

# RIIO-2 Draft Determination

## NGN CEG Response

NB: Throughout this document, where we use the phrase ‘no comment’ this is because we do not wish to make a specific response to that question.

### Core Document

#### 1 Draft determination at a Glance – Introduction. Summary of NGN CEG response

##### Net Zero

The CEG agree that the goal of this regulation framework should be to deliver Net Zero at lowest cost to customers whilst maintaining world class levels of system reliability. However, Net Zero is not an off-the-shelf cost. It’s a pre-emptive measure for mitigation and resilience against climate emergency and greater investment in energy networks will be essential over RIIO-2 and beyond.

##### Reduced revenue

Ofgem acknowledges that investment will need to rise over the next decade and we agree that the companies will need to be efficient to ensure all investment is in current and future customers’ interests. We are therefore concerned that some of NGN’s proposed investment to ensure resilience and reduce environmental impacts has not been accepted at draft determination stage, (in particular its Repex programme) despite CBA evidence provided to the CEG that this is cost effective within RIIO2 and positive customer acceptability testing. We deal with individual decisions/positions as we comment on the specific consultation questions in this and document annexes (GD Sector and NGN).

##### Uncertainty Mechanisms

The greater use of reopeners within Uncertainty Mechanisms (UMs) appears to be a shift from the original SSMD guidance. Through the development of the Business Plan we encouraged NGN to fully justify all baseline costs to avoid additional costs being added at a later stage unless there was very good reason. We are therefore concerned that a significant amount of GDN costs should be subject to re-openers and query whether this could lead to less efficient management and investment decisions.

Clearly there are a number of areas where Government policy is not fixed but the companies should be encouraged to take a greater leadership role in developing pathways to Net Zero where possible: meeting societal expectations, responding to stakeholder feedback and contributing to major international agreements on climate change. We are also concerned about Ofgem’s ability to process reopeners/UMs without

significant additional resources and the delays to programmes that will result. We would wish to be reassured that there is capacity in place and processes will be streamlined.

We believe that Ofgem should highlight at the Open Meetings how the initial energy bill reduction of on average £20 per customer a year would be affected if the GDN proposals were accepted in full and highlight the impact on each individual GDN regions' bills. This would allow stakeholders to understand trade-offs being made on their behalf by Ofgem.

### Innovation

The CEG and NGN stakeholders support the need for greater innovation, and we note that all funding will be subject to a satisfactory reporting framework. We agree that it is essential to capture and share lessons learned across the sector and therefore urge the companies and Ofgem to work speedily to allow NIA and SIF proposals to come forward early in RIIO2. Embedding innovation beyond research and trial phase should become more visible along with customer impacts.

### Customer Service Standards and Vulnerable Customers

We support Ofgem setting some common higher quality of service targets, particularly as this aims to improve services to customers, but we had expected a greater number of bespoke outputs to be accepted where customer testing was positive, and these added nothing or little to costs. In particular we believe that more of the vulnerable customer bespoke outputs could have been accepted. Whilst NGN have told us that they remain committed in principle to the higher levels of standards they proposed in bespoke outputs, we remain concerned as to how this may be achieved with lower levels of revenue and fewer performance incentives. We do recognise, however, NGN's drive to complete as much as possible by way of training, refining processes, preparing for external awards, etc. in RIIO-1 to enable it to be best placed to deliver its ambitions for RIIO-2.

We also note that Ofgem was unable to take into account the impact of COVID 19 at draft determination stage. We urge Ofgem to review their decisions on outputs designed to help vulnerable customers following further stakeholder input and insights, to ensure any proposals by the companies remain valid and will meet those customers' needs in the short and longer term.

### Finance

We have not responded to the sections on Finance as this is outside our scope. However, we make two points

- we agree that a better balance between returns to shareholders and customer bills than resulted in RIIO 1 should remain a prime driver;
- we need to ensure that any short-term bill reductions that Ofgem is seeking do not lead to longer term costs for future customers and a reduction in outcomes relating to safety, reliability customer service and environmental impact.

### Efficiency

We welcome Ofgem's assessment of additional efficiency gains and where companies can outperform their original proposals. We are, however, very keen to ensure that this will not impact customer service standards, particularly where these are proposed as

internal stretch KPIs and not LOs/ incentives. By reducing income, Ofgem is seeking significant efficiencies yet some of the major propositions in the DD – especially around shunting a huge proportion of business into UMs - appear incredibly bureaucratically intensive, and potentially expensive. The net result may potentially be to reduce overall savings or impact efficiency

### Stakeholder Engagement

We welcome the emphasis on customer and stakeholder engagement in RIIO-2 and were pleased to see that Ofgem upped the ante on its expectations from companies. We support Ofgem's proposal that high-quality stakeholder engagement should be part of BAU in RIIO2 and that GDNs should report on this directly to stakeholders. However, we are concerned that Ofgem has not fully considered what NGN's customers have told them about the Company's business plan proposals – or at least Ofgem has not demonstrated evidence of regional stakeholder views in their DD documents.

We believe that NGN responded positively taking a well-reasoned, thorough and pragmatic approach to stakeholder engagement that is now becoming embedded throughout the company's decision-making processes.

We note that NGN's business planning research highlighted that its customers wanted the Company to strike the right balance between a high-quality and environmentally friendly service and affordable bills. Particularly, they wanted:

- safety and reliability to be a key priority (with no compromise on safety)
- a reduced carbon footprint and action to limit impacts on the environment
- NGN to use its reach and resources to support struggling communities and customers (but without doing the job of agencies with statutory duties or voluntary groups better placed to deliver) given that its area covers some of the most deprived places in the country
- NGN to deliver value for money across all areas of its work

Given that Business Plan acceptability testing with stakeholders was 92%, we are concerned to understand how a reduction in NGN's proposed targets, (at a cost that customers appeared to accept and be willing to pay for) will enable NGN to deliver what customers asked for (we comment further in later GD/NGN annexes).

### Impact of Ofgem's DD

Our concern is how the DD will potentially impact on all three of the outcomes Ofgem hopes to achieve – a safe and reliable network; good customer service and lower environmental impact, although we recognise the imperative of keeping costs affordable. We comment later on the specific areas, but our main concern is that the cut in Repex will inevitably make the network less safe and reliable without additional maintenance costs (which we do not believe have been awarded). The impact on customers' average annual bills of the cut to Repex has been estimated at £1.30 a year for NGN customers but this seems to take no account of additional maintenance costs or replacement costs in the longer term if the gas grid is repurposed.

## Green Recovery and Wider Economic Impacts

Given the dramatic changes wrought by COVID-19 and the acceleration of, and emphasis on, a green recovery, we are not convinced that Ofgem's DD will encourage and stimulate companies like NGN to play their full part in the immediate and longer term economic, social and environmental challenges of their region over the RIIO-2 period.

Utilities are relatively stable industries to which the Government look not only for investment but also to help the local economy with the employment of apprentices, development of the local supply chain, creation of jobs, etc. We would like to see more incentives for GDNs' work to support local supply chains in Ofgem's FD and how that links with any Treasury stimulus package.

## 2 RIIO-2 Review

### Net Zero and Whole Systems thinking

We agree that there is currently no one defined pathway towards Net Zero. We believe that more could be done during RIIO-2 to test different pathways. Whilst Ofgem should retain some oversight, we are concerned that lengthy bureaucratic decision-making processes might jeopardise progress that could be made during RIIO-2 in exploring effective systems changes.

Ofgem needs to ensure that RIIO-2 balances the claims from electricity companies that they can offer the solution for heat and transport and competing claims from gas companies. Both industries are asking for resources that energy customers will pay for. In a geographically diverse system Ofgem needs to consider the impact on the system overall as well as respecting the needs and preferences of stakeholders and customers within the companies' boundaries. We recognise this is a difficult task and would encourage a greater focus on whole systems at a national and local level.

### Decision timescales and process

We offer 3 comments:

It would appear that Ofgem's incentive-based approach is being pared back with a more centralised control of costs through re-openers linked to policy uncertainty.

Whilst we accept it is prudent to make contingency plans if COVID 19 continues to put at risk the timescale for the final determination, we urge that if at all possible the original timescales are adhered to and we note that it is Ofgem's intention to make FD by April 2021.

It was helpful to see the different building blocks for RIIO-2. We suggest that in the FD Ofgem map how these differ to RIIO-1 and the customer impacts that will flow from them.

## 3 Embedding the Customer Voice in RIIO-2

We share Ofgem's expectation that customer needs are at the heart of the way companies run their business and indeed we helped to drive NGN's stakeholder engagement strategy to achieve this goal. Whilst many of the initiatives supported by stakeholders and customers have been included in the companies' plans, it is not at all clear how Ofgem have considered those views, which were also reflected in CEG reports on the Business Plans (Dec 2019).

We were disappointed that it was not possible to hold the Open Hearings, however we were pleased to have the opportunity to discuss our report and any differences to the CG's assessment.

We welcome the new proposal to hold Open Meetings in October to allow stakeholders views to be heard prior to Final Determination (FD) and we expect that sufficient time is allowed for their voices to be heard at this critical stage in the decision-making process.

We agree that the CEGs can continue to offer value to customers through an enduring role. We ask Ofgem to note the impact assessment we published as an appendix to our Dec 2019 report which highlighted both the qualitative and quantitative impacts of our Group. We have published a draft revised Terms of Reference on our website which, in the run up to the start of RIIO 2 in April, will be to ensure the Company's readiness to deliver the outcomes and outputs it proposed. A longer-term role is in line with the proposals from Ofgem and in line with NGN's proposals in its Business Plan. We have recently refreshed the group through an open recruitment process led by the CEG.

## Consultation Questions

***Q1. What role should Groups play during the price control period and what type of output should Groups be asked to deliver? Who should be the recipients of these outputs (companies, Ofgem and/or stakeholders)?***

We make no comment on the role of the UGs. The role of the CG was helpful in benchmarking and guiding Ofgem. It is unclear what form of enduring role it should play apart from of course in assisting Ofgem with future price controls including the current ED2 scrutiny phase.

We agree with the purpose of the CEG proposed by Ofgem. There should be one Group per company rather than a single CEG. It would be difficult for one group to undertake the depth and breadth of scrutiny we believe is required for all of the companies without this becoming a full-time role for individuals. This could then jeopardise the independence of the members, their ability to properly reflect and consider regional differences and potentially risk the competitive elements of the process. Working at a regional level, Groups have learned a great deal and have developed a wide and broad understanding of the business and its customer and stakeholder base. To lose this would be a retrograde step. Equally, a national approach would lose the granularity of conversations with customers. Given, among other things, the Government's levelling up agenda, a Group based on NGN's broad, northern, footprint will be more sensitive to how the Company can best contribute to that agenda through its regulated activities. Whilst Customer Engagement Group members need to understand the locality the Company serves, there should also be good sharing of information between groups at a formal and informal level.

A key role must be to ensure stakeholder and customer views continue to be heard throughout the delivery of the Business Plan and that any changing views are properly captured and reflected.



Given the level of funding subject to UMs a key role would be to scrutinise innovation proposals and any new projects that the Company brings forward.

These roles are already embedded in the draft Terms of Reference we are working to, along with our role in scrutinising the preparations NGN are making to deliver their RIIO-2 outputs.

It is Ofgem's role to retain oversight of the work of the Groups and that they follow any guidance issued by the regulator. Ofgem has a role to play in keeping the Groups informed of developments, policy or regulatory methodology changes, and in ensuring best practice is shared.

We would also urge Ofgem to set out how CEG views will feed into decision-making in future, provide clarity to the groups on its internal processes and provide transparency to others on how trade-offs are made between the views of different groups and Ofgem assessments/benchmarking.

***Q2. What role should Groups take with respect to scrutinising new investment proposals which are developed through the uncertainty mechanisms?***

Given the level of funding subject to UMs a key role would be to scrutinise proposals and ensure any new projects that the Company brings forward have been tested with stakeholders as appropriate, while reviewing the CBAs with the aim of ensuring value for money. In the case of NGN, we have a scrutiny mechanism in place to ensure it will follow internal governance procedures established for Innovation programmes. We propose to monitor the impacts on NGN customers in line with the reporting framework.

***Q3. What value would there be in asking Groups to publish a customer-centric annual report, reviewing the performance of the company on their business plan commitments?***

A set of outputs are envisaged by the NGN CEG including an annual report to Ofgem, but which is accessible by all stakeholders. We would also hope to hold an annual Company stakeholder event with the Citizen's Jury to hear stakeholder responses to annual performance and the Company's plans for the next year. We would be content to contribute to a national event to share good practice, stakeholder experiences and profile effective partnerships.

***Q4. What value would there be in providing for continuity of Groups (albeit with refresh to membership as necessary) in light of Ofgem commencing preparations for RIIO-3 by 2023?***

In our view, there is a need for continuity of the CEGs to ensure a good understanding of the regulatory framework and company operations. The membership should be refreshed on a regular basis (NGN CEG members had an initial contract for 2 years which has been renewed by 3 years for 8 of the original 10 members and a further 2 appointments were made in May 2020). Some existing knowledge should be retained for RIIO-3 but new skills and experience should also be sought where needed depending on future guidance from Ofgem. Maintaining a conflicts of interest log will be essential.

## 4 Quality of Service

We support Ofgem's proposals for more stretching targets for RIIO-2 and we welcomed NGN's plans to enhance customer service outputs and to return funds to customers where they fail to meet quality standards. We also support the fairer sharing of funds where efficiencies have been found to reduce costs.

It seems very sensible that where companies submitted similar bespoke outputs that these should become common outputs. Consideration of alternative types of incentives for outputs is also helpful where these deliver the same or improved services to customers more cost effectively. Where stakeholders and customers have already expressed a clear preference for a service at no additional cost, we expect those to be supported by Ofgem.

We note that final guidance is still awaited from Ofgem on best practise on **Modernising data/digitalisation**. We also acknowledge that whole systems innovation may depend on open data sharing. Our scrutiny of NGN's Business Plan focussed not so much on the type of data but on data security.

### ***Q5. Will the combination of the two proposed Licence Obligations support the delivery of a digitalised energy system and maximise the value of data to consumers?***

The way in which data is made available, and to whom, will be important in future whole systems development and changing LOs to enable this is clearly an important move.

### ***Q6. Do you agree with our proposed frequency for publication of updates to the digitalisation strategy and the digitalisation action plan, respectively?***

Yes, this proposal seems sensible to encourage greater transparency.

### ***Q7. What kinds of data do you think should comply with the data best practice guidance to maximise benefits to consumers through better use of data?***

All data should comply with best practice. Any exceptions should be noted with caveats/justifications e.g. GDPR. Where individual data is not accessible due to GDPR, scaled data should be available. This is particularly important to assist the market to provide solutions for many energy challenges. The digitisation of the energy system and a move to greater digital transparency will be a key theme for the industry as a whole in the coming years. For the GDNs in the short-term better use of data could impact rural energy poverty challenges and improve the identification of fuel poor households off the gas network.

### ***Q8. Do you agree that the Groups could have an enduring role to work with the companies to monitor progress and ensure they deliver the commitments in their engagement strategies?***

See section 3 above. Yes – we believe this is an important function. Ofgem must also retain control and not delegate its responsibilities to the Groups. There is however a clear need to monitor engagement strategy deliverables and to ensure that GDNs

continue to listen to their customers and are agile in responding to what they hear, including any changes to their strategy. The CEGs should report on this activity to Ofgem.

We note that Ofgem has now decided that it will not replace the Stakeholder Engagement Incentive with an ODI as there appeared to be no common outputs proposed by the companies. We believe that Ofgem should establish a benchmark of good practice and expected deliverables for the GDNs given the emphasis on stakeholder engagement as an essential part of both regulatory decision-making and how the companies should run their business.

### Maintain a Safe and Resilient Network

The deliverables in the EAP were tested and supported by stakeholders. NGN made significant improvements to its initial draft EAP and we wish to ensure the company is properly incentivised for delivery/penalised for non-delivery of its deliverables.

***Q9. Do you agree with our proposal to accept the proposals for an ODI-R for BCF and the other proposals set out above as EAP commitments and to require progress on them to be reported as part of the AER?***

Whilst generally supportive of the ODI-R for BCF we are concerned that delivery of EAP commitments are monitored closely and there is sharing of best practise. Using common standards will help ensure regulated businesses can engage all staff, processes, products and procedures in their EAP and provide good challenge mechanisms for continuous improvement. As part of the enduring role of the CEGs we propose to scrutinise the programme and the roll out of these commitments along with reporting requirement under the AER as per the guidance due to be published this autumn.

### 5 Ensuring Efficient Cost of Service

We note that a significant amount of GDN Totex will be linked to UMs (Repex reopeners in particular) and PCDs. We support the use of PCDs but as stated earlier we remain concerned that so much of the funding may not be agreed until late in RIIO-2 if processes to bring forward and agree proposals prove to be protracted.

***Q10. Do you agree with our proposed RPEs allowances? Please specifically consider our proposed cost structures, assessment of materiality, and choice of indices in your answer.***

We support the use of CPIH as a common standard used across government and the public sector more generally. We also support including forecast RPEs with annual true-up.

***Q11. Do you agree with our proposed ongoing efficiency challenge and its scope?***

We requested that Ofgem carry out an additional assessment of efficiency levels as we did not have the resources to do this as part of our scrutiny role, and this was considered to be a sector-wide issue more properly led by Ofgem. We are not equipped to comment on the levels proposed. However, we seek firm reassurances from both NGN and Ofgem that the drive to greater efficiency will not lead to lower customer service standards and



NGN's ability to deliver a safe and reliable service. We also note that NGN embedded significant efficiency savings and as a frontier company has historically been shown to deliver high standards and increase efficiency through the Totex incentive mechanism and outsourcing contracts. We expect that efficiency gains from embedding innovation from GD1 have been fully considered.

## 6 Financing

N/A

## 7 Managing Uncertainty

### ***Q12. Do you agree with our proposed common approach for re-openers?***

We believe the UM mechanisms themselves are appropriate and we highlighted in our report (Dec 2019) that we believed that NGN had properly allocated costs against these in its Business Plan.

We believe that as areas of Government policy become clearer Ofgem should have the opportunity to re-open certain output areas where revenue is not already committed. There are clearly advantages and disadvantages to increasing the number of re-opener slots and these should only be used where the case can be clearly made in customers' longer-term interests. We are also concerned as to whether Ofgem has the capacity to deal with potentially large numbers of re-openers. We expect it would need to increase resources to meet potential demand and also demonstrate that it is working efficiently and not adding to licence costs. Sufficient time must be allowed for proposals to be prepared and for stakeholder scrutiny as well as Ofgem consideration. Where the companies identify major changes are required in customers best interests, and they have the support of stakeholders, they should have the opportunity to propose re-openers. A number of relevant Government policy documents have been delayed but are expected to emerge in coming months so early re-openers should be considered as soon as possible in RIIO-2.

### ***Q13. Do you agree with our proposals on a materiality threshold, a financial incentive, a 'foreseeable' criterion, and who should trigger and make the application?***

We agree there should be clarity on these issues and that the case is clearly articulated why these are in customers best interests.

### ***Q14. Do you consider that two application windows, or annual application windows, are more appropriate, and should these be in January or May?***

No comment.

### ***Q15. Do you consider that the RIIO-1 electricity distribution licences should be amended to include the CAM, or wait until in 2023 at the start of their next price control?***

Licence changes should be amended in line with a clear need to do so which would lead to positive customer outcomes. It is not clear to us at this stage whether the need to amend ED1 is necessary.

***Q16. Do you agree with our proposed re-opener windows for cyber resilience OT and IT, and our proposal to require all licensees to provide an updated Cyber Resilience OT and IT Plan at the beginning of RIIO-2?***

Yes.

***Q17. Do you agree with our proposal for the Non-operational IT and Telecoms capex re-opener?***

No comment.

***Q18. Do you agree with our approach to using a re-opener mechanism for changes to government physical security policy?***

Yes.

***Q19. Do you agree with our approach regarding legislation, policy and standards?***

It is important for the Companies to be able to respond to major changes that are unforeseen or fundamentally change the nature of their business. We assessed that NGN had appropriately reflected policy uncertainty in developing its Business Plan outputs. Where Companies are advocating changes to policy and legislation their positions should be made transparent to customers and stakeholders along with any impacts they will have on them.

## 8 Net Zero and Innovation

### Net Zero

***Q20. Do you agree with our overall approach to meeting Net Zero at lowest cost to consumers? Specifically, do you agree with our approach to fund known and justified Net Zero investment needs in the baseline, and to use uncertainty mechanisms to provide funding in-period for Net Zero investment when the need becomes clearer?***

In principle yes. However, the associated costs need to be fully understood and the impact on current and future customers should be equitable. We also seek reassurance from Ofgem that there is not a 'double charge' on consumers through different regulatory frameworks. Where customers have expressed a clear view that they want a company to go faster towards Net Zero targets and there are regional plans (LAEPs) to support this; where costs are not significant and customers are willing to pay and understand the short and longer term impacts on bills, we believe the Companies should have the remit to go faster.

***Q21. Do you think the package of cross sector and sector-specific UMs provides the appropriate balance to ensure there is sufficient flexibility and coverage to facilitate the potential need for additional Net Zero funding during RIIO-2?***

We agree that there needs to be more focus on cross-sector packages e.g. DNO to GDN and cross-company e.g. GDN to GDN incorporating heat and transport transition roadmaps. The Government should also be funding policy changes and not relying solely on this price mechanism for any major investment (see our response to Innovation questions)

***Q22. Do you have any views on our proposed approach to a Net Zero re-opener?***

Stakeholders expressed clear preferences for NGN to be ambitious in tackling environmental impacts and will not wish to see any unnecessary delays. Clearly there should be a strong link to national policy and carbon budgets especially at a regional level. However, the materiality threshold may exclude smaller scale but meaningful proposals coming forward as part of whole systems transition.

**Innovation**

***Q23. Do you agree with our proposals for the RIIO-2 Strategic Innovation Fund?***

We welcome this approach to supporting major developments although we understand that the level of funding remains the same as under RIIO-1 despite Ofgem acknowledging that more investment will be needed to meet Net Zero over the next decade. We note that all customers pay towards these costs and we wish to see the benefits set out for different customer segments including those in vulnerable circumstances. Decisions should be linked to Climate Change Commission reports and evidence from other bodies including the National Infrastructure Commission and proposed new infrastructure taskforce should be explored, along with a coordinated approach with other bodies where possible.

***Q24. Do you have any comments on the additional issues that we seek to consider over the coming year ahead of introducing the Strategic Innovation Fund?***

Whilst it is helpful to align goals with other essential partners' ambitions and targets in the public and other sectors, there is a danger that timescales might be lengthy and drawn out as different interests and funding streams are drawn together. We urge Ofgem to set out how they envisage processes working and timescales to minimise delays but build in quality assurance and ensure delivery within RIIO-2. We also need to make sure that SIF is not biased for power/electricity; that it reflects different regional solutions capturing different rural and urban systems; and provides incentives for cross-sector and third-sector involvement to ensure the consumer voice is incorporated – particularly the vulnerable consumer.

***Q25. Do you agree with our approach to benchmarking RIIO-2 NIA requests against RIIO-1 NIA funding?***

No comment.

***Q26. Do you agree with our proposal that all companies' NIA funding should be conditional on the introduction of an improved reporting framework?***

Yes – but we urge Ofgem and the companies to bring this forward as soon as possible to allow early NIA funds to be released. It also needs to have more transparent oversight, greater evidence of BAU adoption across sector, a more multi-disciplinary approach and highlight the fails as well as the wins.

***Q27. What are your thoughts on our proposals to strengthen the RIIO-2 NIA framework?***

We agree these look sensible but urge early approval to allow innovation proposals to develop and be implemented as soon into RIIO-2 as possible. Improved external communication and greater multidisciplinary expertise will become ever more essential. It may be beneficial to build an advisory panel or group to help address one or more issues and avoid internal expertise promoting a gas industry orthodoxy where learning from other sectors could be helpful and relevant. But it is important that any framework does not thwart very new innovation.

***Q28. Do you have any additional suggestions for quality assurance measures that could be introduced to ensure the robustness of RIIO-2 NIA projects?***

There should be strong internal governance and stakeholder input to ensure the projects meet the aims of the Business Plan and bring external knowledge and expertise. We were pleased to see NGN have developed governance and assurance controls and we shall be monitoring the application of these. CEGs should review stakeholder acceptance of the projects before final approval by Ofgem and Ofgem should seek feedback from customers/stakeholders impacted or likely to be impacted.

***Q29. Do you agree with our proposals to allow network companies and the ESO to carry over any unspent NIA funds from the final year of RIIO-1 into the first year of RIIO-2?***

We agree that if any NIA programmes have been impacted by Covid 19 these are allowed to carry over. If projects cannot be completed any underspend could be added to support new projects subject to them meeting the new criteria for RIIO-2 to support vulnerable customers.

***Q30. Do you agree with our proposal that all work relating to data as part of innovation projects funded via the NIA and SIF will be expected to follow Data Best Practice?***

This seems sensible however the Data taskforce seems very industry centric. Ofgem needs to ensure it doesn't add more cost to the consumer and is paid for out of efficiencies. However, we can't comment in detail until we have seen the guidance on best practice.

## **9 Increasing Competition**

***Q31. Do you agree with our proposed position on late competition?***

No comment as NGN is only subject to native competition

***Q32. Do you agree with our proposed approach on early competition?***

As above.

**10 Totex and Business Plan incentive Mechanisms**

***Q33. Do you agree with our view that SHET, SPT, SGN and WWU passed all of the Minimum Requirements, and as such are considered to have passed Stage 1 of the BPI?***

No comment.

***Q34. Do you agree with our rationale for why NGET and NGGT should be considered to have failed Stage 1 of the BPI?***

No comment.

***Q35. Do you agree with our rationale for why Cadent and NGN are considered to have passed Stage 1 of the BPI?***

We agree with Ofgem's decision on NGN but have no comments on Cadent's BPI.

***Q36. Do you agree with our overall approach regarding treatment of CVP proposals?***

The Customer Value Proposition was introduced late into the business planning process, and it was difficult for CEGs to make judgments on the CVP propositions for a variety of reasons, however we agreed that most of NGN's proposals merited recognition. We used the level of customer support expressed in stakeholder engagement mechanisms as our key benchmark, and evidence of the methodologies used in calculating any financial benefits.

We support OFGEM's proposed award to NGN of £1.6m for setting stretching timebound targets to make repairs to lower rise leaking pipes.

However, we would also welcome early guidance, discussion and agreement on the approach to be taken to bringing forward and forming a view on any future CVP for RIIO-3 as considerable time and effort was expended in pulling together the propositions and in considering them without sufficient clarity from Ofgem on its expectations.

It was emphasised in the DD briefing that CVP is a prize, a competition that not everyone can win. If Ofgem is genuinely seeing the process in that light, then perhaps in the future it should be an actual competition with a clear set of rules. The same degree of analysis and rationale underpinning any entry could be required but framed in a way that allowed comparisons and assessment of outcomes. A common SROI might be valuable for RIIO-3 (and ED2)



We would also make the observation that while some of NGN's proposals might not be 'innovative' in the sense of being new or different, they are new innovations for their customers. As such, we are keen to ensure that the Company is in a position to deliver them.

***Q37. Do you agree with our proposed clawback mechanism to treat received CVP rewards?***

We agree that non-performance should generally not be rewarded.

## 11 Interlinkages

***Q38. Do you have any views on the interlinkages explained throughout this chapter?***

**CEG perspective on the Repex-opex interface** - If Repex is disallowed then there will be an impact on Opex as the 'pressure-bearing' nature of the network will change, meaning that pressure regulation will be required to reduce leakage, for example. Pressure regulation comes at a cost as it is a separate intervention that requires management supervision from a control room to monitor and efficiently implement. A new pipe is a more secure and resilient asset and requires less attention than a potentially less robust, ageing one. Customer awareness of the linkage between Repex and Opex is likely to be low but reducing the safety and resilience of the network and increasing operational costs to do so cannot be in the customers' best interests.

***Q39. Are there other interlinkages within our RIIO-2 package that you think are relevant to the three pillars identified in this chapter?***

No comment.

***Q40. Do you have any views on our proposal to include a statement of policy in Final Determinations that in appropriate circumstances, we will carry out a post appeals review and potentially revisit wider aspects of RIIO-2 in the event of a successful appeal to the CMA that had material knock on consequences for the price control settlement?***

No comment.

***Q41. Do you have any views on the proposed pre-action correspondence, including on the proposed timing for sending such to Ofgem?***

No comment.

***Q42. Do you think we need specific mechanisms in RIIO-2 to manage the potential longer-term impacts of COVID-19? If yes, what might these mechanisms be?***

COVID 19 has required organisations to consider

- the resilience of its system
- the resilience of its operations and preparedness

- remote working practices

These could be the same challenges presented from other unforeseen tragedies e.g. flooding. Annual reporting on the impacts of COVID 19 and other disaster readiness should be made by the Companies to Ofgem.

There is also the opportunity to survey staff about learnings from changes implemented at different stages during the COVID 19 outbreak. Any lessons should be shared/rolled out to other organisations for the benefit of the whole system.

Any responses/adjustments to major longer-term COVID 19 challenges should be subject to stakeholder scrutiny and views where there is any impact on customer services and costs.

## GD Sector Annex

### Introduction

The NGN CEG views have been developed based principally on their potential impact on the customer-centric parameters where we ascertained that customers' priorities lay, including

1. Customer quality of service
2. Customer perceptions
3. Customer bills
4. Safety
5. Environment
6. Asset life (for future generations to bear the cost)

There seems to be an over pre-occupation with 'uncertainty around the future of the gas network'. Whatever happens in the move to hydrogen or electrification of energy, it is likely to be phased, vary depending on local systems, and extend beyond 2037. There will be significant residual reliance on gas networks. Whilst we recognise the need to ensure investments meet future need, the reasoning behind the majority of cost rejections of a greater than 16 year payback is somewhat weakened.

We are not sure how Ofgem has considered the granularity of Company costs as a function of region and request these be set out in the FD to allow stakeholders to better understand variations in charges. A GDN region is a function of: geographical location, local labour rates, urban and rural mix, soil type, population density variability, industrial base, etc. We are uncertain how reflective of NGN's unit costs the allowed revenues are. (We also note that NGN's innovation around contractual design (gainshare) and supplier engagement has driven down costs and we also note the impact of historic investment costs in final charges.) It is also an advantage that lower labour rate areas of the country such as NGN's region hold as a customer advantage. This cannot be ignored, or investment profiles and decisions skewed as a result of using average unit costs. This is not in the customers' interests. Ofgem appear to have created an instrument to penalise lower cost regions and to reward higher cost regions by not acceding to the use of true regional costs. An explanation of how impactful this is on customer bills might usefully be explored at the Open Meetings.

### 1 Output consultation questions

***GDQ1. Do you have any views on our common outputs that haven't been covered through any of the specific consultation questions set out elsewhere in this chapter? If so, please set them out, making clear which output you are referring to.***

Generally, the CEG is supportive of the approach Ofgem is taking (including ODIs) of focusing on penalty rather than reward in interruptions to supply as this appears to be of customer benefit. Our concern is that NGN proposed Bespoke Outputs based upon detailed customer and stakeholder feedback and we are not yet convinced that Ofgem's proposed changes reflect the minimum level of service customers specified.

Whilst the CEG remains concerned that there is potential for unintended consequences in terms of behaviours and performance as a result of changes to GSoPs and Caps we

support the ambition to improve service overall. We also recognise that the changes to GSoPs and other outputs are broadly in line with NGN's BP despite Bespoke Outputs not being accepted. NGN has indicated that it will continue to strive for service improvements indicated by stakeholders during engagement and reflected in its Bespoke Outputs such as 3 calendar days (with some exclusions) for reinstatement (GSoP2). The CEG appreciates that some details are still being discussed with Ofgem but supports NGN's ambition in providing higher standards. We will, of course, monitor performance and stakeholder feedback to ensure service levels do not drop or disadvantage any customer groups.

Measuring customer satisfaction (CSAT) is an integral part of monitoring performance and the targets associated with it need to be both stretching and achievable. We offer some thoughts on this even though it is not a formal part of this consultation exercise.

The CEG welcomes the results of the October 19/Mar 20 trial of a new methodology for collecting CSAT data and believes it to represent a more accurate picture of what customers think about certain elements of the service they receive from GDNs. Surveying closer to the interaction and broadening the demographic of customers provides a richer and clearer perception. We are concerned that Ofgem uses the right drivers to improve customer satisfaction and seek assurance that Ofgem has fully assessed the risk that the use of penalties alone might drive poorer performance or unintended consequences. In introducing a new process Ofgem has not afforded the GDNs a similar amount of latitude to that given in the overall complaints target – i.e. space to embed the new process at a target level that is stretching but does not penalise previous good performance or encourage unintended behaviours. The CEG urges Ofgem to consider whether:

- on balance the proposed deadband ought to be removed or applied to both the positive and negative sides of the target –to penalise poorer performance and reward good performance
- it is appropriate to base RIIO-2 targets on RIIO-1 performance without taking into account the more accurate (and lower overall) results of the Oct 19/Mar 20 trials.

Customers at NGN's first Citizen's Jury meeting believed that a score of 9 was "a fantastic score". It is unclear where the customer voice is reflected in the new methodology.

***GDQ2. What are your views on the reporting metrics we have proposed for the consumer vulnerability ODI-R?***

Ofgem are proposing 3 simple metrics

- Average customer satisfaction for PSR customers
- Number of FPNES connections – reported at an annual event
- Average CO awareness score via a common survey.

These are very high level and do not measure the impacts or outcomes.

For example - It is unclear what criteria GDNs will need to use for FPNES. Evidence of fuel poverty is defined differently in the 3 countries of GB and it is not easy to assemble all data required at a reasonable cost to ensure accurate reporting. However, a reporting

metric on the impact of any intervention in terms of anticipated energy bill savings could be used, and proxies identified that allow the companies to better target FPNES. New AI tools are available to predict fuel poverty and Ofgem should explore with BEIS how these could be used across the sector. Reporting on FPNES at a national event could be useful in showcasing different approaches to share lessons on how to deliver holistic best practice outcomes.

We agree with the PSR metric but still feel neither NGN nor Ofgem is going far enough. Whilst measuring high level satisfaction provides some indication of performance it fails to take account of the spirit of the PSR – to provide priority services to those who need them most. The industry must ensure that the right referrals are made to and accepted onto the PSR. Measuring customer satisfaction with the PSR will not provide this. We highlighted this in our report, but we are yet to see evidence that anyone is monitoring the quality of referrals or that PSR customers actually get more help.

We consider that measuring Social Return on Investment is very important and we propose that Ofgem should work with the companies to develop a metric that can be trialled in GD2 and implemented beyond that period.

***GDQ3. What are your views on the design of the annual showcase events, including whether they should be held at a national or regional level?***

National versus regional annual showcase events - an argument can be made for both. A regional focus with regional stakeholders will be invaluable for concentrating on regional issues and enabling NGN to better engage with local partners. Equally, a national focus would bring together good practice, sharing of ideas and discussion at a national level. It might also develop some 'healthy competition' but some of the richness of the regional focus would be lost. We would recommend a blended approach comprising an annual regional event supplemented by a focused national event that looked at areas of common interest. There is a logic to combining a national event with another pre-existing event to make best use of stakeholders' time and would provide a platform for discussing common themes. Given that a percentage of UIOLI funding is for collaborative projects there is scope for GDNs to share platforms and engage with stakeholders at a sensible level.

Disseminating good practise might usefully be done via on-line events to increase access by those unable/unwilling to travel to events and might offer better value for money. Also – learning the lessons from LCNF events we suggest that Companies do not charge stakeholders; ensure diverse audiences and seek to demonstrate genuine sharing of lessons that could be adopted by others.

Ofgem asks about the content of such an event and whilst it should not be the CEGs that specify topics, any contextually relevant event must focus on regional issues and provide customers and stakeholders with clear evidence of what is being done, how that links to what customers and stakeholders said they wanted and what the Company is proposing to do in the next year based on feedback.



**GDQ4. Do you agree with our position to change the FPNES from a PCD to a capped volume driver?**

We agree with Ofgem's approach –although we challenged NGN to be more ambitious in this area. The ability to deliver a holistic package is at risk with the focus on renewable heat and shift away from gas central heating in programmes such as the Government's new Green Homes Grant and likely restrictions to proving gas heating under ECO beyond 2022.

Regarding Customer Complaints: We agree with the approach including setting the overall target at 5. The CEG believes that this provides space for GDNs to improve over time. However, given Ofgem states it expects the level of complaints received to be maintained, we believe that Ofgem should require companies to report on actions taken to reduce the numbers of complaints received. We would not want to see a return to the bad behaviours of the early 2000s but do not believe that penalising the time taken to deal with complaints and supporting this with customer satisfaction measures will necessarily reduce the causes of customer dissatisfaction and therefore the number of complaints. We have challenged NGN on this aspect of their performance, and they provided evidence of targeting areas of poor performance at a granular level including particular age groups and the impact of different types of communication used during works. Requiring Companies to report on complaint reduction activity would focus minds on quality of service as well as complaint handling performance.

**Guaranteed Standards of Performance**

**General comments**

As referred to above the CEG is supportive of the drive to improve service and performance across the sector and believe that mandating automatic payments and doubling GSoP Payments and Caps will encourage better performance by some GDNs. The concern remains, however, that, in some areas, service may not improve as anticipated and GDNs may not be as ambitious as their original plans suggest.

We also support linking payments to increases in CPIH as this will provide consistency but urge Ofgem to clarify the process for increases – will they be in the current regulatory year or the following year? Who will be responsible for determining this, how will customers be informed, etc.?

**GDQ5. For GSOP3, is a 48-hour exclusion period for the provision of access to hot water and food in the event of a major incident appropriate? Should this be extended to cover interruptions that are not a major incident?**

The CEG believes that customers, particularly those in vulnerable circumstances, will welcome the 48-hour provision of access to hot water and a hot meal although it seems a little perfunctory. We propose a small degree of flexibility to assess what is genuinely needed (above what is ordinarily provided during interruptions) for those affected by the interruption. This may well be a hotplate or a shower but, for example, in summer a hot meal may not be required. In terms of extending the GSoP to interruptions that are not deemed major incidents the CEG believes the same rules ought to apply. GDNs should be given a window of time to provide customers affected with what they need to manage the interruption. This will be determined by local need and potentially time of year.

**GDQ6. In relation to our proposal to extend quotation GSOPs on entry and exit connections, is it sufficient – in regard to green gas entry enquiries – for these GSOPs to apply to the provision of initial and full capacity studies? Are there other parts of the green gas entry process we need to consider to ensure an improved service provision?**

We note NGN has improved engagement with biomethane producers and have introduced new codes of practice to meet their needs. Monitoring the impact and any remaining barriers to entry might be a useful first step before setting a new GSOP and perhaps linked to any re-opener on the future of heat policy.

**GDQ7. What are your views on our consultation position to monitor the provision of and adherence to appointment timeslots for purge and relight activity through an ODI-R? Are our suggested reporting measurements reasonable?**

The CEG supports Ofgem's consultation position in relation to the provision of and adherence to appointment timeslots for purge and relight activity through an ODI-R. In today's world customers are used to appointment slots for a variety of services and prefer not having to wait around for engineers, etc. There is a logic to making this an ODI-R instead of a financial penalty but the CEG would expect Ofgem to monitor performance in this area going forward with a view to introducing penalties for suboptimal performance.

The CEG believes the reporting measures suggested are appropriate given the newness of this area of work but, as mentioned above, would expect Ofgem to review this over time with a view to introducing a penalty for failure.

**GDQ8. Do you agree with our proposed option to provide Cadent and SGN with consumer funding through Totex baseline or a financial ODI reward for collaborative streetworks activities?**

No comment.

### Delivering an environmentally sustainable network

**GDQ9. How should we set targets for the shrinkage financial incentive?**

Reducing shrinkage was high on NGN customers priorities as it accounts for 95% of the Company's CO2 emissions. The theft of gas represents just 3% of total shrinkage and whilst attention should be paid to this, it seems that the bigger prize is to be won elsewhere. It would be perverse for Ofgem to reduce funds that reduce shrinkage cost effectively (either through pressure management or Repex)

GDQ10. Do you have any views on what clarifications are needed to ensure a consistent method of calculating the benchmark shrinkage volumes?

GDQ11. Do you think a deadband should apply to the financial incentive? If so, please provide evidence as to how this

**GDQ12. What are your views on our consultation position for the four GDNs' EAP proposals in RIIO-2 as set out in this document?**

Our comments are limited to NGN's EAP. NGN stakeholders and CEG supported NGN's EAP goals and believe these will lead to meaningful outcomes - and these have largely been accepted by Ofgem. Ofgem's request for additional information from the Companies prior to FD seems reasonable particularly in relation to vehicle replacement costs. Monitoring performance against goals could be part of an enduring role for the CEGs.

***GDQ13. Do you agree with our consultation position to include progress on biomethane in GDN's AERs, alongside standard connections data?***

Yes. We have seen improved engagement by NGN with biomethane producers and monitoring the connections alongside other connections data will ensure processes become embedded in BAU activities giving biogas producers more confidence to develop new connections as other policies aimed at decarbonising the gas network are brought forward. NGN's ambition to increase biomethane to 15% of network gas by 2030 will require significant engagement with the producers to enable this increase. Offering more transparency to green gas producers and/or suppliers might also be done through some special mapping of the GDN region to indicate optimal locations to connect. Of course, it is not possible to consider this agenda in isolation from evolving national policy and any subsidy regimes or other forms of market intervention.

***GDQ14. Do you have any other comments in relation to this section?***

NGN Stakeholder responses around this agenda were very clear and it would be against the stated interests of customers for Ofgem to do anything that would inhibit or limit the ability of NGN to make progress in this area of activity.

Repex

***GDQ15. What are your views on the proposed set of Workload Activities for the Tier 1 mains replacement PCD?***

No comment.

***GDQ16. What are your views on our proposal to adjust allowances for the Tier 1 mains replacement PCD on the basis of mains decommissioned?***

No comment.

***GDQ17. What are your views on our proposed approach to setting unit costs for the Tier 1 mains replacement PCD?***

No comment.

***GDQ18. What are your views on our proposed Allowance Adjustment Mechanism and Allowance Adjustment Restrictions for the Tier 1 mains replacement PCD?***

The concept of GDNs being penalised for over-delivering is nonsensical from a customer point of view, especially given the miniscule impact on customers' bills. We note how

NGN customers relate to Repex; they equate new pipes with a safer and more resilient network – something that they have repeatedly stated when surveyed.

**GDQ19. What are your views on our proposed Workload Activities for the Tier 1 services PCD?**

No comment.

**GDQ20. What are your views on our proposed approach to setting unit costs for the Tier 1 services PCD?**

We raised above our concerns about regional variations and the use of average unit costs.

**GDQ21. What are your views on our proposed Allowance Adjustment Mechanism and Allowance Adjustment Restrictions for the Tier 1 services PCD?**

Our response to these questions has been summarised below and our comments reference very specifically Ofgem's DD on NGN's proposed Repex programme.

We have two general concerns regarding how environmental impacts have been assessed and how Ofgem have considered NGN customers views: \*by stripping out all non-mandated Repex the level of increased shrinkage needs to be considered with resulting environmental impact.

\* customer views supported increased action on shrinkage at a time when NGN was also offering a 13.6% cut in customer bills. Ofgem's position on Repex seems to be at odds with NGN customer preferences.

**NGN's Submission versus Draft Determination:**

**Costs Submitted: £530M**

**Draft allowance: £379M (-28%)**

- A 28% reduction is material in terms of infrastructure asset management, especially where the asset base is already recognised as being 'optimally' invested in.
- The way in which this reduction falls is fundamental to its impact.
- There is a shift of Tier 1 iron stubs to a re-opener scenario.

**Allowances by Pipeline Breakdown**

**Unaffected submissions:**

**Tier 1:** 2,122.9 km allowed as per submission. As such, no impact.

**Steel <=2":** 186 km allowed as per submission. As such, no impact.

*Note: Tier 2 pipes are > 8" and < 18"*

**Tier 2A:** 10.1 km allowed as per submission. As such, no impact.

**Tier 2B:** 100 km allowed as per submission. As such, no impact.

**Affected submissions:**

**Tier 3 (>18" iron pipes):** 50 km reduced to 0 km on the basis that the CBA did not payback until after 2037, with the rider that there is also a degree of uncertainty about the future of the gas network.

We make the following points on Tier 3:

We are concerned that Ofgem has focussed on a 16 year payback for the whole non mandatory programme of Repex based on its assumption of value for money. Other considerations include:

- Failing to replace pipes of this diameter and pressure rating increases the likelihood of significant joint leakage. This has a disconcerting effect on customers (gas smells), it increases the number of reported cases of gas leakage, increases call-out volumes and may ultimately cost the customer through more unnecessary emergency response costs. In addition, it adds to greenhouse gas emissions and is environmentally detrimental.
- Replacing these pipes has an overall positive impact on the above. With an 80-year design life, polyethylene (PE) pipes provide a lasting solution and opportunity to green the gas network. The diameter of the PE pipe and the cost of laying these equate to a higher cost which drives the longer payback period. A nominal 20-year payback (>17 years) is still only 20% of the design life. PE future-proofs the network allowing other gases such as hydrogen to be conveyed, thus facilitating the journey to net zero. The customer benefits of replacement are, therefore, significant and we therefore challenge the elimination of the 50 km replacement target to NGN's business plan.
- The alternative to replacement is to seal the joints using a tried-and-tested technology in anaerobic sealant injection or to apply cured-in-place liners. Both require trench excavations resulting in urban disruption. In time this leads to customer impacts – aesthetically, traffic management, potential loss of supply for periods of time, etc.
- So, if replacement is being rejected, there should be an increase in maintenance expenditure (Opex) to address the potential for ongoing leakage from these ageing assets. By doing so, customer safety risk will be reduced, and the environmental and shrinkage effects also reduced. It is not clear that Ofgem has understood the linkage and no associated opex increase has been made.
- Line-packing of these pipes will also need to be taken into consideration from a pressure management, leakage reduction and gas storage point of view. As such, replacing ageing, pressure de-rated pipes with ones able to be pressurised as storage vessels has huge customer benefits in terms of safety and reliability) and cost savings (noting the elimination of all gas holder operating and maintenance costs).

## Context

**Steel Mains > 2":** 149 km reduced to 0 km on the basis that the needs case was not justified, in particular, that:



- The expenditure increase between RIIO-1 and RIIO-2 was significant.
- Sensitivity analyses round key parameters was not presented.
- Aggregate level benefits in CBAs are not clear.

The CEG believes that NGN made a decent case for this investment but clearly failed to provide the necessary analysis to Ofgem.

- The leakage argument made above also applies here.
- Through-wall corrosion will continue; leakage will result, and the hybrid nature of the network will persist, lessening its ability to operate with other gases in the future.
- Whereas there will likely be no immediate benefit to customers, the ongoing degradation of steel in this diameter range will need to be addressed at some future point. To eliminate all replacement is naïve. We would encourage NGN to provide more analysis via a refreshed CBA for consideration prior to FD.

## Context

**Iron Mains > 30m:** 40.7 km reduced to 0 km based on the CBA not paying back until after 2037 and the associated uncertainty of the future gas network.

The CEG view is that:

- Replacing all pipes within 30m of a customer's property by 2030 is a very customer-centric operation and one where the costs have been accepted by Ofgem. We agree that extending that where necessary to beyond 30m should be assessed on a risk-based CBA basis. The practicalities of coupling a PE replacement pipe to an aged iron pipe can induce leakage at the interface with all the impacts mentioned earlier. It also means that an investment wave of such pipes is being built up for some future point when the cost will have to be met then. Indeed, there is a customer case for 'going in once' i.e. doing as much to a pipeline asset as possible via one excavation. The environmental and cost advantages of this are significant.
- By extending beyond the 30m line, the network is also being future proofed for use in conveying non-methane gases thus diluting the uncertainty around the future gas network.
- Ofgem should reconsider its DD on Iron Mains > 30m.

**Context - Other:** 18.4 km reduced to 0 km on the basis that the proposed use of PE mains replacement and Phoenix structural liners would not pay back until after 2037.

The CEG view is that:

- NGN's proposals were in effect tidying up and future-proofing actions around the network which will be required to convey non-methane gases in the future. As such, the costs will need to be borne relatively soon for NGN to be able to use current conduits for a hydrogen economy.

- More clarity around the diameter composition of these pipes and their criticality to the network would allow a more transparent picture to be painted around immediate customer benefits, with risk featuring strongly.

**Context - Services:** Where mains replacement has been disallowed, Ofgem have made pro-rata downward adjustments to services.

The CEG view is that:

- The Ofgem logic used here is overly simple. It does not follow that a service intervention is not justified where a main has not been replaced. A metallic service failure near a customer's property is a high-risk event given the risk of explosion. As such, to reduce the service replacement figure to zero in these sections of pipe is naïve. An allowance in the non-mains replacement service figure for these disallowed pipe sections must be made to compensate.

**Capital Investments – (Also reference chapter 3 on Capex)**

***GDQ22. What are your views on our proposal for a common PCD for capital investments?***

Ofgem's proposal will better protect customers from costs associated with non-delivery of outputs.

***GDQ23. What are your views on our proposals for delivery, clawback and deliverables for the capital projects PCD?***

Again – these seem on the face of it to protect customers from companies building in projects that may not take place. In NGN's case we believe they used UMs correctly in their submission and they should be in a position to deliver all Capital project outputs as set out in their plan. If not the proposed clawback and return of funding to customers ensures they are protected.

**Other policy areas**

GDQ24. Do you agree with our approach for funding physical security for the GD sector? And do you agree that in light of the proposed baseline totex that the physical security PCD is no longer required for the GD sect

***GDQ25. Do you consider that the enhanced obligations framework for exit capacity and the additional information being sought are appropriate?***

This is not an area we scrutinised in the planning process as it was subject to a separate Ofgem consultation.

**3 Cost of Service**

***GDQ26. Do you agree with our proposal of using a top-down regression model?***

The CEG is not resourced to comment with confidence on the methodology.

**GDQ27. Do you agree with our proposed approach to benchmarking modelled costs at the 85th percentile?**

Yes - we believe this should drive up standards across the sector.

**GDQ28. Do you agree with our proposed approach to estimating embedded ongoing efficiency and values calculated?**

We commented on efficiency savings in the Core Document but note these are challenging targets.

**Normalisation Consultation Questions**

**GDQ29. Do you agree with our proposed pre-modelling normalisations?**

No comment.

**Model Selection Consultation Questions**

**GDQ30. Do you agree with the selected aggregation level, estimation technique and time period for our econometric modelling?**

No comment.

**GDQ31. Do you believe we should take into consideration revised cost information for the remainder of GD1 including 2019-20 (actuals) and 2020-21 (forecast)?**

No comment.

**Opex Consultation Questions**

If Repex is scaled back, and we are not convinced that is the correct decision, Ofgem needs to consider the impact on Opex costs. Where CBAs showed it was more cost effective to replace pipes in RIIO-2 rather than maintain and potentially replace in RIIO-3 Ofgem should accept NGN proposals.

**GDQ32. Do you agree with our selected cost drivers for Opex?**

No comment.

**GDQ33. What are your views on our proposed approach to the synthetic cost driver for Repex?**

No comment.

**GDQ34. What are your views on our proposed Repex workload adjustments?**

We challenge whether the driver for reducing Repex is fully justified. Whilst there is uncertainty regarding the future of the gas network there are other drivers for continuing to replace non-mandatory mains pipes – including safety and shrinkage – both of which are priorities for customers. We have made these points more fully earlier in our response.

**GDQ35. Where we have disallowed workloads, should we consider making corresponding adjustments to Opex costs? If so, how do you think this could be done?**

In the first instance we consider Ofgem should reinstate some Repex costs. Where a CBA case cannot be fully justified, an assessment of increased maintenance costs (as considered in the Engineering Justification Papers) should be added to Totex.

#### Capex Consultation Questions

**GDQ36. What are your views on our proposed approach to the synthetic cost driver for Capex?**

No comment.

**GDQ37. What are your views on our proposed Capex adjustments?**

NGN's proposed Network Capex has been allowed in full – as supported by customers and the CEG. We agree with Ofgem's decision.

Ofgem have reduced NGN costs for rechargeable diversions by £12.7m (usually repayable by third parties) which was based on historic rather than proposed new works. Some degree of reference to historic performance should be accepted but where future costs can be more accurately predicted these should be a new baseline.

#### Non-regression Costs Consultation Question

GDQ38. Do you agree with our assessment of non-regression costs and our proposed adjustments?

#### Technically Assessed Costs Consultation Questions

**GDQ39. Do you agree with areas selected for technical assessment?**

No comment.

**GDQ40. Do you agree with our proposed approach?**

No comment.

#### Technically Assessed Costs Consultation Questions

**GDQ41. Do you agree with our proposed disaggregation methodology?**

We note that no Stage 4 awards were made due to poor Repex and Capex cost justifications. In our report (December 2019) we asked Ofgem to look more closely at costs as we were not resourced to do in depth benchmarking. We did however feel that the volumes of work proposed by NGN in Capex and Repex were justified based on the CBAs presented to us.

## Chapter 4

### Uncertainty Mechanisms consultation questions

We commented on UMs relating to decisions and consultation questions set out in the Core document. We reiterate our concern that there is an over reliance on UMs which could delay investment decisions and output delivery. We generally support the annual opportunity for companies to submit applications. However, we are concerned that the Net Zero reopener threshold may exclude meaningful but smaller scale initiatives by GDNs.

We note that shrinkage purchase costs will increase if Repex programmes are cut back. The whole purpose of Repex is to make the network more resilient, reduce leakage, reduce methane emissions to the environment and, in general, create a more technically, environmentally and commercially attractive infrastructure asset base. This is fully in-line with customer expectations, as espoused during consultations with them.

***GDQ42. Do you have any views on our common UMs that haven't been covered through any of the specific consultation questions set out elsewhere in this chapter? If so, please set them out, making clear which output you are referring to.***

***GDQ43. What are your views on the proposed re-opener for Tier 1 stubs?***

We believe the case was well made by NGN for stub replacement however it would seem sensible to have a UM until the HSE enquiry is completed. We would expect this to be done as soon as possible to allow greater certainty for work planning with stakeholders and reduce the cost of revisiting sites.

***GDQ44. What are your views on our proposal to introduce a <7bar diversions re-opener?***

We supported a reopener proposed by NGN given the uncertainty about how far north HS2 will reach during the RIIO 2 period.

Where energy network Green Recovery Infrastructure programmes are advancing with Treasury these may not need to be subject to a reopener as it could lead to delays in local economic recovery plans. Transparency over any additional costs to customers must be ensured.

***GDQ45. What are your views on the triggers and windows for the MOB's safety re-opener?***

***GDQ46. What are your views on our consultation position to address bespoke decarbonisation of heat re-openers through our proposed innovation stimulus, Net Zero and Heat Policy re-opener mechanisms?***

Again, we express our concern about the scale of the re-openers and the agility required to respond to these policy reviews. It would be beneficial to reduce bureaucracy both for Ofgem and the Companies to minimise costs and resources in preparing and reviewing bids to the mechanism.



The challenge with heat policy is the ability of communities to adapt to any changes and the costs involved are very dependent upon 'place'. For example, an upgrade project on a flat rural site with full/free access would be significantly cheaper than for a comparable development in a built-up urban setting. Conversely the geographic scale of upgrade in a rural setting to have the same impact (number of customers) as a suburban area would need to be attributed fairly. If consideration is made of these challenges when stimulus budgets are developed, then re-opener mechanisms could provide useful support to the still-evolving government policy in this area.

***GDQ47. What are your views on the questions set out in paragraph 4.57 of this document in relation to large hydrogen projects?***

These questions are important to protect customers from potentially expensive major investment costs. We also consider that Government funding rather than gas customer funding should be called on for major infrastructure programmes so the full impact of costs does not fall on energy customers alone – irrespective of their ability to pay or benefit.

*Should costs for industrial hydrogen decarbonisation projects be socialised or targeted? What level of contribution should there be from industry for long-term asset investment projects in this space?*

We propose targeted and part support only.

Across the Whole Energy Systems sector, there is rightly a push for decarbonisation due to the climate impacts of CO<sub>2eq</sub> emissions.

The challenge is how much of this net zero future energy should be fuelled by electricity via an upgraded power network and how much via green gas (inc. Hydrogen). There is no consensus yet on the pathways. There are strong advocates and lobby groups for both options.

The challenge Ofgem must recognise is to avoid extreme overinvestment in the whole network as both systems evolve simultaneously (but independently) to meet the future system needs. In all likelihood, the ultimate solutions will be a mixture of both electricity and hydrogen specific to geographic locations, regional commercial imperatives as well as speed to market of the innovations.

The push for industrial hydrogen decarbonisation projects is driven by industry being mindful of likely future penalties of utilising high CO<sub>2eq</sub> emitting technologies e.g. fossil fuelled powered electricity. Any move ahead of these penalties to socialise the cost is somewhat premature as the financial beneficiary of the change will be the industrial organisations, not society. However, due to the social impact of climate change and the current need for economic stimulus, a case can be made that support of these changes should be given.

So, a level of contributions from industry that considers the scale of penalties the system changes will help them avoid e.g. EUETS or post-EU equivalent, if no changes were made would seem fairer to the energy customer.

*Is the project intended to inform or reflect (be triggered by) a heat policy decision? If the latter, what policy decision needs to be made? This could include changes to policy frameworks to allow increased volumes of hydrogen blends into the national or local transmission system.*

The policy decision needs to be a change in Ofgem/HSE Safety regulations, or a sandpit regulated area to allow for piloting at scale of these innovations.

*Will there be a need for further changes to legislation, the use of derogations or involvement of other bodies (e.g. HSE)?*

Yes, to underline the safe approach these projects are taking in these significant system and gas mix changes. However, it is not clear how much change will be required during GD2.

*How are GDNs ensuring that projects are coordinated and avoiding undue duplication? Which evidence gaps will each project fill?*

This is very important to ensure best value for the customer, but it should be noted that geographical and other regional differences such as variations in local authority climate emergency plans throughout the energy system should be taken into account when 'rolling-out' projects to other GDN areas.

**GDQ48. Do you have any other comments in relation to this section?**

We wish to reiterate our view that this is a critical time for the Net Zero transition and both the companies and Ofgem will need to be nimble and respond to opportunities in line with local area energy plans. Putting in place building blocks that are likely to be needed for the future should underpin decision making.

**GDQ49. What are your views on our proposal to introduce a new domestic connections volume driver?**

During our scrutiny of the business plan we heard that the volume of connections has been fairly consistent over GD1. Demand may change depending on any changes to the Government's Heat Policy. Just as important is the quality of service for Connections Customers and we support improvements proposed by NGN for their customers.

**GDQ50. What are your views on our proposal to continue with the large loads re-opener?**

No comment.

**GDQ51. Do you agree with our definition of a 'large load' to use for this re-opener?**

No comment.

**GDQ52. Do you agree with our proposal to continue with a smart meter rollout re-opener?**

This seems sensible. However, we consider a later date might be better given the hiatus in installing smart meters during 2020. Also – we note the change in NGN’s position on this. If it is possible to avoid a reopener that might be a better option.

***GDQ53. Do you agree with our proposal to continue with a common streetworks re-opener?***

Yes – it is likely that local authorities will try to recover lost revenue from other sources and we consider a common reopener could be a useful mechanism. It will be important to alert local authorities and other stakeholders to the limited opportunity to trigger a reopener and to set the threshold at a level that allows the companies to trigger the mechanism.

## RIIO-2 Draft Determinations – Northern Gas Networks Annex

### Introduction

We reiterate the general comments on Ofgem's approach to DD that we made in the Core document. We welcome the emphasis on customer and stakeholder engagement in RIIO-2 but are disappointed that Ofgem do not appear to have fully considered NGN customers views in reaching DD. NGN took a well-reasoned, thorough and pragmatic approach to stakeholder engagement that is now being embedded throughout the company's decision-making processes. We support Ofgem's proposal that high-quality stakeholder engagement should be part of BAU in RIIO2 and that GDNs should report on this directly to stakeholders.

Overall, we welcome the focus on reducing bills for customers, and understand the objective for net zero. However, during NGN's research, customers wanted the Company to strike the right balance between a high-quality and reliable service and affordable bills.

Particularly, they wanted:

- Safety and reliability to be a key priority (with no compromise on safety)
- A reduced carbon footprint and limiting impact on the environment
- NGN to use its reach and resources to support struggling communities and customers (but without doing the job of others with statutory duties or charitable aims) given that its area covers some of the most deprived places in the country
- NGN to deliver value for money across all areas of its work

Given Business Plan acceptability was 92% the CEG would like to understand, from Ofgem why it believes how such a reduction in revenue will enable NGN to deliver what customers asked for and what it believes the collective and individual impact of the DD will be on the outcomes that customers said they wanted to see from NGN.

By reducing revenue, Ofgem is seeking significant efficiencies yet some of the major changes proposed to NGN's plans in the DD – especially the greater use of UMs appear bureaucratically intensive and potentially impacting efficiency.

Given the dramatic changes wrought by COVID-19 and the acceleration of and emphasis on a green recovery, we are concerned that DD will hinder NGN's role in addressing the economic, social and environmental challenges that are real for their customers.

Utilities like NGN are relatively stable industries to whom the Government can look not only for investment but also to help the local economy with the employment of apprentices, development of the local supply chain, creation of jobs, etc.

We note that NGN's baseline Totex has been reduced by £166m. It is not clear from Ofgem's DD how much of that translates to £20 reduction on the average domestic

annual gas bill, and how much might be added to that bill if the cost of proposals that moved into UMs are included.

Given the work that had gone on prior and subsequent to RIIO-I in agreeing the role and use of NARMS (formerly NOMS), we are concerned that this construct does not become the sole decision-making tool as opposed to a decision support tool. NARMS is a risk-based, stochastic modelling technique, with in-built error bands. Stochastic implies non-exact, however, in the DD, Ofgem has chosen to treat it as the means of exactly defining asset classes to be replaced. This is not its purpose and is not in the customers' interests. Customers put their faith in NGN to apply fit-for-purpose decision-support tools and to hire competent persons to do so. There needs to be an understanding that engineering decisions in situ must prevail where the model fails to offer the best solution and value for money.

### Common outputs consultation question

***NGNQ1. What are your views on the values for the common output parameters we have set out in the NGN Annex?***

We comment more generally on the Common Outputs above (GD annex).

### Bespoke ODIs Consultation questions

***NGNQ2. Do you agree with our proposals on the bespoke ODIs? If not, please outline why.***

There are only 4 of the proposed bespoke ODIs approved in the DD– all reputational. The CEG and NGN stakeholders supported these which were subject to business plan acceptability testing. Higher standards for NGN customers could have been achieved through more bespoke ODIs. We believe they can outperform many of the common customer service standards but there is less incentive for them to do so if budgets are cut due to the more stringent efficiency targets being set.

We support NGN's proposal for an additional bespoke ODI on improved reinstatement times to be included (reference NGN response to Q4) given the strong customer support for this.

***NGNQ3. What are your views on our proposal to accept the Job completion lead-time including re-instatement ODI? Do you have a view on what the percentage performance target(s) should be and how is it stretching?***

The CEG supports Ofgem's proposal to accept this aspect of the BP. 20 days is a stretch from current performance of 33.5 days. Customers will welcome improved performance in this area. The CEG has not yet seen NGN's proposed percentage achievements in this area and supports Ofgem's proposal to await further detail from NGN.

***NGNQ4. Do you agree with our proposals on the bespoke LOs? If not, please outline why.***

We support the creation of common GSOPs to drive up standards across all regions but remain concerned that this may impact ambition and performance in NGN's area, where the Company had proposed an increase in service levels in bespoke LOs. Ofgem has taken a pragmatic approach to the Bespoke Outputs and has sought to raise performance across the sector to the level achieved or aspired to by NGN and, whilst no longer Bespoke Outputs, much of what Ofgem proposes is in line with NGN's BP.

#### CVP consultation questions

##### ***NGNQ5. Do you agree with our proposals on CVPs? If not, please outline why.***

We have commented on Ofgem's position on CVPs in the Core document earlier.

Where additional information has been provided by the Company to substantiate its claims that projects genuinely demonstrate added value, we request that Ofgem reconsider those as well as any that are consistent with other companies' CVPs.

##### ***NGNQ6. Do you agree with our proposal to accept the CVP for Enhanced Repair for Gas Escapes?***

Yes, we support this but request that the reward calculation is reconsidered given the huge difference in NGN's proposed financial impact methodology.

#### Common UMs consultation question

##### ***NGNQ7. What are your views on the baseline values for the Tier 2A iron mains volume driver?***

We commented on this earlier in response to GD Annex questions. These are in line with NGN's proposals.

#### Bespoke UMs consultation question

##### ***NGNQ8. Do you agree with our proposals on the bespoke UMs? If no, please outline why.***

We have commented earlier in the GD sector section.

The CEG supported NGN's proposed bespoke UMs in our report (December 2019) as appropriate given the information available at the time.

#### Innovation consultation question

##### ***NGNQ9. Do you agree with the level of proposed NIA funding for NGN? If not, please outline why.***

We agree with Ofgem's decision to award the full amount requested by NGN for NIA projects. However, this is dependent on a satisfactory reporting framework – and we reiterate that Ofgem and the companies collectively need to agree this as soon as possible to allow NGN to commence detailed preparation of its proposed projects, engage the necessary stakeholders and start to undertake the research. Given the uncertainty around longer-term impacts of COVID 19 on vulnerable households Ofgem



should consider increasing this allowance if necessary and where a strong case is made that it will lead to meaningful customer impacts.