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12 January 2016

Dear Mick

Consultation on a potential RIIO-T1 and GD1 mid-period review

Thank you for the opportunity to respond to your consultation that sets out Ofgem's initial views on a potential RIIO-T1 and RIIO-GD1 mid-period review (MPR).

As a Gas Distribution Network (GDN) company, we have decided to only respond to this consultation in the context of the need for a mid-period review for RIIO-GD1. We therefore only provide responses to the questions raised in the consultation under Chapters 1, 4 & 5.

In summary, we agree with Ofgem's assessment that a MPR is not required in respect of RIIO-GD1. This is because we believe RIIO-GD1 is delivering outputs that our stakeholders require, and because there has been no change in government policy or consumer expectations that would warrant a change in outputs since the commencement of the RIIO-GD1 Final Proposals in April 2013.

We agree with Ofgem's view that the MPR should not result in two four year price control periods, as such an approach will result in undermining GDN investment strategies and investor confidence.

Our detailed responses to the questions raised in your consultation are provided below for your reference under each chapter heading.

## CHAPTER 1

Question 1 – Do you have any views on the additional clarity we have provided on the RIIO-T1 and RIIO-GD1 MPR scope?

The RIIO-GD1 price control framework is delivering meaningful outputs for our customers and is incentivising GDNs to deliver these efficiently through an increased application of innovative techniques such as the Robotics Network Innovation Competition (NIC) project.

We do not consider there has been any change in government policy or consumer expectations that would warrant a change in outputs since the setting of these at the outset of the RIIO price control framework. We therefore do not consider there are any new or material issues that should be considered under the terms for a MPR that were clearly stipulated within the RIIO-GD1 Final Proposals.

It is very important to recognise that an underlying principle of the RIIO framework is to provide longer term certainty in the setting of stakeholder driven outputs and the allowances for GDNs to achieve these. This underpins investor confidence in the ability of GDNs to deliver outputs, and changes should only be considered where there is a clear and logical rationale to do so.

We wholeheartedly agree with Ofgem's view that the MPR should not be used to address any performance issues and/or effectively result in two four year price control periods. Such an approach will result in undermining GDN investment strategies and investor confidence that could ultimately have adverse effects on customers as a result of increases to the cost of capital. Future decisions on such matters should be reserved for future price control resets.

Question 2 – Do you consider the issues we have identified for RIIO-T1 and RIIO-GD1 in this consultation fall within this scope?

Yes we agree with Ofgem's assessment for there to be no MPR in respect of RIIO-GD1.

Question 3 – Are there any other issues within the defined scope that we have not included when assessing the need for an MPR for RIIO-T1 and RIIO-GD1?

No. We are not aware of any further issues that need to be considered for an MPR in respect of the RIIO-GD1 price control framework.

## CHAPTER 4

Question 17 – Based on our current assessment we have not identified any material issues for RIIO-GD1 which we think require further examination through an MPR. Do you agree with this assessment?

We agree with Ofgem's assessment that there are no additional material issues requiring further attention through a MPR process.

Question 18 – Do you agree with our current assessment that there is no need to review the risk reduction output associated with the iron mains risk reduction programme, as part of a MPR?

Yes we agree that a review of the risk reduction output is not required as part of a MPR.

We consider the RIIO-GD1 IMRRP is already driving a noticeable improvement in iron mains risk reduction across our networks. This is leading to safer gas networks and is assisting in reducing gas transportation losses without the need for a review of the Pipeline Safety (Amendment) Regulations 1996 (PSRs).

Question 19 – Do you agree with our current assessment that we do not need to review the asset health and risk secondary deliverable as part of a MPR?

Yes we agree that a review of the asset health and risk secondary deliverable is not required as part of a MPR.

As noted in the consultation paper, Ofgem is aware of the ongoing work to develop a comprehensive Network Output Methodology and reporting requirements through the GDN Safety and Reliability Working Group that will fully satisfy the relevant licence conditions. We look forward to continuing this work with the other GDNs and Ofgem over the coming months.

At this time, we do not consider that we have any further asset health data to support an increase in our allowed expenditure. We therefore do not consider a further review can be included as part of the MPR process.

## CHAPTER 5

Question 20 – Do you agree that we should clarify some areas where it isn't clear how late or non-delivery will be treated? If so, which areas do you consider would benefit from such clarification?

Yes we consider further clarification would be useful in the following areas:

### Assessment Periods for Output Delivery

RIIO-GD1 provides for different assessment periods across the required outputs and secondary deliverables. For instance, the RIIO-GD1 Final Proposal states that many outputs are assessed on an annual basis whereas others, such as gas holder decommissioning, are assessed at the end of the price control period. However, we believe there is an increased tendency for stakeholders to assess progress against each of the primary outputs and secondary deliverables on an annual basis. This can create the perception that a GDN is not achieving a primary output or secondary deliverable, when in fact this is not the case as the actual assessment period does not close until the end of RIIO-GD1 in March 2021.

We therefore consider it would be helpful for Ofgem to clarify, for the avoidance of doubt, the assessment periods for all primary outputs and secondary deliverables that are to be measured only at the end of the current RIIO-GD1 price control period. We do not consider that any of the primary outputs or secondary deliverables for RIIO-GD1 need to be amended, but further clarification on this point would be useful. This clarification could be provided in Ofgem's future annual reports of GDN performance.

### Delivery of Outputs

We consider it would be helpful for Ofgem to clarify further how any under and over delivery of outputs will be treated under RIIO-GD1. While we fully understand the importance to customers of delivering all primary outputs and secondary deliverables, the Final Proposals indicate that Ofgem has discretion to penalise or reward under/over performance by as much as 2.5%.<sup>1</sup> It would therefore be useful for Ofgem to elaborate further on how this may work in practice for each output category.

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<sup>1</sup> "RIIO-GD1 Final Proposals – Supporting Document – Outputs, Incentives and Innovation", Ofgem, 17 December 2012; paragraph 7.31; page 51

For example, this principle has recently been applied to the resetting of GDN fuel poor connection targets which are easy to measure, both in terms of connection numbers and totex allowances. However, it is not clear to us how this may be applied in other areas such as interruptions definitions, where the direct impact on totex performance is much harder to accurately quantify. This clarification could also be provided in Ofgem's future annual reports of GDN performance.

Question 21 – How material do you consider innovation tax relief has been and is likely to be for the network companies? Do you consider this is an issue that we need to pursue as part of any MPR? We request that the network companies provide estimates of the benefits accrued so far due to this tax relief as part of their responses.

We do not consider this is an issue that needs to be pursued as part of a MPR.

Our forecasts suggest the eligible costs in relation to research and development in RIIO-GD1 will result in a relatively minor cash tax benefit, and therefore we do not regard this as a material area.

Should you require any further information with regards to our response then please do not hesitate contacting me at [paul.mitchell@sgn.co.uk](mailto:paul.mitchell@sgn.co.uk) or on 07584 011046.

Yours sincerely,

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Regulation Manager