

3 September 2020

## **SGN CEG Response on Draft Determination Consultation**

Dear Akshay,

As a CEG we are pleased that Ofgem has formally recognised (at 3.14 of Core Document) that the business plans have been improved through the CEGs' involvement and your own comments on the call on 9 July reinforced that message. However we do have a real concern as a CEG that a number of the areas where we pressed SGN hard to get it to change its approach, in line with consumer and stakeholder views, have been rejected or made light of by Ofgem. This risks both undermining our credibility with SGN (putting the focus back on what the regulator wants not what consumers want) and ultimately calling into question the value of the enhanced engagement process, including the significant consumer and stakeholder research that SGN undertook.

We have set out our main areas of concern below and have attached an annex with responses to individual questions where we have a particular contribution to make.

### **1) Balancing competing priorities**

As a CEG we scrutinised the extensive consumer research which SGN undertook to understand consumers' priorities, their willingness to pay for enhanced outputs and the overall acceptability and affordability of the Business Plan. Based on that evidence we were supportive of where SGN landed with their Plan in terms of the balance between bill reduction and delivery of outputs (although we noted that the cost of innovation funding was not included in the bill impacts). Our sense is that Ofgem have placed a much stronger emphasis on short term bill reductions and we are concerned that this is not informed by any consumer evidence.

At a time when the cost of capital is extremely low and there is an emphasis on the need for investment to support an economic green recovery, there would seem to be a strong case for bringing forward planned expenditure. While the effects of Covid-19 will leave some customers struggling to afford their energy, the evidence from SGN's updated acceptability testing is that that has not led to a material shift in how consumers make these tradeoffs. We would urge Ofgem to ensure that its Final Determinations are grounded in evidence of what consumers actually want not what Ofgem thinks they want. Where Covid-19 has led to affordability challenges this would be better addressed by an increase in the targeted help available through UIOLI funding.

### **2) Biomethane (including SIUs)**

This was an area where the CEG had repeatedly pressed SGN to be more ambitious, motivated in large part by our focus on "future consumers" and the strong steer from consumers about the need to reduce carbon emissions in the short term as well as looking ahead at how to meet net zero.

Reflecting feedback from biomethane producers we stressed the need to focus not just on the number of biomethane connections but the volume of biomethane able to be injected, in particular during the summer months when demand on the system is lower. This would

avoid the need for “flaring” of constrained-off gas which seems an unacceptable waste as well as being environmentally damaging. Addressing injection capacity also fundamentally impacts the business case for producers and hence the level of connections.

We are disappointed that Ofgem does not seem to see this as an important area – or indeed to acknowledge the issues at play - and gives no recognition to SGN for having stepped up in this area and, as we read it, being more ambitious than other GDNs.

In terms of metrics, Ofgem has rejected SGN’s proposal that the total amount of biomethane capacity should be an ODI-R. While we recognise absolutely that the wider policy will be a critical driver of connections in this area, we still see the GDNs as having an important role to play in making biomethane connection easier or harder for producers. Ofgem argue that the level of connections will continue to be reported. However it needs to be made clearer that this is also about the volume of gas injected at existing sites (as Ofgem appeared to accept in the Sector Specific Methodology decision). This absolutely sits with the networks as an issue to be dealt with. While of course SGN can report this as a KPI to its stakeholders it will have little impact if the sense is that this is not a priority for Ofgem.

On a more positive note the proposed extension of the GSOPs to cover green gas entry should in theory help producers looking to connect or to increase their capacity by ensuring a clear and consistent timeframe for responses. However we are aware that these projects will vary in complexity and are therefore unsure how workable a mechanistic process like GSOPs would be or how the proposed service standards compare with what is currently being achieved. If Ofgem are persuaded by the GDNs that this is not workable then we would suggest that, as a minimum, some additional reporting standards are introduced.

In terms of specific propositions, Ofgem has rejected SGN’s proposal for three trials on improved access for biomethane while accepting the proposal to rollout that technology, which we welcome. We hope that the rollout funding will be sufficient to also cover the initial trials. Ofgem has also rejected the proposed reopener for CCS for biomethane which is an opportunity that SGN are still exploring. While we do not have a view on the merits of this specific proposal, it is not clear to us that any of the formal uncertainty mechanisms or innovation funding could be used for this sort of project where the business case is likely to become clearer through the GD2 period in what is a fast changing area but where the focus is short term carbon emissions not the 2050 net zero target. We would welcome confirmation that the scope of these mechanisms would include such initiatives.

Ofgem has also rejected the idea of doing feasibility studies for using biomethane in the SIUs and have just treated the SIUs as part of overall totex. Having visited one of the SIU sites, members of the CEG pressed hard for SGN to find more creative solutions for these stand-alone networks (which also seemed consistent with [previous Ofgem correspondence](#) on the SIUs). We were therefore very disappointed in the way this initiative was dismissed.

In summary, we are concerned that Ofgem does not acknowledge the important role that biomethane can play in reducing emissions in the short term and are focussed primarily on the solutions for 2050. Ofgem has signalled that it will take account of the sixth carbon budget in reaching its final determination and we hope that this (and the associated need to

meet existing statutory carbon budgets through to 2032) will increase the attention paid to short-term carbon reductions and the role of biomethane.

The CCC envisage a role for biomethane injected into the gas grid through to 2030 and BEIS recently announced the Green Gas Support Scheme, signalling the importance of biomethane in the energy mix. The CCC's recent progress report in fact stated in relation to anaerobic digestion that: "priority should be given to injection of biomethane into the gas grid, in line with BEIS recent 'Future Support for Low Carbon Heat' proposals". The latest FES net zero scenarios acknowledge that while biogas may not feature in 2050 (as alternative uses for bioenergy take priority) it remains a necessary step in the transition. Ofgem should be looking to ensure that the gas networks play their part in increasing the level of biomethane in the system and should be signalling more clearly the importance of action in this area.

### **3) Leakage**

Given that leakage accounts for around 95% of SGN's total carbon footprint we had pressed SGN to focus on steps they could take to tackle leakage as part of efforts to reduce carbon over the GD2 period. In the consumer research SGN undertook on their EAP, the absolute top priority for consumers was for SGN to tackle leakage. As a result, we had pressed SGN hard to be creative in finding new ways to address leakage (beyond repex which is discussed below).

We are therefore very disappointed that Ofgem has rejected the request for funding for the rollout of the innovative stent bags and the high volume gas escapes toolbox which together were expected to save 4.7ktCO<sub>2</sub>e in GD2. We were also disappointed that Ofgem has not acknowledged SGN's commitment to reduce third party damage (a source of unplanned interruptions and leakage) or to build on its already high performance on repairs within 12 hours. Ofgem has provisionally agreed to fund a pilot project on active pressure management, which we welcome, but this is subject to SGN making clear why this cannot be funded through the ODI-F mechanism that exists.

This assumption that the current ODI-R and ODI-F should be adequate to drive action on leakage misses the point that the metrics around leakage are modelled and hence the incentives only give credit for factors that are built into the model (essentially as we understand it repex, MEG and average system pressure). We had pressed SGN to identify actions that could have a material impact on leakage but that may not be captured by the current model. We would also have liked further work to be done to quantify these going forward and the message about improving measurement also came through SGN's expert roundtable on environmental issues. We would have expected Ofgem to support such a move to improve measurement in a critical area which accounts for the overwhelming majority of the GDNs' business carbon foot print.

### **4) Accelerated repex**

As set out in the CEG report, this was for us a totemic issue around the weight given by SGN to the results of its engagement. Consumers and stakeholders strongly supported the proposal for accelerated repex and the in-depth stakeholder engagement that was undertaken on the topic was, in our view, exemplary. As a result we pressed SGN to continue to include the programme when they proposed cutting it last summer.

Ofgem gave only brief reasons for rejecting this proposal which were that there is uncertainty around the future of gas and that acceleration of the programme had the potential to exacerbate labour shortages in the gas sector. There is no acknowledgment of the reasons that we considered the proposal to be important which were:

- As flagged by stakeholders it is good practice to build in contingency for hitting the 2032 deadline. The example was given by one local authority stakeholder of the risk of something like foot and mouth causing disruption to plans – which in the light of Covid-19 seems quite prescient. The point was also made that labour supply is likely to get tighter as all GDNs near the end of their mandatory programmes and also that phasing the work avoids a “cliff edge” for contractors at the end of the programme.
- As well as these common sense points there was strong support for an acceleration from an environmental perspective given that if the work needs doing at some point doing it sooner rather than later will mean lower cumulative carbon emissions (and will facilitate achievement of statutory carbon budgets).

Since the Business Plan was submitted Ofgem has signalled that it will be asking the HSE to carry out a review of the IMRRP programme given the uncertainty around the future of gas. If the 2032 deadline is changed then clearly that would affect the business case for accelerating work which otherwise legally has to be done (and hence SGN only needed to consider the question of timing). However, Ofgem is proposing a re-opener to deal with changes in HSE policy which would allow any outputs to be changed in the event that the legal requirements change. Beyond that, we cannot see why the uncertainty around the future of gas affects the case for accelerated repex while the safety requirements remain in place.

Clearly there are now question marks around the feasibility of the full accelerated repex programme given the impacts of Covid-19 in GD1 which have not yet been fully worked through. However given that Ofgem is anyway proposing a volume driver mechanism for repex to take account of the mix of work (including unit costs for different sizes of pipe etc) there would seem to be a strong case for allowing flexibility for SGN – and indeed other GDNs – to carry out some level of repex beyond the “flat line” run rate if in due course that looks to them to be the most efficient way of meeting their 2032 target.

We are aware that for SGN the bigger concerns from a safety perspective are actually around replacement of steel pipes (where there are also arguments around levels of customer disruption with repeat failures), dynamic growth in iron mains replacement and replacement of some larger pipes. We have not scrutinised these proposals to the same extent but given the safety implications and the wider benefits in terms of reduced leakage – both critical consumer concerns - we would ask Ofgem to consider carefully the additional evidence that SGN will put forward to support the case for this work.

## **5) Environmental Action Plan Reporting**

More generally on the Environmental Action Plan we would have liked to see Ofgem acknowledging where it felt companies were being more or less ambitious. In some cases, such as on the Business Carbon Footprint, the different measures used by companies make this comparison hard but it is disappointing that Ofgem have only now requested the information on a consistent basis. Ensuring consistent metrics and reporting is essential to

enable us as a CEG to understand the relative ambition levels which is important where Ofgem is relying on reputation as a driver.

Ofgem seem to view it as adequate that companies have “science-based targets” for reducing their carbon footprint (excluding leakage). However, as we flagged in our report to Ofgem, that framework continues to evolve. Companies can now sign up for different levels of ambition<sup>1</sup> – either to meet the 1.5 degree target (consistent with net zero) or to meet the original less ambitious target that Ofgem quote, aligned to the Paris agreement “to limit global warming to well-below 2°C above pre-industrial levels and pursue efforts to limit warming to 1.5°C”. Our understanding is that SGN are working towards the more ambitious target. We would ask that Ofgem clarifies the different targets that companies are working towards so it is clear if some are being more ambitious than others.

We are pleased that in general, aside from the points above, Ofgem seems to have agreed to the funding requested for EAP initiatives. However, we do have some concern that these are not being treated as PCDs but are being left to be covered through the reputational tool of the AER. While we do believe that SGN are committed to the wider sustainability agenda – reflected in the fact that they have established a new ESG Board committee to track progress - we recognise the temptation, if the overall price control is very tight, for them to cut back on projects that are not absolute regulatory requirements.

Having a UIOLI fund for EAP actions would be another way of ensuring that monies are not simply retained by the company as “efficiency” savings while allowing a bit more flexibility in identifying the most cost effective means of achieving carbon savings and also being potentially less onerous than multiple PCDs (which seems to be Ofgem’s concern).

As a CEG we expect to continue to play an enduring role which will include scrutiny of the extent to which EAP commitments have been met but ultimately our influence is limited. If GDNs get the impression (as they might from the draft determination) that Ofgem is not particularly concerned about performance in this area then it will be harder for CEGs to hold them to account.

## **6) Climate Change Adaptation**

We agree with Ofgem that this does not naturally fit in the EAP and that it is more appropriately considered as an aspect of resilience. However we do not agree that it can simply be viewed as BAU. A bit like cyber security this is an area that needs increasing focus going forwards (as SGN’s stakeholders have consistently made clear and has been reinforced again recently by various Government advisers<sup>2</sup>). As a CEG we actively welcomed SGN thinking about this area despite it not being mentioned in the Ofgem Business Plan Guidance.

Having rejected the proposed UIOLI mechanism it is unclear to us how any specific projects SGN identify are to be funded and we would urge Ofgem to ensure that it is clear about the additional actions that might be needed in future given the impacts of climate change. In

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<sup>1</sup> <https://sciencebasedtargets.org/step-by-step-guide-2/>

<sup>2</sup> [https://www.theguardian.com/environment/2020/aug/15/uk-infrastructure-inadequate-for-climate-emergency-experts-warn?CMP=Share\\_iOSApp\\_Other](https://www.theguardian.com/environment/2020/aug/15/uk-infrastructure-inadequate-for-climate-emergency-experts-warn?CMP=Share_iOSApp_Other)

particular we would be reassured if Ofgem were to test its thinking with the CCC's Adaptation Committee who have particular expertise in this area.

We also note that as part of the ED2 Sector Specific Methodology consultation Ofgem suggest the ENA should establish a 'climate resilience' taskforce to explore the risks from climate change. There would seem to be a strong case for this to extend to other networks not just electricity distribution.

While we see this as a part of resilience rather than the EAP we understand SGN's interest in including it in AER reporting given it will be of interest to environmental stakeholders.

## **7) Approach to social impact**

While the CEG has been keen to see SGN stepping up in terms of the service it provides to customers, the approach that we supported in the Business Plan was one that was flexible to allow the best form of support to be provided to meet individual customer needs against an overall metric of customer satisfaction rather than prescribing particular measures.

We were therefore somewhat surprised that Ofgem has gone down the path of mandating specific actions – the provision of hot water and hot meals for PSR customers, the offer of appointments for purge and relight and the doubling of GSOP compensation. None of these proposals are supported in the draft determinations by consumer evidence but build on initiatives that individual GDNs have elected to pursue (albeit presumably based on evidence from their customers and stakeholders). It is not clear to us that the case has been made for these to be mandated and SGN's own research did not find particular support for them. It is unclear what the point was of carrying out local engagement on these issues if ultimately Ofgem were wanting to put a national framework in place.

The proposal to reduce the timescales for reinstatement under GSOP2 for PSR customers is another example which in our view is not supported by consumer evidence. Moreover, in this case we have concerns about differential service for customers in the same road as well as the efficiency of such an approach. Ofgem argues that "this will help ensure that particularly vulnerable groups of consumers are prioritised for quick restoration of supply". We do not follow this logic as reinstatement is about filling in any holes or trenches that have been dug not about restoring supply.

Finally, where SGN was looking to break new ground was in the use of SROI as a tool for gauging the social value of initiatives – including to ensure that the UIOLI fund delivers outcomes of value for consumers. This was an initiative that we had strongly welcomed. The reframing of the SROI based social value coordination project and the decision not to include a common SROI metric as part of vulnerability ODI-R reporting appear to put a dampener on any initiatives in this area. However we have also just seen the draft guidance around the UIOLI mechanism which actually includes reference to SROI. Bringing these elements together we would like to see Ofgem sending a clearer message around the need for the SROI methodology to continue to be developed through GD2, recognising as well that something similar is being actively pursued by the DNOs for ED2.

## **8) Enhanced Engagement in GD2**

We were very struck that Ofgem did not comment on the proposals that SGN had put forward for enhanced engagement in GD2 (which they were required to include in their plan). We had welcomed a number of aspects of their proposals including their intention to carry out deliberative research on the 10 complex challenges they identified which they had proposed as a bespoke output under the stakeholder engagement ODI-R. While the Core Document states that bespoke engagement ODIs are covered in the company annexes this is not picked up in the SGN annex. We had also made clear that more thought was needed on Local Area Energy Plans and on engagement to improve workforce diversity which SGN had committed to do. Again, if SGN get the sense that these agendas are not important to Ofgem it will be harder for us to hold them to their commitments in this area.

In terms of the enduring CEG role we have responded to the questions Ofgem raise and confirmed that we do see value in the CEG continuing to hold SGN to account for the commitments it has made and to provide a challenge where uncertainty mechanisms are being invoked, testing the level of engagement that has been done. We believe this is best done by individual company CEGs who can be closer to the detail of company plans and ongoing engagement, provided steps are taken to avoid capture. However there could be scope for CEG chairs / members to work together to facilitate cross company comparisons.

In terms of the scope of the enduring CEG role, this has to be dependent, at least in part, on what Ofgem would find useful. We have found it hard to see how our report, or SGN's wider engagement, were taken into account in reaching the draft determination. As indicated in our introductory paragraph, if Ofgem is not evidently heeding our views then our influence over SGN itself will be weakened. In reflecting on the enduring CEG role we would therefore encourage Ofgem to be clearer what value it has drawn from our input to date and hence how we can build on that going forward. There is no point in requiring us to provide, for example, annual reports to Ofgem unless they are going to be utilised.

We hope that these comments are helpful to Ofgem in considering where further work is needed ahead of final determinations. We would be happy to discuss them with you directly or at the proposed open meeting.

As a final reflection we would note that as a CEG we found the Ofgem documents quite hard to navigate. We recognise that there is a significant level of information that has to be conveyed but if Ofgem is looking for stakeholders (beyond the companies) to engage with the detail of the proposals then it is important that the documents are accessible and facilitate that engagement. The webinars have provided helpful overviews but the documents themselves remain important.

Yours sincerely

Maxine Frerk  
Chair SGN CEG

## SGN CEG Response to Questions in the Draft Determinations

### Core document

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 invite stakeholders' views on whether the one Group per company set up is likely to deliver as effectively during the price control period as it did during the Business Plan development stage or whether a single Group per sector (ie transmission, gas distribution) may be more suitable to achieve the right outcomes.

A1 Building on the role that the Groups have played in the process to date we believe their role on an ongoing basis should be based around:

- providing a framework for ongoing **challenge to the companies**, building on and adding value to the knowledge, relationships and culture change within companies that has developed through the RIIO 2 process; and
- providing formal and transparent **assurance to Ofgem** both on the delivery of commitments in the Business Plan and on new proposals brought forward under uncertainty mechanisms, of which there seem likely to be an increased number during the upcoming price control period.

We believe this is best done by individual company CEGs who can be closer to the detail of company plans and ongoing engagement, provided steps are taken to avoid capture. It also allows account to be taken of particular local needs and issues which we see as of particular importance in the Scottish context. However there could be scope for CEG chairs / members to work together to facilitate cross company comparisons and potentially to engage with equivalent bodies in other sectors to share learning. The more Ofgem wants to move to having common national standards rather than locally determined outputs then the more important that co-ordination becomes.

In terms of the scope of the enduring CEG role, this has to be dependent, at least in part, on what Ofgem would find useful. It is important that Ofgem retains an interest in the outputs of the Groups to strengthen our hand as we seek to influence the companies, and to provide a sector-wide perspective.

As we note in our response to Q3 we see one valuable output as being an annual report reflecting on delivery against the commitments and any developments during the year, which we hope that Ofgem would find of value and may also be helpful to other stakeholders. We would also expect to provide our views to Ofgem on company proposals on reopeners where appropriate.

From the draft determinations it is clear that Ofgem is proposing to rely heavily on reputational ODIs and the UIOLI funding for social impact leaves discretion with the companies on how this is spent. It is critical that the companies deliver meaningful outcomes for customers and we believe the Groups are essential to ensure firms are designing and delivering services that reflect real customer need, based on high quality engagement. The Groups would also play a valuable role in providing scrutiny over the customer outcomes that companies have delivered in those areas, enabling stakeholders to put the companies' performance in perspective and make meaningful comparisons between companies. In SGN's case they are putting in place steering groups for both their social and environmental commitments. The CEG would be represented on those groups and would provide assurance that the processes put in place for UIOLI spend deliver value for customers.

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

A2 Our role, as with the Business Plans themselves, should be to test that, where appropriate, the proposals are underpinned by high quality engagement and reflect the needs and wants of customers and stakeholders, including reviewing any new engagement that is undertaken to support the proposals. This may not be relevant in all cases (eg for volume drivers or more technical reopeners such as smart meter costs) and needs to be done proportionately to avoid creating delays in the process. Also, as with the Business Plans themselves, the Groups can provide a strategic challenge on key assumptions for example but do not have the resources to carry out the level of technical and cost scrutiny that the Ofgem team do.

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?

We believe that there would be value in Groups producing an annual report reviewing the performance of the company on their Business Plan commitments. We would expect this to be customer-centric in that it would focus on the issues that we know are of particular concern to customers (present and future) and stakeholders – including environmental issues. We would not expect the report to be read by individual end consumers but it would be of value to consumer representatives and other stakeholders, and give Ofgem an ongoing benchmark against which to assess progress within individual companies and across the sector.

While there is clear value in the CEG annual reports sharing some common elements to facilitate an overview of sector-wide progress, we would encourage Ofgem to leave some flexibility in the precise form of the report so that we can establish what would be of most value to all of the stakeholders who would benefit from them. In particular we have floated the idea that our report could form part of the company annual report which would potentially give it greater profile but may carry risks for our perceived independence.

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?

We think there is real value in providing for continuity of Groups in readiness for RIIO-3. The Groups have built up considerable expertise around both the business and the regulatory framework. Making a link between monitoring of commitments in RIIO-2 and preparing for RIIO-3 also provides an additional incentive on companies to deliver against reputational incentives in RIIO-2 as a failure to do so will impact on their credibility when it comes to RIIO-3.

As Ofgem notes, there does then need to be some refresh of membership both to ensure the right mix of skills and experience going forward but also, crucially, to reinforce the independence of the Group and avoid any perception of capture.

*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?*

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

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?

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?

A8 We agree that monitoring delivery of the commitments in the companies' engagement strategies is an important element of the Groups' role and could be expected to be a part of the annual report referenced above. Clearly this is an area in which the Groups are likely to have a particular expertise and their scrutiny of performance in this area – including challenge to the companies – should be of particular value. We do see a risk if the Groups “work with” the companies too closely that their independence could be compromised. In SGN's case they have a separate Stakeholder Advisory Panel that they would use to help them with early thinking and idea generation so for us this is not an issue. And more broadly we recognise that throughout the process to date all Groups have had to tread a careful line, providing suggestions and challenge without being left having to mark their own homework. We would expect the Groups to be able to manage that balance going forward.

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?

A9 We welcome the efforts by Ofgem to collect information on BCF targets on a consistent basis which we see as essential for this to be an effective reputational incentive. We believe that, as a result of our focus on this area, SGN had set ambitious targets and we would have liked to see acknowledgment of that fact. It remains important that Ofgem shows that it considers these aspects of performance important if Groups are to have influence with the companies in holding them to account for delivery.

We note that Ofgem has chosen to define the BCF as covering scope 1 and 2 emissions excluding leakage. Our understanding is that the Science Based Targets initiative defines scope 1 emissions as including fugitive emissions from operations and as such we would have expected leakage to be included. Indeed, we had encouraged SGN to include leakage in its targets given that is the largest component. We can see the case in terms of transparency for splitting leakage out but would encourage Ofgem to require reporting on both bases. Clearly the scope of the science-based targets has to be consistent with the definitions used by the science based targets initiative itself.

Also, as we flagged in our report to Ofgem on SGN's plan, the definition of science-based targets continues to evolve. In the draft determinations Ofgem say '*Greenhouse gas reduction targets are considered 'science-based' if they are in line with the latest climate science advice on what is needed to meet the goals of the Paris Agreement - to limit global warming to well below 2°C above pre-industrial level and pursue efforts to limit warming to 1.5°C*'. However targets set on that basis would not be in step with the UK's statutory 1.5 degree net-zero commitment by 2050 which goes beyond the Paris Agreement. The leading advisory body on science-based targets now [encourages](#) companies to sign-up to targets consistent with 1.5 degrees, although targets in line with the original

definition are still accepted. Ofgem should require companies to make clear in their BCF reporting which level of ambition they have signed up to in terms of their science-based targets.

More generally we see the EAP commitments as an important part of the package, noting the increasing importance that consumers attach to environmental issues. We would have liked to see the EAP commitments treated as price control deliverables so that we could be confident that they would be delivered or that, if not, the money would be returned to customers. While we believe SGN is committed to delivery of its EAP we are aware that financial pressures could lead to savings being sought in areas that are not formal requirements. In such circumstances reputational incentives alone may not be sufficient. That said we stand ready to use our position as a CEG to ensure, as far as we can, that SGN do continue to focus on these issues and deliver against their commitments.

*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.*

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

A11 We said in our report that we would welcome Ofgem applying further scrutiny on efficiency, recognising that we do not have the technical expertise but that cost is a central issue for consumers. We are slightly surprised by the scale of the overall efficiency challenge imposed by Ofgem given the assurance that SGN had undertaken on its costs and that as an organisation they appear to be relatively efficient historically. We had welcomed SGN's wide use of CBAs to justify individual projects and are concerned if this has led to them getting penalised as part of the BPI.

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

A12 Our only concern is that Ofgem are able to make timely decisions on re-openers to avoid any delays to what might be essential investment.

*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?*

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

*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?*

*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?*

*Q17. What are your views on including the delivery of outputs such as: CAF outcome improvement; risk reduction; and cyber maturity improvement, along with projects-specific outputs?*

*Q18. Do you agree with our proposal for the Non-operational IT and Telecoms capex re-opener?*

*Q19. Do you agree with our approach to using a re-opener mechanism for changes to government physical security policy?*

Q20. Do you agree with our approach regarding legislation, policy and standards?

A20 We agree that there is significant uncertainty around legislation, policy and standards which could impact the GDNs and a re-opener to deal with these makes sense.

Q21. 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?

A21 We would encourage Ofgem not to set too high a bar for what it considers “known and justified” needs. There will always be a level of risk and uncertainty in the investments that need to be made and simply waiting for the need to become clearer risks deferring investment to the extent that net zero may not be achieved. Cost is obviously important but there are valid trade-offs to be made around increasing the prospects of net zero being met and the cost. “Lowest cost” may not achieve that balance and in particular lowest cost now may well lead to costlier interventions in the future. In thinking about “lowest cost” Ofgem need to ensure they are considering the impact on future users of the network not just current customers.

Q22. 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?

A22 Ofgem have suggested that some of the proposals they have rejected eg on biomethane CCS could be funded through other mechanisms. We would appreciate confirmation that these mechanisms could provide funding for initiatives on biomethane that result in material carbon saving in the short to medium term (and noting that biomethane is included in the CCC and FES pathways) even if biomethane is not expected to be part of the 2050 net zero energy mix.

Q23. Do you have any views on our proposed approach to a Net Zero reopener?

The key requirement is that decisions can be made in a timely way and further detail is needed on how Ofgem will achieve this and the timescales it is committing to. We note that only Ofgem would be able to trigger the reopener but it is presented as a route that SGN could use for funding some of the decarbonisation projects that it proposed but which were rejected. It is unclear how this is meant to work and what confidence we can have that any such proposals would fall within the scope of the reopener.

Q24. Do you agree with our proposals for the RIIO-2 Strategic Innovation Fund?

Again this is presented as a potential route for funding some of the decarbonisation projects that SGN put forward but that were rejected. Given that Ofgem will be setting out the “challenges” that

will be the subject of SIF funding it is unclear what confidence we can have in this as a route for funding initiatives that SGN may identify.

*Q25. 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?*

*Q26. Do you agree with our approach to benchmarking RIIO-2 NIA requests against RIIO-1 NIA funding?*

Given the scale of the net zero challenge one might have expected the level of funding to be commensurately higher than in RIIO 1. A more flexible arrangement with, for example, the potential for a further tranche of funding to be allocated in period if required, would seem to be in the spirit of adaptive regulation. The priority is that the funding delivers real benefits for consumers and Ofgem's proposed changes are aimed at addressing this.

*Q27. Do you agree with our proposal that all companies' NIA funding should be conditional on the introduction of an improved reporting framework?*

*Q28. What are your thoughts on our proposals to strengthen the RIIO-2 NIA framework?*

*Q29. Do you have any additional suggestions for quality assurance measures that could be introduced to ensure the robustness of RIIO-2 NIA projects?*

*Q30. 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?*

A30 Agreed

*Q31. 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?*

*Q32. Do you agree with our proposed position on late competition?*

*Q33. Do you agree with our proposed approach on early competition?*

*Q34. 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?*

Agreed in relation to SGN

*Q35. Do you agree with our rationale for why NGET and NGGT should be considered to have failed Stage 1 of the BPI?*

*Q36. Do you agree with our rationale for why Cadent and NGN are considered to have passed Stage 1 of the BPI?*

Q37. Do you agree with our overall approach regarding treatment of CVP proposals?

A37 We have struggled with what Ofgem has been trying to achieve with the CVP. We had understood that the overall aim was to reward ambition in the plans and are concerned that the focus on individual initiatives with a “wow” factor does not do that. In our view ambition in a particular area can be demonstrated through stretching targets, a consistent focus and a combination of initiatives, underpinned by strong engagement, and should not just be about one-off original ideas. While we support all the elements that SGN had put forward in its CVP we absolutely recognise that they are not generally stand-out proposals and reflected more an attempt by SGN to quantify the value that its plan overall delivered for consumers which, it is now clear, was not what Ofgem were looking for.

However we do believe that there are elements of SGN’s plan where they showed real ambition that reflected the views and needs expressed in the extensive customer engagement that they have undertaken – on their proposals for future engagement around complex issues, on their plans to make use of SROI to assess the value of social interventions, on their Environmental Action Plan and commitments around leakage and biomethane to reduce carbon emissions in GD2 and on their whole systems thinking around the use of hydrogen. The fact that the CVP mechanism does not allow for such ambition to be rewarded appears to us to be a weakness in the current arrangements.

The fact that Ofgem does not call out what it sees as the relative strengths in the different plans means that there is not even a reputational benefit in being more ambitious.

*Q38. Do you agree with our proposed clawback mechanism to treat received CVP rewards?*

*Q39. Do you have any views on the interlinkages explained throughout this chapter?*

*Q40. Are there other interlinkages within our RIIO-2 package that you think are relevant to the three pillars identified in this chapter?*

*Q41. 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?*

*Q42. Do you have any views on the proposed pre-action correspondence, including on the proposed timing for sending such to Ofgem?*

Q43. 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?

A43 We recognise the potential for Covid-19 to have significant impacts on the companies’ plans in potentially unpredictable ways. We would encourage Ofgem to consider carefully any proposals put forward in this space.

## GD Sector Document

### Output 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.

AGD1 We do not understand the rationale for amending GSOP2 to provide for reinstatement work to be done in 3 days for PSR customers. Ofgem says "This will help ensure that particularly vulnerable groups of consumers are prioritised for quick restoration of supply". This does not make sense as reinstatement is about filling in the holes not about restoration of supply. There are clearly efficiency arguments for doing all the reinstatement work in a road at the same time and a risk of wider customer dis-satisfaction if reinstatement work is visibly done for some customers before others.

The customer satisfaction standards that have been set are extremely challenging. Even maintaining a steady score would require ongoing investment as customer expectations continue to rise. Moreover it is unclear what effect (if any) Covid-19 will have on levels of satisfaction. Ofgem should consider carefully any further evidence presented to ensure it is setting targets that are stretching but not impossible to achieve, with incentives calibrated taking account of customers willingness to pay.

SGN's customers were clear that, while they expected SGN to maintain existing high levels of customer satisfaction and recognised the effort this would require given rising expectations, they did not support significant further investment in this area. While as a CEG we place high value on the importance of incentivising ongoing improvements in customer services, it is important that targets take account of customers' views and willingness-to-pay for further improvements. It would be an anomaly if the targets set by Ofgem required companies to depart significantly from the findings of the extensive customer engagement that they were encouraged to undertake.

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

AGD2 The metrics seem reasonable but we would have liked to see encouragement for the companies to continue to develop a common framework for SROI reporting as the DNOs are being encouraged to do in the ED2 SSM in order to ensure a focus on outcomes not just outputs.

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?

AGD3 We believe a national event is helpful to share learning and to provide a reputational incentive for companies to be ambitious in the proposals around vulnerability. Of course companies will also need to do regional events with local partners who they are dependent on for delivery but this should be BAU.

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

AGD4 We had always understood that the PCD was able to be flexed with volumes and it was this structure that gave SGN the confidence to put forward the relatively ambitious proposals that it did for FPNES given the high level of policy uncertainty that exists in this space. Making this formally a volume driver probably makes this flexibility clearer.

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?

AGD5 As a CEG we had not seen the need for prescriptive standards in this area and were keen for SGN to focus instead on providing appropriate support taking account of the individual customer needs (which is in effect what the evidence presented by Ofgem at footnote 34 seems to say). As such if the GSOP is to be amended we would be comfortable with a 48 hour exclusion and have not seen any evidence to suggest this GSOP should be extended to cover other interruptions. We remain concerned that the proposal has been driven by Ofgem rather than by consumer evidence.

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?

AGD6 As evidenced at Biomethane developer/stakeholder workshops, there is concern regarding capacity studies & connection quotations timescales & undue bureaucracy. Information on capacity is a first critical step in proving the viability of a project. We can therefore see potential benefit in using GSOPs to achieve reduced timeframes. However we are aware that projects are often bespoke and can vary in complexity and hence a rigid tool like GSOPs may not be workable. We are also not clear what the proposed targets would be and how they compare with current performance in the sector. As an alternative we would suggest Ofgem at least requires companies to report on their performance in what is a critical area.

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?

AGD7 Based on the joint GDN research that was carried out we had not felt there was a case for requiring appointments. Customers seemed to be more concerned about being kept updated. Monitoring the provision of appointments for purge and relight will help shine a light on different practices and should help drive improvements where needed.

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?

AGD8 We had strongly supported SGN's proposal in this area which we saw as being in part about SGN taking on a leadership role in this space. SGN's customers expressed a clear, consistent and

strong view on the need for not simply collaboration but leadership around streetworks to minimise the negative impact on customers, which has long been a source of significant frustration for customers. We understand that Ofgem considers it more appropriate for the proposals to be progressed together, working with the GLA, and we appreciate there may be value in this. We do, however, urge Ofgem to ensure that the final proposal reflects the needs and priorities reflected by customers of both SGN and Cadent and, critically, creates sufficient incentives for effective and efficient leadership around collaboration on streetworks. We have not looked in detail at the Cadent proposal but had seen this leadership element as a key strand of SGN's proposal. We are also keen that the focus that the SGN proposal had on the use of social value metrics to establish a value for collaboration is not lost.

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

AGD9 The shrinkage financial incentive should be designed to ensure that companies take account of the cost of carbon in taking decisions which may affect leakage levels. The value of the incentive should reflect the higher Global Warming Potential of methane and use a cost of carbon that is consistent with achieving net zero. Companies should be rewarded / penalised for any reduction / increase in methane compared to current levels.

We would agree with Ofgem that the benchmark level should be set at the close off figure for GD1 given that will have determined the rewards earned in GD1.

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

AGD10 While we understand the importance of consistency, we had pressed SGN to explore options for reducing leakage even if they would not be captured by the model and hence would not be rewarded under the current framework. In our view the incentive should have flexibility to allow GDNs to be rewarded for other actions that they can demonstrate reduce leakage but which are not captured in the current model (which is used for other purposes in terms of allocating costs among shippers and hence can be slow to change).

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

AGD11 We would be concerned about the use of a deadband if it created a disincentive on companies to work to reduce leakage. It is not clear to us that it is needed.

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

AGD12 We have provided our comments on the SGN elements in our response to the SGN document. We would have liked to be able to get a clearer picture from the GD report as to the relative ambition of the different companies' EAPs, to help us in judging how ambitious SGN's EAP was. The GD report does not facilitate this except in areas where it is very clear-cut (ie companies have or have not included an element) – although our sense is that SGN's plan was ambitious

compared to others. In thinking about how to ensure the EAP/ AER is an effective reputational incentive we would encourage Ofgem to think about how to facilitate comparisons.

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

AGD13 We would have liked this to be included as a formal ODI-R to reinforce the importance attached to it. However our primary concern is that the measure used should reflect the volume of biomethane injected not just the number of connections. Networks action to avoid having to constrain off biomethane during summer months is a major concern among producers and is within networks control. Having consistent metrics across companies would then be helpful in enabling us to monitor relative performance.

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

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

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

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

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

AGD18 We understand why Ofgem is looking to adjust allowances to reflect the mix of work undertaken. What we cannot understand however is why Ofgem will not make any adjustment if volumes are exceeded. Some flexibility in this would allow companies to programme their work efficiently over GD2 and GD3, assuming that no changes are made to HSE requirements in the interim. If changes are made then Ofgem has provided for a reopener.

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

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

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

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

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

*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 sector?*

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

Approach to Cost Assessment Consultation Questions

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

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

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

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

Model Selection Consultation Questions

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

*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)?*

Opex Consultation Questions

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

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

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

We are concerned as set out elsewhere in this response about the reductions in repex workload and that no account appeared to have been taken of stakeholder input and some of the arguments they put forward. Ofgem has employed a 16 year payback period without any particular rationale. While we recognise the issues with long payback projects we had been supportive of the decision tree approach that SGN had developed to better understanding stranding risks (in the context of a front loaded 45 year payback). This would provide support for rather longer paybacks in some cases. That said we understand SGN will be submitting more focussed proposals which have shorter paybacks which we hope that Ofgem will support.

*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?*

Capex Consultation Questions

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

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

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?*

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

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

## Uncertainty Mechanisms consultation questions

*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?*

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

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

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?

AGD46 Provided Ofgem is satisfied that the bespoke issues are covered by the common re-openers a common approach is clearly to be preferred.

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

AGD46 Our view is that the costs of these projects should be socialised given that they are, at this stage, very much about learning and demonstrating the potential of hydrogen, from which all GDNs will benefit.

While these projects are likely to need some changes to policy, our sense is that detailed policy development is likely to progress in parallel with the projects themselves. If the companies have to wait for changes to rules around gas injection to be implemented before they can start work, overall progress on net zero will be delayed. As such we do not see that policy change should be a trigger for allowing these projects which are in part aimed at informing that policy process. This clearly has implications for the choice of reopener mechanism that Ofgem uses for these projects.

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

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

AGD49 As set out in our report, we support the use of a volume driver for new domestic connections as Ofgem are proposing, reflecting the significant uncertainty that applies in this area dependent on the impacts of government policy and local planning rules about gas in new homes.

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

AGD50 Although not triggered in GD1 a common “Large Loads” re-opener is required given the potential numbers of peaking plant projects.

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

GDQ52. Do you agree with our proposal to continue with a smart meter rollout reopener?

AGD52 Yes

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

AGD53 Yes

## SGN Questions

SGNQ1. Do you agree with our proposals on the bespoke ODIs? If not, please outline why.

Bespoke social value incentive (rejected) – We were extremely disappointed that this was rejected, especially given the strength of the messaging on this from SGN's customers and the very high quality engagement that SGN undertook with renowned experts in measuring social value to develop and refine the proposal. Provided that the combined incentive working with Cadent can be developed in a way that reflects the needs of both companies' customers and creates the right incentives for efficient and effective leadership around collaboration this should deliver what customers care about. One element of the proposal we had particularly welcomed was the use of SROI methodology and as set out in our response to GDQ2 we believe Ofgem should encourage the GDNs to develop SROI reporting.

Reduction in shrinkage from theft and own use (rejected) – We were disappointed that this was rejected but recognise that this could reasonably be covered in the BCF reporting provided Ofgem's definitions aimed at ensuring consistency allow for this.

Biomethane capacity (rejected) – We were very disappointed that this was rejected as it was an area that we had pressed SGN hard to be more ambitious on. As set out in our response to GDQ13 the focus needs to be on the volume of gas injected not just the number of connections. Inclusion of reporting in the AER could help, in particular if done on a consistent basis (and relative performance will also help reveal how far this is simply driven by policy or whether individual network actions are also having an impact).

12 hour standard for repair (rejected) – We were disappointed that this was rejected and are struggling to understand how this sits with Ofgem's decision to award NGN a CVP reward for effectively a similar proposal. Ofgem argues that there are strong environmental and consumer benefits in NGN reducing the proportion of repairs that are completed within 7 days or within 28 days but does not seem to see any value in companies even reporting the proportion repaired in 12 hours. This seems perverse to us and we had welcomed SGN's focus on the 12 hour repair target as part of its response to our challenge to them around leakage (even if their target was only to maintain their industry leading performance). Ofgem refers back to its decision in the SSMD to drop the 12 hour repair metric but at that point it was seen as essentially a safety target which all companies were comfortably meeting. The reason that SGN and NGN have proposed including it now as an ODI is driven by environmental considerations. We would therefore argue that there is a strong case for reinstating this as a common ODI – or alternatively for requiring all GDNs to track the related measures proposed for NGN's CVP, given Ofgem's recognition that this is an important area. Introducing a common ODI-R in this area would also help provide assurance that NGN's targets do represent an improvement on what other GDNs are doing and hence merit a CVP.

Stakeholder Engagement – We were very disappointed that Ofgem did not even comment on SGN's proposal for an ODI-R around its engagement on complex challenges which we considered to be stretching and ambitious. During the business planning process, the CEG was particularly impressed by the consideration that SGN had given to its customer engagement. In particular, we supported its ambition for and commitment to ongoing progress and evolution in this area to embrace new methods and ensure that engagement both reflects stakeholders' views and builds their capacity to respond to some of the more complex, longer-term challenges that energy companies are facing. In our view, SGN's proposals on engagement on complex challenges would result in a significant step-change in stakeholder engagement and add considerable value to the company and its stakeholders.

SGNQ2. Do you agree with our proposals on the bespoke PCDs? If not, please outline why.

We welcome Ofgem's proposal to accept the PCDs on biomethane improved access, intermediate pressure alignment and remote pressure management (subject to further information from SGN).

Of the PCDs that have been rejected those where we have the greatest concerns are:

Proactive steel and accelerated repex – as set out in our cover letter, repex was a totemic issue for the CEG with very strong customer and stakeholder support for action in this area to address leakage and to mitigate a clear safety risk (as well as making the network hydrogen ready). Our understanding from SGN is that replacement of steel mains is the more important of these as levels of leakage and customer disruption are higher. We therefore encourage Ofgem to reconsider their decision on proactive steel in the light of updated evidence SGN may provide. On accelerated repex we cannot see why Ofgem cannot at least allow some flexibility between GD2 and GD3 through a limited volume driver given that it has already put the mechanics in place to deal with variations in the mix of pipe diameters. We set out in our cover letter the benefits of such an approach.

Stent bags and HVGET – these proposals were introduced as a result of us pressing SGN to find more innovative solutions to tackle leakage and we are therefore very disappointed that they have been rejected. While Ofgem suggests NIA funding may be an option we are not clear whether this is actually the case as the technology is essentially proven. We would prefer a clear PCD.

SIUs – as set out in our cover letter the CEG had visited one of the SIUs and we had pressed SGN to be more creative in the way it approached the SIUs which are currently very costly to serve but present valuable opportunities for innovation as stand-alone networks. While we recognise the cost of the biomethane surveys is immaterial and that Ofgem has included wider SIU spend within totex, we are concerned about Ofgem's dismissal of the SIUs as a specific challenge that SGN needs to address. We find this particularly surprising in the light of previous Ofgem correspondence on the SIUs<sup>3</sup> in which Ofgem said *"In the next price control review, RIIO-GD2, we will want to return to the longer term solution for supplying the SIUs. We will expect you to include clear plan for the implementation of a longer term solution for the SIUs as part of your RIIO-GD2 business plan submission. This should analyse in detail other options for supplying energy to these locations including non-gas solutions, building on the work that you have done so far. The plan should also demonstrate that you have fully engaged with stakeholders on all potential options."*

Climate change adaptation – While Ofgem has said it will fund the survey, it has rejected the capex that might be needed to address issues identified on the grounds that this should be covered by normal totex. We believe that climate change creates new risks for resilience that need specific consideration (as is proposed in the SSM for ED2). We accept that SGN has not yet made a case for this expenditure but saw inclusion of the spend as a PCD as a way of providing for investment that may or may not be needed and could be clawed back if not. The recent incident near Alloah is an example of the way that climate change can impact on the gas distribution networks and needs to be taken seriously.

Aside from these there are a number of other PCDs where we are pleased that Ofgem has said it will provide funding but where it is not proposing to treat them as PCDs (biodiversity, installation of PV, MOB risers). We would have liked these to be treated as PCDs to ensure they are delivered and to

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<sup>3</sup> <https://www.ofgem.gov.uk/ofgem-publications/87824/siusolutionlettertosgn19may2014-pdf>

send a signal about the importance that Ofgem attaches to action in these areas. In particular the riser surveys (and by implication the isolation valve surveys) were seen by consumers as crucial safety actions in the context of Grenfell.

On vehicles we recognise that it makes sense for Ofgem to collect information from across the companies and to consider a common ODI. However we would note that again we had pressed SGN to be ambitious and not to only include vehicles for which there is a known solution now, recognising that technology will develop over the RIIO-2 period. We therefore encourage Ofgem not to set the target too low in this area (but with the scope to clawback allowances if appropriate vehicles do not come onto the market).

On DCC membership we agree the case has not yet been made but had suggested that SGN look for the flexibility so that these costs could be included in future given the growing interest from stakeholders in smart meter data to help in local area planning around heat solutions for example. We had thought that a PCD was a way to provide that flexibility with funding able to be clawed back if it was not needed.

SGNQ3. Do you agree with our proposal for SGN's bespoke biomethane technology rollout PCD?

We agree and are pleased that Ofgem has recognised the value in these innovative approaches to support biomethane injection. We trust SGN can find the funding for the trials (eg through NIA) as these are clearly a pre-requisite but have been rejected by Ofgem.

SGNQ4. Should we include Kings Ferry within the Capital Projects PCD, rather than setting a separate PCD?

Agreed

SGNQ5. Do you agree with our proposal for SGN's IP services reconfigurations PCD?

Supported.

SGNQ6. Do you agree with our approach for SGN's Remote Pressure Management PCD?

We agree with the approach. We note that Ofgem has raised the question as to why this cannot simply be funded from the ODI-F on shrinkage and environmental emissions. Our understanding is that this incentive is based on an industry model which is driven by average system pressure that would not therefore reflect the benefits of more dynamic remote pressure management. We trust that SGN can provide the additional information that Ofgem are looking for.

SGNQ7. Do you agree with our proposals on CVPs? If not, please outline why.

As set out in our response to the core document we have concerns with the overall approach to CVPs which has failed to reward ambition across broad areas of the business plan. Of the CVP proposals we believe SGN's EAP, its approach to social evaluation, its ambition on hydrogen and leadership on GSMR are all areas where we believe SGN is doing more than other GDNs and hence in our view is going beyond BAU. In particular on GSMR the actions being taken by SGN on behalf of

the industry can be expected to deliver very significant cost savings for customers. However, given the criteria that Ofgem has applied, there are no specific CVP proposals that we would argue should have been rewarded.

We had welcomed SGN's wide use of CBAs to justify individual projects and are concerned if this has led to them getting penalised as part of the BPI in what they are terming a "penalty for transparency".

SGNQ8. Do you agree with our proposals on the bespoke UMs? If not, please outline why.

In most cases where proposals are rejected Ofgem is proposing a common uncertainty mechanism which we are happy with. On EAP UIOLI and process, we recognise why Ofgem considered these were too broad and ill defined.

The two UMs that we are disappointed were rejected were:

The reopener for biomethane carbon capture and storage. While we recognise that more work is needed to make the case for this, we were keen that innovative ideas to support biomethane could continue to be developed. The suggestion is that this could be covered by the net zero re-opener or the strategic innovation fund. Our concern is whether it would actually fall within the scope of these mechanisms given biomethane is not expected to be part of the 2050 energy mix but is essential for reducing carbon emissions in the near term. We also note that these reopeners will be focussed around particular developments or challenges and biomethane CCS may not be picked out in that context. If a reopener is not provided then a clearer understanding is needed as to which other mechanism would actually be the right one to use in cases such as this.

The proposed volume drivers for reinforcement associated with connections. As noted in our response on the GD sector document, we were very supportive of a volume driver for connections given the uncertainty around future gas heating and planning rules. In our view the same logic applies to the reinforcement costs. Ofgem argues that a volume driver would remove the incentive to explore non-build capacity options. However our concern was that SGN's connection volume forecasts were too high and hence that they would get a higher allowance than needed. We are unclear whether Ofgem's benchmark modelling addresses this concern in relation to reinforcement. If not then we would argue that a volume driver is needed to avoid consumers paying for more activity than may be required in this area.

SGNQ9. Do you agree with the level of proposed NIA funding for SGN? If not, please outline why.

We note that the level of proposed NIA funding for SGN was very significantly below what they asked for and are concerned in particular that our comments on their BAU innovation have been used in part to justify that. Our view as set out in our original report is that SGN have a good track record on innovation. We had noted the relatively low level of BAU innovation spend they proposed in their Business Plan. However where there is a payback within the price control period we are confident that SGN would pursue innovative solutions. In contrast, the focus of NIA funding is on innovation in areas that do not provide a payback to SGN, in particular on carbon reduction and the transition to net zero. Given the scale of the net zero challenge it does not seem unreasonable that SGN were asking for more than they had in GD1. In our view the primary requirement is that the money is well spent and Ofgem have set out their proposals for improvements around governance

to provide assurance in that area. On that basis it would seem that one option might be to provide for SGN to be able to apply mid period for an increase in its allowance if it is clear there is a need and that the original tranche of expenditure has been well spent. SGN have a clear view already of many of the specific projects that they would hope to undertake with this funding. In our view this is a further reason for considering a higher level of funding could be justified.