reflect changes in the planned works.

2.13 We applied a 3% efficiency adjustment to the proposed allowances for each of the remaining four Regulatory Years in the RIIO-ED1 period.[7] This was to reflect the level of cost savings through efficiencies and innovation that we consider reasonable for DNOs to achieve in the remainder of the price control period.

Methodology to assess permit volumes

2.14 To assess the total volume of permits for each DNO on a consistent basis and to establish an appropriate driver for permit costs (ie permit fees), we removed permit variations from submitted permit volumes and allowed volumes for the first four years of RIIO-ED1. [8] We recognised that there are a number of challenges associated with determining a robust forecast, such as the timing of when a new scheme may be introduced (including where a scheme was introduced part-way through a year), movement from a partial scheme (for example, one which operates only on traffic-sensitive roads) to a full scheme, and where DNO boundaries and HA boundaries overlap. In the absence of actual data for partial schemes, we applied a 50% scaling adjustment.

2.15 In order to establish a reasonable number of future permits in each licensee's area, we asked them to confirm the number and percentage coverage of HAs operating in their licence area. We also used information provided in submissions to understand when DNOs expected future permit schemes to be implemented. Based on the data provided, we calculated the average number of permits issued per HA each year where we considered historical information was sufficiently robust.

2.16 We then used this average number of issued permits to establish what we considered to be reasonable forecast volumes, based on the number of HAs expected to be operating a permit scheme. This total figure was compared against the DNOs' submitted forecast volumes. Where DNOs' submitted forecast volumes were lower than our view of reasonable permit volumes, we accepted their forecast volumes; where they were higher, we used our view.

[7] When setting proposed allowances, we applied the lower of the licensee's submitted costs and our benchmarked costs, unless otherwise justified in the DNO's submission. We only applied a 3% efficiency adjustment where we applied the benchmarked unit cost.
[8] Permit variation costs were not excluded from the DNOs' submitted permit fee costs for the first four years of RIIO-ED1. As such, permit fee costs take into account a level of variation costs.

3. Consultation responses and additional information received

Consultation responses and additional information received

3.1 We received eight responses to our consultation published on 2 August 2019, from Centrica, Citizens Advice (CA) and all six DNOs (ENWL, NPg, UKPN, SSEN, SPEN and WPD). Non-confidential versions of these responses have been published alongside this decision. The responses from several DNOs were extensive and raised a number of concerns with our approach encompassing a wide range of issues. We have provided a high-level summary of the key themes raised in the responses here, with further detail below.

3.2 Several respondents had comments on the **costs categories** that DNOs were permitted to recover through this reopener.

3.3 One key theme was the **use of a benchmark** to establish a view on the efficient level of cost. Several DNOs set out their views on how costs have been justified, noting that their limited ability to influence where work needs to occur, or what permit fees are charged, mean that many costs are not comparable with other DNOs and their submissions should therefore be considered individually.

3.4 Respondents made several points relating to the **methodology used for establishing a benchmark** of costs in this reopener. These were broadly in relation to the application of our approach, and the data that was considered and/or excluded from the unit cost assessment. Some respondents raised concerns about how we had treated applications where there were **variations from benchmarked costs**.

3.5 All respondents commented on our application of an **efficiency adjustment** to future costs. DNOs also highlighted concerns with our approach to **assessing forecast volumes of work**. This included how we assessed forecast volumes in HAs that operated across multiple DNO regions.

3.6 Two respondents made reference to a number of **other points**:

- The requirement for 12 months of cost data to be eligible for this reopener

- The treatment of resubmissions and/or additional information provided by DNOs
- Our approach to assessing lane rental costs in the future.

3.7 We discuss the points raised on these issues in more detail below.

Cost categories

3.8 Some DNOs raised concerns that we had not included costs associated with certain activities in our assessment of efficient costs. These included *permit variation costs, one-off set-up costs, and penalty charges*. We note the points raised on each of these below.

Permit variation costs

3.9 Centrica and CA were supportive of our approach, with Centrica considering that permit variation costs are inefficient costs that should not be borne by consumers.

3.10 By contrast, a number of DNOs outlined that certain circumstances may mean that it is necessary to incur permit variation costs and that there are legitimate reasons for incurring permit variation costs where these are outside the control of the DNO, such as minimising the disruption to customers or meeting a customer's request. WPD noted that our approach, which removed the permit variation volumes but retained the associated costs, caused a misalignment of the benchmarked unit costs.

3.11 NPg stated that it is efficient to incur some level of variation and it would be disproportionately costly to avoid permit variations altogether, arguing that the efficient costs associated with avoiding permit variations would be greater than the permit variation costs. It also argued that avoiding permit variations altogether would result in incurring higher levels of penalty charges. NPg also noted that Cadent's permit variation costs were explicitly evaluated and allowed in the 2015 RIIO-GD1 reopener.[9]

[9] https://www.ofgem.gov.uk/sites/default/files/docs/2015/09/150929_-_determination-_riio_gd1_review_streetworks_costs_0.pdf

One-off set-up costs

3.12 WPD noted future policy developments that it expects will impact its street work costs, such as the expected implementation of a new software system and associated costs. WPD requested clarity on whether such future costs could be claimed under a logging-up mechanism as these will be incurred in compliance with Department for Transport (DfT) requirements.

Penalty charges

3.13 NPg was the only DNO to seek funding for penalty charges. There was broad consensus among the other respondents on this issue that penalty charges should not be funded by consumers.

3.14 NPg considers that an efficient level of penalty charges should be allowed and that avoiding permit penalties altogether would not be efficient as it would incur more costs to do so (such as devoting additional staff time on site to ensure ongoing compliance, training staff and putting an audit regime in place to ensure ongoing internal compliance). It stated that the RIIO-ED1 licence and Regulatory Instructions and Guidance (RIGs) do not prevent DNOs from receiving a reopener allowance for penalty charges or the administration costs associated with processing penalty charges. NPg further stated that Ofgem previously recognised an efficient level of costs for penalty charges in the RIIO-ED1 price control review.

3.15 Conversely, SSEN stated these costs should be within the control of the DNOs and should not be borne by the customer. Similar views were expressed by Centrica, CA, ENWL, SPEN and WPD.

Use of a benchmark

3.16 CA and Centrica were supportive of Ofgem's assessment approach. Centrica considered our methodology for estimating efficient costs to be reasonable. CA recognised the difficulties we faced with data cleansing and forming average unit costs for benchmarking, and noted that where unit costs are above this benchmark, they expect to see adequate evidence from DNOs to justify their initial submissions.

3.17 ENWL expressed broad support for using benchmarking to inform a check of submitted costs and, where appropriate and carefully applied, aspects of future

funding. It did not favour benchmarking of permit fee costs as, in its view, DNOs cannot determine where works will take place and, consequently, have limited control over the level of fees. ENWL accepted that some form of comparative analysis between DNOs may need to be made and suggested some improvements that could be made to our approach, such as the use of an inter-quartile range rule to detect outliers. This approach would, in ENWL's view, produce a more accurate benchmark for condition costs than that used in our initial assessment.

3.18 UKPN shared similar views to ENWL. It noted that the RIIO-ED1 Strategy Decision states that, at the time of setting the price control, benchmarking was not considered appropriate for assessing permit volumes and the associated costs. Similarly, UKPN referred to the RIIO-ED1 Final Determination where Ofgem acknowledge that it "is difficult to benchmark [permit condition costs]".

3.19 SSEN supported the principle of benchmarking as a tool only in assessing cost efficiency, and highlighted the need to consider the efficiency of costs incurred. They also noted that circumstances may not always be comparable and that there is a risk that our approach could be overly simplified.

3.20 WPD set out several concerns with our approach to benchmarking, mirroring SSEN's concerns that the approach was over-simplified. WPD argued that the approach overlooked the wider policy environment. It highlighted the differences between how HAs operate, as well as the potential differences in how DNOs report certain costs. Finally, WPD suggested that our approach should take greater account of regulatory precedent, such as the position on assessing permit condition costs set out in the Final Determinations, which prescribe a case-by-case assessment of such costs.

3.21 Other DNOs made reference to the RIIO-ED1 Strategy Decision and/or the Final Determinations to highlight the conflicting positions on assessing SSWC. UKPN indicated that the Strategy Decision sets out that benchmarking would only be used for specific cost categories, rather than for all of them.

Methodology used for establishing a benchmark

3.22 Centrica and CA expressed support for the methodology used for establishing a benchmark. Centrica considered this to be reasonable and CA stated that it was broadly supportive of our assessment approach.

3.23 A number of DNOs stated that our benchmarking approach should include data from a wider spectrum of network companies and only exclude clear outliers, with some highlighting that this would reflect the wide range of variability that is driven by local conditions. UKPN noted that, irrespective of the applicability of benchmarking to SSWC, our initial assessment did not consider all the data that was available at the time (in that we did not use data from London Power Networks (LPN) or South Eastern Power Networks (SPN)). Finally, UKPN contested the application of the benchmarked unit costs stating that this effectively reduces the actual costs incurred by DNOs without evidence that the costs were incurred inefficiently.

3.24 WPD disagreed with the exclusion of its data from our benchmarking approach, stating that changes in unit cost over time occur for a number of reasons (HAs changing their fees or the design of the permit schemes, for example). Similarly, NPg highlighted that it has, and will continue to, incur administration and condition costs associated with permits and therefore disagreed with the exclusion of its costs from the benchmarking.

3.25 WPD considered that the RRP data is not comparable with the data provided in the submissions and that combining the two sources in a simple average is not appropriate. WPD expressed a preference for the RRP data to be excluded from our benchmarking approach.

3.26 WPD also noted that our approach had not benchmarked the costs provided by the DNOs against those from other industries, such as the unit cost applied to Cadent in the 2018 RIIO-GD1 SSWC reopener.[10]

3.27 WPD also requested that we acknowledge that HAs charge a range of fees rather than a single fee and that the benchmarking should be more sophisticated in this regard. Alongside this, WPD requested that our approach to benchmarking is more transparent when it comes to data cleansing, variations between DNOs' submissions and any normalisations or adjustments that are made. It noted that our quantitative assessment should be supplemented by qualitative, case-by-case assessments of DNOs' submissions in each cost category.

[10] https://www.ofgem.gov.uk/publications-and-updates/decision-riio-1-price-control-reopeners-may-2018

3.28 NPg further argued that the different approach applied to its costs was not explained and led to inconsistent outcomes. For example, NPg noted that WPD's costs were also excluded from the benchmarking but nevertheless had the benchmarked unit cost applied to its volumes whereas NPg did not. It also commented that other DNOs' costs, some of which had more variable data, were not excluded from the benchmarking exercise.

3.29 Finally, ENWL proposed the use of statistical techniques to select the relevant data, and as a result it suggested administration costs for NPg, SSEN and WPD's licensees should be removed from all calculations.

Treatment of variation from benchmark costs

3.30 ENWL and WPD noted that DNOs have limited influence over where works will be undertaken on the network, and there is no scope to require HAs to only charge permit fees aligned with the benchmarked cost.

3.31 ENWL considered it inappropriate to benchmark administration costs due to differences in efficiencies already achieved by those DNOs that had established portfolios of permit schemes at the beginning of RIIO-ED1. ENWL also considered that historic costs should not be benchmarked and that its future costs relating to traffic management plans should not have been removed.[11]

3.32 WPD asserted that its submission set out sufficient justification for its higher permit condition costs, but that Ofgem did not issue sufficient further information requests in relation to these costs. WPD noted that its higher permit condition costs are driven by differences between how HAs operate, which have not been taken into account in our benchmarking approach. ENWL and UKPN made similar points, suggesting it is inappropriate to benchmark these costs.

3.33 WPD stated that in a previous reopener assessment, Ofgem determined that permit condition costs are not comparable; WPD therefore recommended that these costs are considered on a case-by-case basis.

[11] This relates to certain works in the Lancashire and Greater Manchester areas, where there is a requirement for multi-way temporary traffic signals, or road or lane closures.

3.34 NPg stated that there are legitimate reasons for its unit cost variations over time and across both licensees and as compared with other DNOs in the first four years of the price control, such as different portfolios of schemes across licensees. It pointed to schemes introduced in 2015 in NPgY's licence area that had very limited coverage on HA road networks and which focussed on traffic-sensitive areas only. It also noted that NPgN's licence area had only one permit scheme in place for the majority of ED1 to date. Both were presented as unique factors for why NPg's unit costs should be expected to vary compared to those of other DNOs.

3.35 WPD disagreed with our view that significant variations in unit costs over time are inconsistent and stated that year-on-year movements in unit costs do occur. It requested that its data be included in the calculation of the benchmark on the basis that unit cost fluctuations is an unreasonable justification for its costs being excluded from the benchmark, and also to provide a more representative view of the reopener submissions and to avoid a downward bias to unit cost benchmarking.

Efficiency adjustment

3.36 Most respondents expressed views on the application of a 3% efficiency adjustment to forecast permit fee costs, administration costs and permit condition costs.

3.37 Centrica and CA expressed support for our minded-to position to apply an efficiency adjustment, with Centrica going on to note that licensees should be able to achieve operational efficiencies over time.

3.38 Some DNOs expressed concerns with the application of our proposed efficiency adjustment and in particular, several DNOs questioned the basis for determining and justifying a rate of 3%. WPD, UKPN and ENWL noted that this efficiency rate is significantly higher than the 1% assumption that was applied when setting the RIIO-ED1 price control.

3.39 ENWL highlighted that there are a number of upward cost drivers which are beyond the DNOs' control (such as HAs revising permit fees and changes in market rates for labour) that they have to work hard to manage, and which will be harder to manage with a 3% efficiency adjustment applied to forecast costs. ENWL also disagreed with the removal of forecast costs for traffic management plans. WPD noted that the local application of DfT street works policy makes it harder for DNOs

to achieve significant efficiencies. WPD also stated that street works arrangements are still bedding down in some areas, with a number of schemes in their infancy, making an efficiency rate of 3% "unreasonably stretching".[12]

3.40 Some DNOs considered, to varying degrees, that the efficiency adjustment should not be applied to all cost categories, saying that permit fees are beyond the DNOs' control, administration costs have already been streamlined to their most efficient level and that there are limited opportunities for DNOs to find efficiencies for permit condition costs.

3.41 A number of respondents also highlighted that our approach was inconsistent with decisions on the 2018 RIIO-GD1 street works reopener,[13] where a 3% efficiency adjustment was applied to administration costs only. WPD argued that Ofgem made selective use of precedents to apply efficiency adjustments, resulting in conflicting approaches to assessing cost categories. WPD pointed to precedent in the RIIO-ED1 slow track Final Determination for permit condition costs being justified on a case-by-case basis.

3.42 Finally, ENWL and UKPN highlighted that our approach did not take into consideration efficiencies achieved by DNOs to date. UKPN argued that DNOs are at different levels of maturity in their street works programmes and that some will have more scope than others to achieve efficiencies in the future.

Methodology for assessing forecast volumes

3.43 WPD expressed concerns with Ofgem's assessment of average permits per scheme. It requested that the forward-looking view of the average number of permit schemes should take greater account of the dynamism of the policy landscape if more HAs implement permit schemes by the end of the RIIO-ED1 period. Similarly, SSEN stated that forecasting future volumes based on the average permits issued each year should be judged on a case-by-case basis, to recognise that volumes relate to individual HAs and specific network requirements.

[12] WPD consultation response, p.28
[13] https://www.ofgem.gov.uk/publications-and-updates/decision-riio-1-price-control-reopeners-may-2018

3.44 WPD expressed concerns with Ofgem's method of assessing the reasonableness of forecast volumes, stating that our methodology overlooked its actual permit schemes in operation. WPD stated that Ofgem assessed only 13.8 permit schemes in place for EMID by the end of RIIO-ED1 while it had 17 of 21 HAs in EMID's licence area at the time of submission.

3.45 WPD said that Ofgem was wrong to state that a number of HAs in WMID's licence area are shared with other DNOs but which were included in its submission as sitting fully within WMID's licence area. WPD asserted that it only collates information on street works that have been carried out in its licence area, and would not claim street works undertaken by other utilities as its own. WPD stated that information that suggests otherwise was provided at short notice as part of further information requests.

3.46 WPD also raised concerns that Ofgem only considered overlapping DNO networks from those DNOs that submitted reopener applications and that this impacted the accuracy of our forecast volumes test. It gave the example of a HA shared by both SSEN's southern network and SWEST, stating that Ofgem assessed that 100% of this HA's network came within SWEST's licence area. WPD further noted that our calculations included one partial scheme that received ex ante funding for SSWC.

3.47 WPD states there is a lack of clarity in Ofgem's approach of applying a scaling adjustment in assessing whether a scheme is fully or partially in operation in any one regulatory year. It states that HAs which operate both notices and permit schemes should be viewed as operating a full scheme on less than the full road network. WPD also highlighted that although it applied the same approach to forecasting future volumes to each of its licensees, our assessment drew different conclusions for each. Finally, WPD requested that Ofgem apply a consistent approach to the inclusion or exclusion of HAs where the same road network resides in more than one DNO's licence area.

Other issues

Requirement for 12 months' cost data

3.48 NPg referred to the RIIO-ED1 licence and the Handbook to support its view that Ofgem should not disallow costs where the licensee does not have 12 months' cost data. It also argued that there is no requirement for a DNO to have 12 months'

cost data on its own costs and that data on street works costs from other licensees should be acceptable.

3.49 WPD was also of the view that DNOs should not be excluded from the assessment where 12 months' cost data is not yet available, stating that Ofgem should assess whether a DNO has 12 months' cost data as part of its assessment of a claim (rather than informing whether to consider the submission at all). Finally, WPD also considered that the ability to provide 12 months' cost data in the future would meet Ofgem's requirements and that licensees should not be excluded where they will be able to provide this information later within ED1.

Treatment of resubmission and additional information

3.50 Three DNOs provided additional information after submitting their Notices. In response to a supplementary question (SQ), UKPN revised its future volumes following the identification of a mistake in its original methodology. WPD provided additional information to confirm the certainty of implementation dates for three additional permit schemes to be rolled out during the RIIO-ED1 period.

3.51 Finally, as part of its SQ response, NPg provided a revised Notice with updated information and its formal consultation response included corrected information on the level of coverage of partial schemes. NPg considered that Ofgem was wrong not to accept its resubmitted Notice and to exclude the revised data from this resubmission from aspects of our minded-to position. NPg noted that at least one other licensee's resubmitted data was accepted and noted that it is good regulatory practice to use the best available data. NPg stated that its efficient costs should be assessed to ensure equal and fair treatment with other submissions.

Lane rental scheme related costs / provisions for continued uncertainty of SSWC

3.52 All DNOs requested further clarification on any logging-up arrangements that Ofgem plans to put in place to help address the continuing uncertainty of SSWC. They noted the potential lane rental scheme costs that may be incurred in the remainder of the RIIO-ED1 period.

3.53 SSEN and ENWL agreed with our approach to lane rental costs and logging-up, but sought clarity on the application of the materiality threshold and any potential amendments to the licence that may be needed. SPEN sought assurance that any mechanism put in place will treat DNOs fairly, giving all companies the opportunity

to recover an equivalent level of costs. WPD stated that any logging-up mechanism needs to be clarified, and noted that future street works activities may be affected by policy changes from DfT.

4. Our updated view

4.1 Following a review of the consultation responses, new evidence submitted and further analysis undertaken, this chapter sets out our updated view of SSWC.

4.2 As part of our consultation, we published our SSWC reopener quantitative assessment.[14] Since the consultation, we have sought an independent review of this assessment from the Government Actuary's Department (GAD). We have published its report alongside our decision.[15] Based on responses to the consultation, further follow-up questions to the DNOs, and GAD's recommendations, we have made a number of amendments to our assessment methodology; these are detailed below.

Summary of GAD's review

4.3 With regards to our overall methodology, GAD considered our approach to deriving a benchmarked unit cost and applying this to future volumes to be one that is frequently used in projecting future costs. On this basis, GAD considered this to be an appropriate method to use for these calculations. It highlighted that the validity of the method used is crucially dependent on the assumptions that underpin it.

4.4 GAD provided a number of detailed recommendations on our approach, which are summarised in Table 4.1. In this table, we also summarise our view on those recommendations.

4.5 In addition to the recommendations set out in Table 4.1, GAD made two further observations on our approach to assessing volumes.[16] Based on these observations, GAD highlighted the importance of both the consideration of any justifications provided in the DNOs' submissions and any observable trends in each DNO's data.

[14] https://www.ofgem.gov.uk/system/files/docs/2019/08/specified_street_works_costs_reopener_quantitative_assessment_150819_for.xlsx

[15] 'Ofgem – Specified Street Works Costs Reopener assessment', Government Actuary's Department (GAD) report

[16] GAD set out that if Ofgem establishes a view on the reasonable future permit volumes and subsequently derives a benchmarked unit cost, it is possible that the allowed costs could be lower than both Ofgem and the DNO had assessed as reasonable. GAD also commented that the method used to calculate volumes assumes that the future volume will be the same as the historical average. GAD highlighted that there may be reasons why a historical average may not be an appropriate assumption for the future.

Table 4.1: Summary of GAD's recommendations and Ofgem's view

Recommendation		Ofgem's view
1	Selection of data for benchmark calculation - recommend that only one source of data is used for the benchmark calculation.	We agree. We recognise that the RRP data is not currently reliable for benchmarking purposes and have now used only data provided as part of the DNOs' reopener submissions.
2	Simple vs. weighted average - recommend the use of a weighted average to calculate benchmarked average unit costs.	We agree, and we have amended our approach accordingly.
3	Splitting out component parts of costs - recommend that the benchmarking exercise is carried out for all types of cost combined.	We agree, and we now use a combined cost consisting of permit fees, permit condition costs and administration costs.
4	Allowance for variations and trends in data - recommend that in selecting the final benchmarked unit cost, Ofgem should consider any submissions from the DNOs making a case for their actual costs having varied over the data period or reasons for future variations. Also recommend that the year-on-year unit costs are reviewed to look for any trends in the base data.	We agree, and have carried out a detailed review of their submissions to identify whether WPD and NPg's costs are materially different to the DNOs that we included in our assessment of efficient costs and whether these differences are justified.
5	Calculation of number of permit schemes per DNO - recommend that if it is possible to obtain the actual percentage of each HA network covered by permits then this data should be used rather than the 50% currently used for partial schemes.	We agree, and where the data was available, we have used the actual percentage of each HA network coverage.

Our updated view

Cost categories

Permit variation costs

4.6 A number of DNOs stated that in certain circumstances it is necessary to incur permit variation costs where these are outside their control. NPg consider there is

an efficient level of permit variations and highlighted that variation costs were allowed in RIIO-GD1 reopener.

4.7 In setting a benchmarked unit cost, we have allowed for the permit variation costs incurred to date to recognise that some level of permit variations are outside the DNOs' control. However, we maintain our initial view that, in the majority of cases, permit variation costs are avoidable; we therefore expect DNOs to minimise these through improved operational efficiencies.

4.8 We do not believe that the removal of permit variation volumes while retaining permit variation costs misaligns the benchmark unit cost; this is supported by the independent GAD report, which indicates that including the permit variation volumes would further reduce the benchmarked unit costs.

One-off set up costs

4.9 SPMW's submission included forecast costs to replace its existing IT system, in anticipation of an upcoming DfT requirement. WPD noted that this is something it will need to do in the future, but given the remaining uncertainty around the date and impact of these new requirements, it did not include these costs in its submission.

4.10 As set out in Annex A of the Regulatory Instructions and Guidance (RIGs), one-off set up costs are the costs of "developing the necessary IT system to process Permit and Lane Rental applications". We have reviewed the responses to the consultation and consider that it would be appropriate to review these costs at the end of the price control, when there should be more certainty around the requirements of DfT and more comparable information on the cost of meeting these requirements should be available. We have, therefore, decided to maintain our minded-to position not to allow these costs as part of this reopener; however, we will consider these costs as part of the logging-up mechanism.

Penalty charges

4.11 NPg requested allowances for penalty costs incurred to date and penalties it expects to incur in the remainder of ED1. However, it did not provide justification explaining why each penalty was incurred or why it should be allowed. NPg asserted in its consultation response that it is efficient to incur some level of penalty charges.

4.12 We note other respondents' views that these charges are within the control of the DNO and should therefore not be allowed. We agree, and consider that these are avoidable costs and that exposure to charges of this nature are within a DNO's control. Licensees are best placed to manage this risk and should be able to plan and complete works in accordance with permits approved by the relevant HA, failing which they should be liable for any charges incurred.

4.13 There may be cases where we would exceptionally consider a claim for recovery[17] – however, there would be a high bar in respect of any such claim, which would require a robust justification in each instance where funding is sought, including why it would be in consumers' interests to bear these costs. On that limited basis, we may consider this as part of a DNO's logged-up costs.[18]

Use of a benchmark

4.14 The RIIO-ED1 Strategy Decision stipulated the requirement for 12 months of costs data to allow for benchmarking of SSWC against those of other operators.[19] It also set out our intention to benchmark one-off set up costs, additional administration costs and the impact of any permit conditions against previously assessed in electricity distribution, those submitted by other network companies at the time of the reopener and those from other industries (eg gas distribution).[20]

4.15 In the slow-track Final Determinations[21] we applied a form of benchmarking to lane rental costs. We acknowledge that the Strategy Decision and Final Determinations do not provide a consistent view on the use of benchmarking.

4.16 However, we believe that benchmarking remains the most effective tool for establishing a view of efficient costs, not least because there is a greater level of data available than there was at the beginning of the ED1 price control.

4.17 In our submissions, we require sufficient justification of forecast costs. We expect that at this point in the price control, DNOs should be able to obtain confirmation

[17] For the avoidance of doubt, this does not extend to penalties or fines for criminal offences.
[18] This has not been demonstrated on the basis of the information provided by NPg.
[19] Strategy decision for the RIIO-ED1 electricity distribution price control: Uncertainty mechanisms, para 3.17
[20] Ibid. para 3.21
[21] https://www.ofgem.gov.uk/sites/default/files/docs/2014/11/riio-ed1_final_determination_expenditure_assessment_0.pdf

from relevant HAs that future schemes will be implemented in their licence areas by 2022, if HAs have sufficient certainty of this.

4.18 We acknowledge that there are factors that may compel HAs to implement permit schemes in the remainder of ED1, such as a letter from the Secretary of State for Transport and the DfT requirement for HAs to implement a new street works related software system in the near future. However, we consider this alone does not provide sufficient certainty to justify significant forecast costs as not all HAs will require the operation of permit schemes for their road networks in the remainder of the ED1 period. In addition, there is insufficient certainty over whether there will be full or partial coverage of permit schemes in the remainder of the ED1 period.

Methodology used for establishing a benchmark

4.19 Some DNOs questioned the data that should be used to establish a benchmark,[22] whether that related to data submitted by DNOs in this reopener or RRPs from a wider spectrum of network companies. Similarly, WPD and NPg disagreed with the exclusion of their data from the benchmarking and ENWL proposed statistical techniques that could be used to select the relevant data.

4.20 As part of our approach to establishing a benchmark in our initial assessment, we did not include the RRP data of those licensees who did not submit a reopener application as these were not consistent with the data provided in the submissions.

4.21 One recommendation from GAD[23] was to use only the identified unit costs from the reopener submissions for ENWL, SPMW and EPN, rather than also including data from their RRPs; WPD also suggested this in their consultation response. We agree with this approach.

4.22 GAD and ENWL also recommended deriving the benchmarked unit cost based using a weighted average instead of a simple average and ENWL suggested using statistical techniques to exclude clear outliers.[24] We agree; these changes have increased the benchmarked unit cost from £139 per issued permit to £143.

[22] We have no reason to believe that DNOs' submissions included avoidable street works costs or those that are recoverable from third parties. For the avoidance of doubt, these costs are not eligible SSWC.
[23] 'Ofgem – Specified Street Works Costs Reopener assessment', Government Actuary's Department (GAD) report
[24] Using this approach highlighted that WPD and NPg's data should not be included in the benchmark.

Treatment of variation from benchmarked costs

4.23 Following responses to the consultation and the GAD review, we have carried out further work to understand whether it can be shown that some DNOs experience materially higher costs in some HA networks than others. We have also sought to understand whether these materially higher costs should be considered separately from the benchmark exercise.

4.24 In reviewing whether there are material and justified differences between DNOs, we looked in detail at the costs associated with the removal of surplus material[25] provided in ENWL and WPD's submissions. Based on the evidence provided in the submissions and in response to SQs, we consider that the additional cost of this activity for WPD is driven by underlying assumptions that have not been sufficiently justified. These assumptions include the number of days per permit on which surplus material is removed and the average amount of time per day spent removing this material. We provide further detail in Appendix 3.

4.25 We have also looked at administration costs to understand whether there is justification for why WPD's costs are higher than the Ofgem benchmark. We note that WPD uses the same assumptions across its three licensees that submitted a SSWC reopener application, but have not sufficiently explained why these assumptions justify the difference from the benchmarked unit cost. We have therefore applied our benchmark to WPD's administration costs.

4.26 Following its consultation response, we requested further information on ENWL's forecast costs for traffic management plans. We consider that it is not a new requirement that street works require multi-way temporary traffic signals, or road/lane closures, and that this would require an element of planning irrespective of whether this is a formal or informal requirement. ENWL provided a breakdown of the volume of its permits to date that required a traffic management plan. We have adjusted its claim by the annual average of these volumes using ENWL's forecast unit cost, and applied a 3% annual efficiency adjustment to this.

4.27 We note that DNOs may have limited scope to influence where work is undertaken on their network, and that HAs may charge permit fees that are not aligned with the benchmarked unit costs. However, we believe that setting a benchmark based on an average, followed by a qualitative assessment of the justification for

[25] For WPD this makes up around 60% of its requested permit condition costs.

deviations from this benchmark, allows us to set allowances that cover the range of scenarios DNOs may encounter.

Efficiency adjustment

4.28 We have considered the points raised in the consultation responses in relation to the application of an efficiency adjustment. We have decided to maintain our minded-to view to apply a 3% annual efficiency adjustment to all cost categories for the last four years of the RIIO-ED1 price control.

4.29 We applied a 1% efficiency adjustment at the start of the price control in recognition that systems and processes were in the process of being embedded as early permit schemes were established.

4.30 We note that, in the RIIO-GD1 reopeners, efficiency adjustments have been applied differently in different circumstances. In the 2015 RIIO-GD1 street works reopener, we applied a 3% efficiency adjustment across all cost categories;[26] in the 2018 RIIO-GD1 street works reopener, we applied a 3% efficiency adjustment to administration costs only.[27] Both of these applications reflect our expectation that efficiencies should be achievable as street works activities become business-as-usual.

4.31 We consider street works to be an area that is sufficiently established such that DNOs are familiar with the ways of working and can drive efficiencies, but not so established to mean efficiencies cannot be achieved. As such, we believe DNOs have the scope and ability to deliver greater efficiencies than the 1% adjustment applied at the start of the price control. Some DNOs' consultation responses highlighted the efficiencies they have achieved in street works to date, and we expect them to continue to drive these efficiencies over the remainder of the price control.

4.32 As highlighted in our consultation, we consider that DNOs can gain efficiencies over time. This can be done by (among other actions): adopting better and more collaborative ways of working; adopting innovative solutions where possible and taking advantage of any available permit scheme discounts.

[26] https://www.ofgem.gov.uk/sites/default/files/docs/2015/09/150929_-_determination-_riio_gd1_review_streetworks_costs_0.pdf
[27] https://www.ofgem.gov.uk/system/files/docs/2018/09/specified_street_works_costs_decision.pdf

4.33 We believe DNOs can achieve these efficiencies through either the volume or unit cost element of the total cost allowance; however, we do not consider it appropriate to specify where DNOs should target these efficiencies. We therefore maintain our approach to apply the efficiency adjustment to the total costs for each category.

Methodology to assess volumes

4.34 In light of consultation responses, we have reviewed our approach to assessing DNOs' submitted permit volumes. We maintain the view that using a historical average as a basis for forecasting volumes is because there remains uncertainty around the future volume of work that will be required; we have considered all available information provided by DNOs in setting forecast volumes.

4.35 In relation to partial schemes, WPD raised concerns that we did not review coverage of overlapping HA permit schemes from DNOs that did not submit applications in this reopener, and that we assessed that one HA came fully within SWEST's network when it is in fact shared with SSEN. Our subsequent review acknowledges this. WPD also noted that a partial scheme that received ex ante funding was included in our initial assessment of their volumes. We reviewed this and confirm that no DNO has been adversely affected by this.

4.36 We have looked at each licensee in turn, and used new information where sufficient justification was provided. We have:

- used NPg's view on partial schemes. We had used an assumption of 50% coverage for any HA that operated a partial scheme. NPg provided its view for each of the 10 HAs that had operated partial schemes, with its assumption ranging from 5-32%.[28, 29] We also took this into account for EMID, which had six HAs that had, at some time in the first four years of ED1, operated partial schemes
- used EPN's updated volumes. UKPN further revised its forecast permit volumes in response to the consultation. We accept that these revised volumes (72,394) are consistent with EPN's actuals to date and have taken these into account in our decision

[28] We also corrected an error on the NPgN tab – this is set out in the changes log of Appendix 1
[29] This increased our assessed view of NPgN's permit volumes to 67,936

- accepted that three HAs in WMID's licence area and three in EMID's licence area that we had excluded due to uncertainty on whether they would introduce a permit scheme, are now likely to introduce permit schemes before the end of RIIO-ED1. This is based on further evidence submitted by WPD of a planned implementation date for these HAs.

4.37 We have also considered whether it was appropriate to use each DNO's submitted volumes or our assessed reasonable forecast volumes, where these are lower. Our assessment is provided in Table 4.2. DNOs will have the opportunity to log up additional costs for HAs that have not been funded through this reopener.

Table 4.2: Rationale for assessed reasonable permit volumes

Licensee	Volumes used	Reason
ENWL	DNO submitted volumes	Submitted volumes are lower than our assessed volumes. At the time of submitting its reopener application, it had 17 of the forecast 18 HAs operating a permit scheme.
NPgN	Ofgem assessed volumes	We do not accept its forecast volumes, and have used our assessed volumes. Of the 17 HAs that NPg has forecast to be operating a permit scheme by the end of RIIO-ED1, only two were in operation at the time of its submission in May 2019.
NPgY	DNO submitted volumes	Currently, 13 HAs operate a permit scheme (forecast to increase to 18 by the end of RIIO-ED1). Supplementary information provided in respect of partial schemes shows that NPgY's forecasts are in line with our expectations. We recognise that our initial assessment did not fully account for the impact of partial schemes in place, and that NPgY's forecasts are more appropriate.
SPMW	Ofgem assessed volumes	While SPMW is not forecasting any additional HAs to introduce a permit scheme; its forecast volumes are based only on the volumes experienced for a single year. We consider an average of the first four years is more appropriate.
EPN	DNO submitted volumes	EPN is not forecasting any additional HAs introducing permit schemes, and its (updated) forecast volumes are lower than our assessed volumes.
WMID	Ofgem assessed volumes	Only seven of 18 HAs currently have a permit scheme in operation. In response to the consultation and to SQs, WPD provided greater certainty that three HAs (included in the 18) would implement a permit scheme in 2020. We have included these HAs in our assessment, but do not consider sufficient evidence has been provided to justify using WMID's total submitted volumes.

EMID	DNO submitted volumes	17 HAs are currently operating a permit scheme, and a further four are expected to introduce them by the end of RIIO-ED1. Our initial assessment calculated a total of 13.8 permit schemes, after removing four permit schemes, for which there was insufficient certainty of implementation. Following the consultation, WPD provided greater certainty that three of those four HAs will introduce permit schemes by the end of the ED1 period. We have also tested the impact for EMID's partial schemes based on the average percentage of NPgY's partial schemes to ensure they were not disadvantaged.
SWEST	Ofgem assessed volumes	As there are no HAs that currently operate permit schemes in this licence area and no actual costs data, there is insufficient justification for the 10 HAs that are forecast to introduce a permit scheme.

Other points

Treatment of resubmission and additional information

4.38 In its submission, NPg did not provide sufficient justification for the costs it anticipated it would incur for permit conditions and administration. It stated that it had not captured the costs incurred over the first four years of RIIO-ED1 and therefore provided estimates. It also stated that it may have omitted significant permit condition and administration costs from its submission. This made it difficult to establish whether NPg's submitted costs had been incurred efficiently as well as difficult to establish whether these costs were an appropriate basis on which to forecast future costs. For these reasons, we did not include NPg's submitted permit condition and administration costs in our benchmark and we did not allocate costs to NPg for these categories.[30]

4.39 In its response to the consultation, NPg noted that it will incur permit condition and administration costs where it incurs permit fees, and stated that Ofgem should use our benchmark to allocate costs for these costs. We accept that all DNOs, including NPg, will incur permit condition and administration costs where they incur permit fee costs.

[30] We did not include NPg's permit fee costs in our benchmark for two principal reasons: (i) the variation in NPg's costs both between years and between its own and other licensees; and (ii) its data was a significant outlier. For these reasons, we also did not include WPD in our benchmark.

4.40 We sought further detail through the SQ process after the consultation closed, in order to establish how NPg arrived at its cost estimates. This included requesting the formula and underlying assumptions used for estimating these costs.

4.41 After reviewing NPg's response to our consultation and SQs, we have considered its revised data and conducted a separate assessment, which was a recommendation provided in the GAD review.[31]

4.42 For NPg's historic costs (ie the first four years of the price control), we took the lower of NPg's weighted average unit cost and our benchmarked unit cost. For forecast costs (the final four years of the price control), we considered two options. The first option included using the same unit cost as for the first four years, and applying a 3% annual efficiency adjustment. The second option would use NPg's forecast weighted unit cost for the final four years, (applying the 3% efficiency adjustment to the total forecast costs).[32] For both options, we would use the updated permit volumes data based on the information provided by NPg in its consultation response. For both options, we would deduct NPg's penalty charges from its permit fees so this is excluded before deriving a unit cost. We considered the second option to be more appropriate. The first option would use the lower, by component part, of NPg's submitted costs and Ofgem's benchmarked costs which (as highlighted by GAD's report) could be seen as being selective. We therefore chose the second option.

4.43 We compared NPg's total costs (both actual and forecast) to our benchmark. Since these costs were lower than our benchmarked view, we accepted these costs.

Lane rental scheme related costs / provisions for continued uncertainty of SSWC

4.44 Following a review of consultation responses, we maintain our view that additional funding requested for future lane rental scheme related costs are not eligible for consideration under this reopener, since WPD and SPEN were unable to meet the requirement for 12 months of lane rental costs data.[33]

4.45 Further, no application for lane rental costs was able to provide certainty that lane rental schemes will be implemented by 2022. As these are voluntary schemes that

[31] GAD's review also agreed with the exclusion of NPg when establishing our benchmark and from applying the benchmark to its costs.
[32] We derived a weighted average unit cost by obtaining an aggregate of the actual or forecast total costs for each cost category and dividing this aggregate cost by the total volumes in the first four years.
[33] ENWL, NPg and UKPN did not include lane rental costs in their submissions.

HAs are not required to implement, there is currently insufficient evidence to justify these forecast costs. However, should SSWC (which includes lane rental costs) which have not been funded through an ex ante allowance or through this reopener be incurred by DNOs, these can by logged-up and will be considered under the log-up mechanism. Further detail on the log-up mechanism is in Appendix 2.

4.46 Finally, we note that WPD's licences do not currently provide for the recovery of lane rental costs. This appears to have been an oversight and, following this decision, we intend to consult on modifications to CRC 3F.25 in WPD's licences to include these costs in the definition of SSWC.

Requirement for 12 months' costs data

4.47 The RIIO-ED1 Strategy Decision sets out that, in order to be able to benchmark additional SSWC at the reopener, we would require at least 12 months' costs data.[34, 35] In addition, CRC 3F is to be read and construed in accordance with, among other things, the Handbook. One of the requirements in the Handbook is that the licensee "has provided, or will be able to provide, 12 months' worth of cost data to support its proposal".[36]

4.48 We have therefore not considered costs where a DNO has been unable to provide 12 months' cost data (for actual costs incurred).

[34] Paragraph 3.17 of https://www.ofgem.gov.uk/sites/default/files/docs/2013/02/riioed1decuncertaintymechanisms_0.pdf
[35] For the avoidance of doubt, we consider that the DNO should provide 12 months of its own cost data.
[36] Please see 7.40 (ii) b. and c. of ED1 Price Control Financial Handbook (slow track): https://www.ofgem.gov.uk/system/files/docs/2017/08/ed1_handbook_v3_slowtrack_0.pdf; and 7.42 (ii) b. and c. of the ED1 Price Control Financial Handbook (fast track): https://www.ofgem.gov.uk/system/files/docs/2017/08/ed1_handboook_v4_fasttrack_0.pdf

5. Our decision

Our decision:

5.1 Table 5.1 sets out our decision for the SSWC reopener and explains the changes from our minded-to position.

Table 5.1: SSWC decision and change from minded-to position (£m, 2012-13 prices, rounded to one decimal place)

	Funding Requested	Consultation			Decision		
		Ofgem assessed efficient costs	Materiality threshold	Proposed allowance	Ofgem assessed efficient costs (updated)	Funding allowed	Change from consultation
ENWL[1]	10.3	9.2	6.2	9.0	9.7	**9.7**	0.7
NPgN[2]	5.2	-	4.5	-	4.2	**-**	-
NPgY[2]	9.3	-	5.9	-	8.9	**8.9**	8.9
SPMW	21.3	8.0	5.8	8.0	8.2	**8.2**	0.2
EPN	10.2	9.3	9.7	-	9.9	**9.9**	9.9
WMID	24.5	3.8	5.7	-	4.6	**-**	-
EMID	20.7	7.6	5.7	7.6	7.9	**7.9**	0.3
SWEST	11.0	-	4.2	-	-	**-**	-
Total	**112.5**	**38.0**		**24.6**	**53.5**	**44.7**	**20.1**

[1] Our assessed efficient costs at consultation produced a value based on volumes and unit costs, but the proposed allowance was capped at the level of funding requested by each DNO (after excluding lane rental costs). See paragraphs 2.11 and 3.2 in the consultation.

[2] NPg's funding request is based on its May 2019 reopener submission. In response to SQs, NPg identified errors in its submission and provided additional information that allowed us to disaggregate its data to produce specific unit costs. We have considered this additional information in our assessment.

5.2 Table 5.2 sets out the revised Price Control Financial Model (PCFM) values for SSWC, which will be directed by 30 November 2019. This means that adjustments to DNOs' allowed revenues will take place from 2020-21.

Table 5.2: Revised Allowed Expenditure - Specified Street Works Costs - CRF 3F - UCSSW (£m, 12/13 prices rounded to one decimal place)[37] – Inputs into PCFM

	2016	2017	2018	2019	2020	2021	2022	2023
ENWL	1.1	1.0	1.3	1.4	1.2	1.3	1.2	1.2
NPgN	-	-	-	-	-	-	-	-
NPgY	0.7	0.7	0.6	0.8	1.1	1.7	1.7	1.6
SPMW	1.2	0.7	0.7	1.1	1.2	1.1	1.1	1.1
EPN	1.1	1.2	1.3	1.5	1.3	1.3	1.2	1.2
WMID	-	-	-	-	-	-	-	-
EMID	0.4	0.6	0.9	1.2	1.1	1.2	1.2	1.2
SWEST	-	-	-	-	-	-	-	-

[37] Where, for each licensee, the total of the annual values in Table 5.2 does not match with the funding allowed in Table 5.1, this is due to rounding. For input into the PCFM as part of the 2019 Annual Iteration Process (AIP), DNOs should use the tab 'Input into PDCFM' in Appendix 1.

Appendices

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Appendix 1

Supplementary supporting analysis file to RIIO-ED1 Reopener Decision - Specified Street Works Costs

https://www.ofgem.gov.uk/system/files/docs/2019/10/supporting_analysis_file_to_ssw_costs_-_for_decision.xlsx

Appendix 2

Logging-up of SSWC for the remainder of RIIO-ED1

Introduction

A2.1. Some respondents requested clarity on the position regarding logging-up of SSWC.

A2.2. At the end of RIIO-ED1, we will consider submissions by licensees for logged-up SSWC and, subject to consultation[38] and review by us, determine any revision to the RIIO-ED2 Price Control Financial Model (PCFM). By logged-up costs, we mean those costs which have been incurred by the licensee during the RIIO-ED1 period, but which were not included in the licensee's ex ante allowance or were not allowed as part of the SSWC reopener. Our view on how we intend to consider logged-up SSWC is set out below.

Logging-up of SSWC

A2.3. DNOs will be able to log up SSWC and apply for funding for these costs at the end of RIIO-ED1. As set out in the ED1 Strategy Decision,[39] any logged-up SSWC will be assessed on the same basis as the May 2019 reopener; therefore, the same requirements as set out in CRC 3F and the RIIO-ED1 Price Control Financial Handbook will apply.

A2.4. An overall materiality threshold applies in respect of relevant adjustments for SSWC. The materiality threshold for each licensee, in 2012/13 prices, is specified in the table in Appendix 3 to CRC 3F. Those licensees who submitted a request under the May 2019 SSWC reopener and have, after our efficiency assessment, passed the materiality threshold in CRC 3F will not be required to pass the materiality threshold a second time. Those licensees who have not passed the materiality threshold after our efficiency assessment, or who have not submitted an application under the May 2019 SSWC reopener, will be required to pass the materiality threshold for any logged-up costs to be allowed.

[38]Consultation refers to both a consultation on any legacy adjustments as part of the RIIO-ED2 price control and a separate consultation on our minded-to position following review of any claim made by a DNO for logged-up SSWC.
[39] Para 3.18 of the Strategy decision for the RIIO-ED1 electricity distribution price control: Uncertainty mechanisms

A2.5. We understand that in the remainder of the RIIO-ED1 period, lane rental schemes may be implemented in areas where permit schemes are currently, or are expected to be, in operation. Any adjustments for logged-up costs will take account of any ex ante allowance or funding through the reopener, to ensure licensees are not funded twice for the same activities.

A2.6. All licensees will need to provide sufficient justification for those costs that are included as part of a submission for logged-up SSWC. We expect that, where a licensee has received an allowance through the SSWC reopener, any logged-up costs it may have will be based on a unit cost that is no greater than the unit cost allowed through the SSWC reopener. Any unit costs above this level will need to be justified and robustly evidenced.

Reporting in the RRPs

A2.7. We intend to modify the RIGs to require DNOs to report logged-up SSWC in their RRPs. The reporting in the RRPs should be used by the DNOs to support and reconcile with any logged-up SSWC submission.

Submissions for logged-up SSWC

A2.8. We intend to work with stakeholders to establish the process for submitting applications for logged-up SSWC.

Appendix 3

Treatment of variation from benchmarked costs - additional detail

A3.1. To establish whether WPD had sufficiently justified the differences between its costs and our benchmark, we looked further at the assumptions it used. In particular, we looked at WPD's costs for materials and storage, which make up around 60% of its permit condition costs, and cover the removal of surplus materials, plant or spoil (NCT04A). We compared its assumptions with those of ENWL, since ENWL had robust, comparable data in the same format as WPD.

A3.2. Both WPD and ENWL base their claim for NCT04A on (the average number of days on which surplus materials, plant or spoil is removed) X (unit cost) X (percentage of permits with conditions). The unit cost is derived using (the average hours removing surplus materials, plant or spoil) X (the hourly cost of removal).

A3.3. WPD's claim relied on a unit cost of £266 in 2018-19 for NCT04A. This unit cost is explained as "the standard contract unit cost of two operatives and a grab wagon". This is based on an average (across all HAs and its three licensees) of 2.5 hours per visit to remove surplus materials. For comparison, ENWL assumed an average of two hours.

Average hours removing surplus materials, plant or spoil

A3.4. Following our consultation, we asked WPD to provide further justification for its 2.5 hour assumption; in response, it provided data based on a contractor's timesheet during April 2019. We identified several issues with the underlying data, such as duplicate entries for the same work and the omission of all work for one week. WPD confirmed that, once these issues had been removed, the average was closer to ENWL's assumption of two hours.

A3.5. We consider that two hours is an appropriate assumption for the removal of surplus materials, plant or spoil. We do not believe that WPD has sufficiently demonstrated that it takes WPD a materially longer time to remove surplus materials, plant or spoil in its licence areas.

Average number of days removing materials, plant or spoil

A3.6. We also compared the average number of days removing surplus materials, plant or spoil per issued permit, where a NCT04A permit condition applied, as provided by WPD and ENWL:

- WPD claimed an average of 8.4 days per permit, half of which would include a visit to remove surplus materials, giving an average of 4.2 visits per issued permit;

- ENWL's weighted average was 1.8 visits per issued permit. It identified three different average number of days per issued permit: two relate to the north (four days) and south (five days) of its licence area; the third is for a contractor (16 days). ENWL assumed that removal of surplus materials, plant or spoil takes place based on the average number of days, less three days (for contractors, it is less two days). For example, in the south of its licence area, the removal of surplus materials takes place on two days. While we consider the number of days a contractor removes surplus materials appears high, the number of permits relating to contractor work only makes up around 3% of ENWL's sample.

A3.7. In its response to the consultation, WPD included 14 case studies to further justify its claim for permit condition costs. Of these 14 case studies, only four have a condition that requires the removal of surplus materials (NCT04A), with the total duration for each of these four permits being four or five days (compared with the 8.4 days claimed).

A3.8. WPD's justification for the average permit duration of 8.4 days is that: the 14 case studies provided represent a small sample size; the mix of work currently being undertaken by ENWL may be different to WPD; and, DNOs may have different ways of working, different operational and technical models, and the length of a visit may differ depending on the technique used by each DNO.

A3.9. We acknowledge that there will be a different mix of work for each claim. However, DNOs' submissions rely on four years of actual data and we therefore expect the mix to be broadly similar across DNOs over that period. We also acknowledge that DNOs work differently and there are different techniques for removing surplus materials, plant or spoil. However, we would expect DNOs to adopt the most efficient approach, including the amount of time the DNO occupies the road.

A3.10. We have applied assumptions similar to those used by ENWL to WPD's claim. This gives an average of two hours for the removal of surplus material on an average of 2.25 days per permit (instead of 2.5 hours on 4.2 days). This gives a unit cost for permit conditions that is broadly consistent with our benchmarked unit cost.

NCT11A

A3.11. Another component of WPD's permit condition costs is its costs for 'consultation and publicity'; this makes up around 12% of its permit condition costs. For WPD, this relates to 'additional visits to site to display the permit reference number' (permit condition code NCT11A).

A3.12. We have compared WPD's 'consultation and publicity' costs with ENWL's. For the same activity, we have found that WPD used an average unit cost per permit (where NCT11A applies) of over £18, compared to around £1.20 for ENWL. Additionally, in calculating its consultation and publicity costs, WPD used separate annual contract rates for each of its three licensees that are materially different to one another - a 23% difference between the lowest and highest rate. No justification was provided to explain these variations in contractor rates.