

Decision

RIIO-2 Re-opener Applications 2024 Final Determinations – GD Annex

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Contact: Catherine Warrilow

Team: Price Control Operations – Small & Medium Sized Projects

Email: Reopenerconsultations@ofgem.gov.uk

This document sets out our Final Determinations on a number of gas transporter licensees' re-opener applications that were submitted in January 2024 and July 2024. The applications were submitted under the following mechanisms: Diversions and Loss of Development Claims Policy Re-opener, Multi Occupancy Buildings (MOBs) Safety Re-opener and New Large Load Connections Re-opener.

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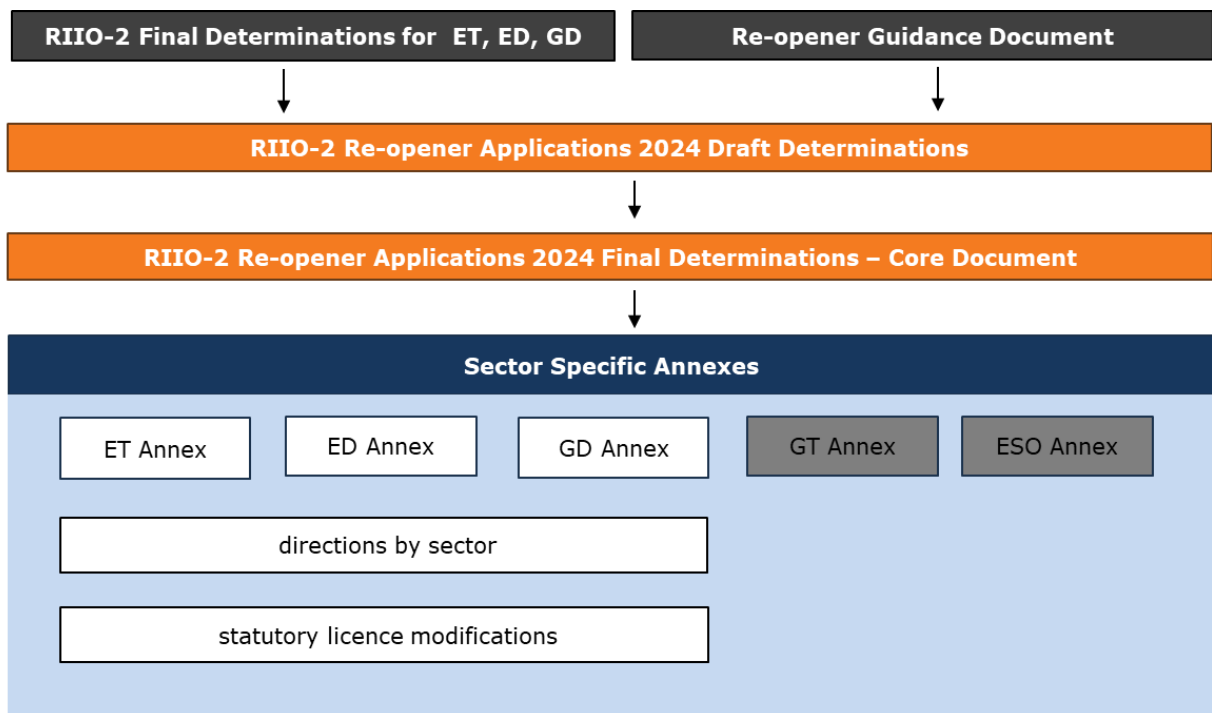
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1.Introduction

1.1 This document is one of three Annexed published alongside the RIIO-2 Re-opener Applications 2024 Final Determination. It focuses on the re-opener mechanisms and the Final Determination of projects submitted in the Gas Distribution (GD) sector. Please refer to the RIIO-2 Re-opener Applications 2024 Final Determination – Core Document for general information including decision making process, stages, etc.

Figure 1: Navigating our Final Determinations



What did we consult on?

1.2 The Gas Distribution Networks (GDNs) applied to Ofgem to add additional allowances into their RIIO-2 price control frameworks under the following mechanisms:

Submitted July 2024

- Diversions and Loss of Development Claims Policy Re-opener (Special Condition (SpC) 3.20)

Submitted January 2024

- MOBs Safety Re-opener (SpC 3.21)
- New Large Load Connections Re-opener (SpC 3.22).

- 1.3 Following their submissions, the licensees also provided additional information to us through a combination of bilateral meetings and Supplementary Question (SQ) responses.
- 1.4 We considered each proposal and the relevant justification for the funding requested in accordance with our principal objective and statutory duties. In line with the [Re-opener Guidance and Application Requirements Document](#), our assessment covered the following three areas for each project:
- the needs case,
 - the options assessment and the justification for the proposed project,
 - the efficient costs for the proposed project.
- 1.5 We combined this information to create our Draft Determinations on what additional allowances, if any, should be provided to each licensee to undertake the relevant projects.
- 1.6 We issued consultations on our Draft Determinations between 03 September 2024 and 01 October 2024, and each included a draft of the direction that would be used to implement the Draft Determination. We received three responses.

Purpose of this document

- 1.7 This document summarises the consultation responses received from stakeholders, and an explanation of the changes made, if any, to our Draft Determination position since the consultation. It also sets out our Final Determinations for applications submitted under the re-opener mechanisms listed in **Table GD1** below.

Table GD1: GD re-opener mechanisms subject to this decision

Reopener Mechanism	Special Condition
Diversions and Loss of Development Claims Policy Re-opener	3.20
MOB safety Re-opener	3.21
New Large Load Connections Re-opener	3.22

- 1.8 Alongside this decision, we are publishing a direction to amend Cadent, SGN and WWU’s licence for this decision.
- 1.9 We are also publishing a statutory consultation to implement our decision to assign PCDs as part of our Final Determinations. This consultation will run from 9 December 2024 to 13 January 2025 and we welcome responses on the proposed licence modifications.

Related publications

1.10 This document is intended to be read alongside:

- [Re-opener Guidance and Application Requirements Document](#)
- [Licences and licence conditions | Ofgem](#)
- GDN applications:
 - (1) Cadent:
 - (a) Diversions and Loss of Development Claims Policy Re-opener - [Diversions-and-Loss-of-Land-Development-Claims-Re-opener-Submission-January-2024.pdf](#)
 - (b) MOBs Safety Re-opener - [Multi-Occupancy-Buildings-Safety-Re-opener-Submission-January-2024.pdf](#)
 - (c) New Large Load Connections Re-opener - [New-Large-Load-Connections-Re-opener-Submission-January-2024.pdf](#)
 - (2) SGN: Diversions and Loss of Development Claims Policy Re-opener - [SGN Diversion Reopener Submission - Redacted.pdf](#)
 - (3) WWU:
 - (a) Diversions and Loss of Development Claims Policy Re-opener - [diversions-and-loss-of-development-re-opener.pdf](#)
 - (b) New Large Load Connections Re-opener - [Microsoft Word - New Large Load connections Reopener Executive Summary v2 Redacted 6.02.2024](#)
- [Draft Determinations on RIIO-2 re-opener applications 2024: Electricity Transmission, Electricity Distribution and Gas Distribution | Ofgem](#)

Summary of our Final Determinations

1.11 **Table GD2** below summaries our Draft and Final Determinations for the GD re-openers covered in this annex. Chapters 2-5 discuss these in greater detail.

Table GD2: Summary of our GD Draft and Final Determinations

Sector group	Network	Company requested - Number of Projects	Forecast costs (£m)	Ofgem's DD- Projects Approved*	Ofgem's DD - Projects Not Approved	Cost adjustment (£m)	Ofgem's DD Allowances (£m)	Ofgem's Adjustment from DD to FD** (£m)	Ofgem's FD allowances (£m)
Cadent	EoE	34	58.06	27	7	-32.38	25.68	2.99	28.67
Cadent	Lon	9	19.63	7	2	-15.20	4.43	2.29	6.72
Cadent	NW	18	50.74	16	2	-21.72	29.02	0.01	29.03
Cadent	WM	8	19.90	5	3	-16.49	3.41	6.02	9.43
Northern Gas Network	NGN	-	-	-	-	-	-	-	-
Scotia Gas Network	Sc	4	15.41	3	1	-3.60	11.81	1.12	12.93
Scotia Gas Network	So	-	-	-	-	-	-	-	-
Wales & West Utilities	WWU	26	53.03	24	2	-0.43	52.59	-2.16	50.43

**We refer to Draft Determinations as 'Ofgem's DD'. Projects approved also include partial approval. **We refer to Final Determinations as 'FD'.*

2.Common considerations and decisions

Needs case and optioneering

Summary of our Draft Determinations

- 2.1 Our Draft Determinations concluded that applications under the Diversions and Loss of Development Claims Policy Re-opener (SpC 3.20) and New Large Load Connections Re-opener (SpC 3.22) presented a succinct needs case which outlined necessary network activities to keep the gas pipeline network running safely and efficiently in accordance with obligations under the Pipeline Safety Regulations 1996 (PSR).
- 2.2 Our Draft Determinations also outlined appropriate optioneering had been considered to address the needs case.

Responses to our Draft Determinations

- 2.3 We received three responses from three GDNs. Cadent were supportive and agreed with our assessment of their needs case and optioneering across both re-opener submissions. SGN and WWU did not disagree with our proposals. Further detail on their positions, relating to our cost assessment of these re-openers, is set out in Chapters 3-5 below.

Our Final Determinations

- 2.4 Our Final Determination is to approve the needs case and optioneering for both re-openers listed in paragraph 2.1.

3. Diversions and Loss of Development Claims

Policy Re-opener

Summary of our Draft and Final Determinations

3.1 **Table GD3** below highlights summaries of our Draft and Final Determinations.

**Table GD3: Summary of our Diversions and Loss of Development Claims
Policy Re-opener Draft and Final Determinations (£m, 18/19 prices)**

Network	Submitted costs	Ofgem's DD allowances	Ofgem's Adjustment from DD to FD	Ofgem's FD allowances
Cadent	91.49	49.61	11.31	60.92
SGN	15.41	11.81	1.12	12.93
WWU	42.27	41.84	0.40	42.24

Cadent

3.2 **Table GD4** below highlights our Draft and Final Determinations for Cadent's Diversions and Loss of Development Claims Policy Re-opener.

**Table GD4: Summary of our Draft and Final Determinations for Cadent's
Diversions and Loss of Development Claims Policy Re-opener (£m,
18/19 prices)**

Project	Trigger	Cadent submitted costs	Ofgem's DD allowances	Ofgem's Adjustment from DD to FD	Ofgem's FD allowances
Named diversion projects	Diversion	17.50	13.12	-1.14	11.98
Encroached mains diversions	Diversion	22.40	5.85	+3.20	9.05
Encroached services	Diversion	33.30	9.39*	+10.03	19.42
Structural removal/legal remediation	Diversion	0.33	10.31	0.00	10.31
Completed, future and forecasted projects	Loss of development claims	8.30	1.92	0.00	1.92
Ulverston and Butterwick projects	Environmental	9.66	9.02	-0.78	8.24
Total		91.49	49.61	+11.31	60.92

*Adjusted for ongoing efficiencies in line with RIIO-GD2 Final Determinations.

Our Draft Determinations

3.3 We proposed an overall downwards adjustment of £41.88m for the following:

- Overheads rates,
- Unit costs,
- Allowance for structural removal/legal remediation activities,
- Future loss of development activities.

Cadent’s response to our Draft Determinations

Overheads rates

3.4 Cadent disagreed with our overheads rate reduction to 11% for named diversions projects and both environmental trigger projects (Ulverston and Butterwick) as, in Cadent’s view, we have misinterpreted all overheads costs to be in addition to direct costs.

3.5 Cadent stated that its overheads uplifts include both attributed and allocated overheads, with costs categorised as “attributed overheads” actually being direct costs. Attributed overheads, such as project management, site supervision and work planning, relate to a specific work activity. If the activity stopped, there would be no need to incur these costs.

3.6 Cadent also argues allocated overheads (not attributable to specific activities, but spread across all activities in relation to direct costs) vary significantly between work types due to the nature of the work and should therefore be different. Allocated overheads covers costs incurred within back office functions which relate to central business functions, such as IT, HR and finance.

Unit costs for encroached mains diversions

3.7 Cadent disagreed with our unit cost reduction from £34,112 to £12,444 per encroached mains diversion.

3.8 Cadent has highlighted that using the median rate for 26 completed projects is not representative of the full range of work. This is a small sample size with an average diversion length of 52.11 metres and therefore an inaccurate unit cost for future expenditure or more complex projects. The average diversion length for future work is 83.02 metres.

Unit costs for encroached services

- 3.9 Cadent disagreed with our proposed unit cost reduction. Cadent states that the £577 per service awarded at RIIO-2 Final Determinations was for mains diversion-associated service jobs, which is not comparable to the standalone encroached service jobs within their re-opener application.
- 3.10 For mains-associated work, costs such as labour, materials and reinstatement are built into the overall diversions job. This unit cost would also not include support costs such as traffic management, permits and planning. Cadent highlights standalone service jobs are not associated with a mains diversion, and therefore have higher unit costs due to inclusion of these support costs.
- 3.11 Costs also vary between network, with higher cost averages in the London network due to regional factors that affect all cost elements.

Structural removal/legal remediation

- 3.12 Cadent was supportive of our proposals of an allowance and associated PCD for this activity for the remaining two years of RIIO-GD2. Cadent proposed an even distribution of overall funding across all four networks.

Completed, future and forecasted projects – loss of development claims

- 3.13 Cadent was supportive of our proposals to allow £1.9m for completed projects and a disallowance of £6.38m for future projects in favour of a future window when there will be higher cost confidence.
- 3.14 Cadent also proposed that any future loss of development claims applications under the re-opener should not be subject to a further Materiality Threshold.

PCDs

- 3.15 Cadent was supportive of all our PCD proposals.

Our Final Determinations

- 3.16 In the section below, we set out our funding decisions relating to Cadent’s Diversions and Loss of Development Claims Re-opener with the exception of forecast Loss of Development Claims due to cost uncertainty. This is discussed further in paragraph 3.32 below. We propose to delay publishing the direction for Cadent under this re-opener until such time as we have sufficient confidence over the full value of Loss of Development Claims in RIIO-GD2.
- 3.17 We will only accept additional cost information relating to forecast loss of development claims relating to years four and five of RIIO-GD2. We will have

already published our decisions on other diversions work activities and would therefore not assess anything additional in these categories.

Named diversions projects overheads rates

- 3.18 Cadent has confirmed that its forecast cost estimates assume the following average overheads rates for diversions in RIIO-GD2:
- Years 1 and 2: 40% attributed, 20% allocated,
 - Years 3 to 5: 37% attributed, 18% allocated.
- 3.19 For Cadent’s attributed overheads rate, we have decided to make an upwards adjustment of our Draft Determinations rate from 11% to 15% which equates to £0.62m for these diversion-specific tasks. Attributed overheads relate to a specific work activity, such as project management, site supervision and work planning. We acknowledge Cadent’s response that diversions work involves additional tasks that are not required for New Large Load reinforcement projects, meaning these two workstreams should have different rates. We have therefore decided to increase this rate by 4% to account for the additional costs that Cadent has identified as not being factored into the original 11%.
- 3.20 We have decided to disallow funding for allocated overheads, with a downwards adjustment of £2.13m. Cadent has indicated that allocated overheads relate to central business functions such as IT, HR and finance. These central business functions are funded through baseline allowances. While Cadent has explained how it allocates these central business function costs to its operational activities for accounting purposes, we have not seen sufficient evidence of a direct relationship between additional diversions work and increases in these central business functions.

Unit costs for encroached mains diversions

- 3.21 We acknowledge that a project sample size of 26 is small. However, these projects give us information to date on the materiality of such projects. We do not consider Cadent to have demonstrated, beyond these 26 projects, that a much higher unit cost rate should be awarded for the remaining projects.
- 3.22 We have decided to increase unit costs from our Draft Determinations proposed £12,444 to £19,825. We acknowledge Cadent’s response highlighting that the completed average diversion length increases from 52.11 metres to 83.02 metres for future work, which is a 59.3% increase in length. We have therefore increased our unit rate proportionately by 59.3% also. This results in the following overall cost breakdown:

- 26 completed encroachments - £433,950,
- 435 remaining encroachments (unit cost £19,825) - £8.62m
- Total allowance - £9.05m,
- Downwards adjustment - £13.35m.

Unit costs for encroached services

- 3.23 We acknowledge the differences between standalone services jobs within Cadent’s re-opener and mains diversion-associated service jobs. We therefore agree that a higher unit cost rate is sensible, however, we do not consider that Cadent has robustly justified such high unit cost rates for this work, particularly in the London network.
- 3.24 As part of its consultation response, Cadent provided a cost breakdown example from the West Midlands network, which we further scrutinised through SQs. Cadent outlined standalone encroachment work rates include team cost, FCO cost, reinstatement, permit cost, material cost and overheads (23% attributed, 25% allocated) within the cost breakdown.
- 3.25 We have decided to increase the unit cost we proposed at Draft Determinations based on this information. We have included the rate activities described above and a 15% for attributed overheads rate in line with other overheads rates in our diversions Final Determinations (paragraph 3.19). We have not awarded allocated overheads as discussed in paragraph 3.20. This gives an updated unit cost of £1,259/service for the North West network.
- 3.26 We acknowledge regional rates can vary, particularly in the London network. We have therefore applied uplifts as per our [RIIO-GD2 regional labour indices](#) (2020-2026)¹ to the Eastern and London networks to give unit rates of £1,272/service and £1,486/service respectively. The unit costs for the West Midlands network remains the same as the North West network at £1,259/service.
- 3.27 Using our updated unit costs, our decision is to award an allowance of £19.42m for this work. This is an increase in allowance of £10.03m from our Draft Determinations position.

¹ Technical Annex Part 1, RIIO-GD2 Final Determinations: Step-by-Step Guide to Cost Assessment, Table 8

Structural removal/legal remediation

- 3.28 None of the respondents disagreed with our Draft Determination. Our Final Determination is therefore to confirm our Draft Determination and to award allowances of £9.98m with associated PCD for the remaining two years of RIIO-GD2.
- 3.29 Our draft direction did not split the allowance evenly across networks. We have updated the final direction, published alongside this annex, to account for an even allowance split.

Completed, future and forecasted projects – loss of development claims

- 3.30 Given no evidence was presented to dispute our Draft Determinations position, our decision is to award £1.9m for completed projects.
- 3.31 Cadent’s view is that future loss of development claims submitted under a future window should not be subject to a further Materiality Threshold. However, SpC 3.20.7 clearly states that applications made under SpC 3.20.4, which includes the loss of development claims trigger, must relate to costs that exceed the Materiality Threshold. In order to remove the Materiality Threshold requirement, we would need to modify the licence. We do not consider it an option to reduce the materiality threshold given the implications this would have on potential additional GD2 re-opener submissions and the impact this could have in GD3.
- 3.32 For Cadent’s forecast loss of development claims, we are not making a final determination at this time as we do not have cost certainty to do so. We will issue our Final Determination on outstanding costs relating to forecast year five claims and the associated direction under the re-opener once Cadent provides more evidence relating to the required funding.
- 3.33 As stated in paragraph 3.17, we will only accept additional cost information relating to forecast loss of development claims relating to years four and five of RIIO-GD2. We will have already published our decisions on other diversions work activities and would therefore not assess anything additional in these categories.

Ulverston and Butterwick projects

Ulverston

- 3.34 Cadent has confirmed this project’s estimated 14% overheads rate only reflects allocated overheads. We have decided to disallow these costs as these are related to central business functions which are funded through baseline allowances. While Cadent has explained how it allocates these for accounting purposes, we have not seen sufficient evidence of a direct relationship between additional diversions

work and increases in these central functions. We are therefore unable to award additional funding for allocated overheads costs and have disallowed £1.16m, resulting in an allowance of £6.97m for this project.

Butterwick

3.35 Cadent has confirmed this project has a 55% overheads rate which is made up of 37% attributed and 18% allocated overheads.

3.36 For Cadent's attributed overheads rate, we have decided to make an upwards adjustment of our Draft Determinations rate from 11% to 15% for diversion-specific tasks. Attributed overheads relate to a specific work activity, such as project management, site supervision and work planning. We acknowledge Cadent's response that diversions work involves additional activities that are not required for New Large Load reinforcement projects, meaning these two workstreams should have different rates. Cadent has highlighted that diversions involve initial customer engagement, multiple third-party visits, design team input, customer feedback, payment processing, variation tracking and refund management if necessary; activities that are not required for reinforcement projects. We have therefore decided to increase this rate by 4% to account for the additional costs that Cadent has identified as not being factored into the original 11%. This equates to £150,000 extra allowance per diversion for the additional activities.

3.37 As per paragraph 3.34 above, we have decided to disallow funding for allocated overheads (£0.18m). While Cadent has explained how it allocates these for accounting purposes, we have not seen sufficient evidence of a direct relationship between additional diversions work and increases in these central functions. We have therefore decided to award £1.27m for this project.

PCDs

3.38 Given that none of the respondents disagreed with our Draft Determinations position our FD is to confirm the following PCDs:

- Named diversions projects – Associated allowances: £11.98m,
- Encroached mains diversions - 461 to be delivered in RIIO-GD2 – Associated allowances: £9.05m,
- Structural removal/legal remediation – forecasted costs for years four and five of RIIO-GD2 – Associated allowances: £9.98m.

In addition, we have decided that a PCD associated with encroached services allowances is appropriate as it better mitigates consumers' risk of under-delivery.

- Encroached services - 16,505 to be delivered in RIIO-GD2 – Associated allowances: £19.42m.

SGN

3.39 **Table GD5** below highlights our Draft and Final Determinations for SGN’s Diversions and Loss of Development Claims Policy Re-opener.

Table GD5: Summary of our Draft and Final Determinations for SGN’s Diversions and Loss of Development Claims Policy Re-opener (£m, 18/19 prices)

Project	Trigger	SGN submitted costs	Ofgem’s DD allowances	Ofgem’s Adjustment from DD to FD	Ofgem’s FD allowances
Cowdenhill	Diversion	1.75	0.00	0.00	0.00
Meadowhill	Environmental	6.70	6.23	0.00	6.23
Pitcairngreen	Environmental	2.87	2.87	0.00	2.87
Below 7bar washouts	Environmental	4.09	2.71	+0.87	3.58
Moorfield	Loss of development claims	0.00	0.00	+0.25	0.25
Total		15.41	11.81	+1.12	<u>12.93</u>

Our Draft Determinations

3.40 We proposed a downwards adjustment of £3.60m for the following:

- Activities not within re-opener scope,
- Contingency,
- Volume adjustment.

SGN’s response to our Draft Determinations

Cowdenhill – activities not within re-opener scope

3.41 SGN states that the £1.75m submitted re-opener costs for this activity covers both capital and legal expenditure, with legal proceedings still ongoing. SGN requests that Ofgem allow £1.60m of incurred expenditure and a future opportunity to recover further costs should legal efforts be unsuccessful in the GD3 period.

3.42 SGN has highlighted there are no other regulatory processes to recover these incurred costs and an inability to recover could lead to disincentives to challenge such decisions in future, leading to a worse consumer outcome. SGN also

highlights that £1.45m (18/19 prices) was incurred in GD1 which SGN have been unable to recover through re-openers or the price control settlement process.

Meadowhill – contingency

3.43 SGN states that, since re-opener submission, project uncertainties have been reduced and a 10% risk inclusion is considered reasonable. SGN therefore agrees with our proposed £6.23m allowance for this project.

Pitcairngreen

3.44 SGN agrees with our proposal to fully fund this project with an allowance of £2.87m.

Below bar 7 washouts – volume adjustment

3.45 SGN has updated its predicted remediation volumes from 150 to 70 over GD2. 27 remediations have been completed or are in progress (with a cost of £1.38m) and 43 remediations are forecast in GD2 (with a cost of £2.20m). SGN has identified each of the 70 washouts via water crossing surveys.

3.46 SGN also updated that it now has three contracting companies carrying out the work, that it is refining repair methods, and that it is working with the Scottish Environmental Protection Agency (SEPA) on innovative repair methods. SGN has therefore reduced its allowance request from £4.09m to £3.58m.

Moorfield

3.47 SGN is now requesting £0.25m to cover the legal settlement and suggested that this is the lowest cost to consumers and avoids continuing legal proceedings at further cost and high possibility of losing. SGN has also included some comparison against alternatives to justify the choice of its preferred option.

Our Final Determinations

Cowdenhill – activities not within re-opener scope

3.48 Given legal proceedings are still ongoing, SGN has been unable to provide further evidence that these Diversion Costs are “efficient and unavoidable” as required under SpC 3.20.6(d). Whilst we acknowledge a final court settlement will take time, it means SGN is unable to demonstrate that this Diversion Cost cannot be fully recovered from the requesting third party at this time.²

² [RIIO-2 Final Determinations – GD Sector Annex \(REVISED\)](#) – paragraph 4.28

- 3.49 We have decided to maintain our Draft Determinations proposal and not award funding for the Cowdenhill project, on the basis that there has not been demonstration that costs are efficient and unavoidable.
- 3.50 In regard to SGN’s view that an inability to recover costs will introduce a significant disincentive to challenging decisions, potentially leading to a worse consumer outcome, our view is that the onus is on network companies to demonstrate costs are efficient and in consumers’ best interests. We also expect sufficient optioneering and clear reasoning behind the chosen option, as set out in our Re-opener guidance. Any assessment will fully consider all elements and ensure funding is in consumers’ best interests.

Meadowhill – contingency

- 3.51 Given SGN agreed with our contingency reduction and no evidence was presented to dispute our Draft Determinations position, our decision is to award £6.23m for this project.

Pitcairngreen

- 3.52 Given no evidence was presented to dispute our Draft Determinations position, our decision is to award £2.87m for this project.

Below bar 7 washouts – volume adjustment

- 3.53 As SGN has reduced its estimated workload volumes, we no longer have concerns around deliverability. Each washout has been identified using a water crossing survey, and SGN has confirmed that it has high confidence with regards to the number of expected washout remediations.
- 3.54 We did note, however, that SGN’s estimated unit cost per washout has increased since its original re-opener submission, and have queried this increase with SGN. SGN has confirmed that each washout project is bespoke and comes with varied challenges. This means that cost can vary significantly between projects. SGN suggested that the scale of washout costs was previously unknown to it, has only become evident as a result to recent unprecedented weather events, and therefore that the revised cost estimates are a result of better information now being available to it.
- 3.55 We have decided to award the updated funding request of £3.58m for this work, noting this is lower than the original £4.09m request and comes with high confidence of deliverability from SGN. SGN has provided evidence which we have properly considered to reach our FD position.

Moorfield

3.56 We have considered SGN’s optioneering evidence and agree that its preferred option is the most cost-effective option. SGN has also added that this option is the lowest risk as it represents a full and final settlement with no construction risks or risks from going to trial. We have decided to award SGN £0.25m for this project as these cost estimates are sufficiently robust given the materiality and have been demonstrated to be the cost-effective option for consumers.

WWU

3.57 **Table GD6** below highlights our Draft and Final Determinations for WWU’s Diversions and Loss of Development Claims Policy Re-opener.

Table GD6: Summary of our Draft and Final Determinations for WWU’s Diversions and Loss of Development Claims Policy Re-opener (£m, 18/19 prices)

Trigger	WWU submitted costs	WWU RIIO-GD1 reduction*	Ofgem’s DD allowances	Ofgem’s adjustment from DD to FD	Ofgem’s FD allowances
Diversion	5.89	-0.27	5.62	0.00	5.62
Loss of development claims	35.79	-1.89	33.47	0.40	33.87
Environmental	2.75	0.00	2.75	0.00	2.75
Total	44.43	-2.16	41.84	+0.40	42.24

**Projects which spanned RIIO-GD1 and RIIO-GD2: removal of costs that occurred in RIIO-GD1 and are therefore not within the scope of this re-opener submission.*

Our Draft Determinations

3.58 We proposed a downwards adjustment of £0.43m for the following:

- Forecasted loss of development claims.

We did not have confidence in the cost estimates and were instead open to directing an additional window for this activity when costs were more certain.

WWU’s response to our Draft Determinations

Forecasted loss of development claims

3.59 One of the two disallowed forecasted loss of development claims has since been settled. WWU is therefore requesting £0.1m for this completed claim which is lower than the forecast £0.13m request at the time of re-opener submission.

3.60 For the outstanding £0.30m claim, WWU proposes a PCD to protect consumers from uncertain costs. WWU disagrees with our proposal for a future additional window for forecasted loss of development claims. WWU disagrees as the

outstanding project would not be sufficiently high value to exceed its Materiality Threshold. This would leave WWU unable to use the additional window and therefore unable to reclaim the costs. WWU suggests that if we decide to proceed with this option then a licence modification would be required to set the Materiality Threshold to zero. WWU adds that the uncertainty here is around the actual cost rather than when it would be incurred. Given that we are proposing a PCD for named diversions projects (where the uncertainty is when these costs occur rather than the materiality), WWU’s view is that it is unreasonable to award a PCD for one type of uncertainty but not for another.

PCDs

3.61 WWU is requesting recognition that some awarded GD2 re-opener spend may be spent in the GD3 price control period as it is not possible to accurately forecast the split of spend between GD2 and GD3. WWU argues that there is precedent for this approach in [RIIO-ET2 Final Determinations](#).³ WWU will update Ofgem of any timing differences as part of the annual regulatory reporting pack and PCD reporting required.

Our Final Determinations

Forecasted loss of development claims

3.62 After considering WWU’s updated cost submissions related to the recently settled claim, we have decided to award an additional £0.10m. We note that this is lower than the original £0.13m requested costs.

3.63 We have decided to assign a PCD for the remaining £0.30m claim. We acknowledge WWU’s response that this forecast claim is low materiality and would not trigger the Materiality Threshold of a future window. Given WWU has provided costs for this single forecasted claim with a reasonable level of confidence, a PCD would protect consumers from uncertainty and allow WWU to recover costs for this claim.

PCDs

3.64 We confirm that funding awarded in RIIO-GD2 may be spent in RIIO-GD3. In this scenario, an under-spend would be reported for RIIO-GD2 and an over-spend for RIIO-GD3. This would be considered when evaluating the PCD.

3.65 We have decided to award the following PCD to protect consumers against under-delivery:

³ paragraph 3.33, points 2 and 3.

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- Named diversions projects – Associated allowances: £5.62m,
- Loss of development claim – Associated allowances: £0.30m.

4. Multi Occupancy Buildings (MOBs) Safety Re-opener

Summary of our Draft and Final Determinations

4.1 **Table GD7** below highlights summaries of our Draft and Final Determinations.

Table GD7: Summary of our Multi Occupancy Buildings (MOBs) Safety Re-opener Draft and Final Determinations (£m, 18/19 prices)

Cadent network	Company request	Ofgem’s DD allowances	Ofgem’s adjustment from DD to FD	Ofgem’s FD allowances
Eastern	12.33	0.00	0.00	0.00
London	10.77	0.00	0.00	0.00
North West	7.29	0.00	0.00	0.00
West Midlands	8.22	0.00	0.00	0.00
Total	18.23	0.00	0.00	0.00

Cadent

Our Draft Determinations

4.2 We proposed to reject Cadent’s re-opener application as we considered the application was not within scope of the re-opener mechanism. This is because Cadent did not demonstrate that its proposals are as a result of a change to the Approved MOB Safety Works Programme.

Cadent’s response to our Draft Determinations

4.3 Cadent disagreed with our Draft Determinations position. Cadent argues that, within the licence, the requirement to specify a change only refers to Trigger 1 (“to respond to any new safety standards for MOBs that the Ministry of Housing, Communities & Local Government (MHCLG), HSE⁴ or other relevant regulators or devolved governments may require in response to the Hackitt Review”) and not Trigger 2 (relating to an Approved MOB Safety Works Programme).

4.4 Cadent also argues that the application criteria of must “relate to changes that have come into effect on or after 1 April 2021”, is listed for SpC 3.21.7 (Trigger 1) but not SpC 3.21.8 (Trigger 2), which, in Cadent’s view, means that Trigger 2 does not have to point to a change to the Programme.

4.5 Cadent states that there are further inconsistencies within SpC 3.21 and have suggested changes to address these.

⁴ The Health and Safety Executive.

4.6 Cadent has also stated that the policy intent was to use this re-opener mechanism to recover additional costs for increased workloads related to the Approved MOB Safety Works Programme. Cadent included excerpts from our RIIO-2 Final Determinations to support its argument.

Our Final Determinations

4.7 Cadent has submitted that there is a difference in wording between SpC 3.21.7 (Trigger 1) and SpC 3.21.8 (Trigger 2). While this is correct, the pertinent part of the licence condition is SpC 3.21.4, which clearly sets out that the scope of the re-opener is when there have been changes to either the Safety Requirements Relating to Multiple Occupancy Buildings OR an Approved MOB Safety Works Programme. SpC 3.21.7 (Trigger 1) and SpC 3.21.8 (Trigger 2) must be read in conjunction with SpC 3.21.4. Furthermore, SpC 3.21.6 clearly states that an application made under SpC 3.21.4 must “specify the changes set out in paragraph SpC 3.21.4 to which the application relates”.

4.8 In RIIO-2 Business Plans, Cadent proposed a bespoke re-opener to cover costs relating to new safety standards for MOBs. This was following the Grenfell Tower tragedy where inquiry outcomes may have affected actions that the GDNs would have to undertake in relation to high-rise MOBs. In our RIIO-2 Draft Determinations, we proposed to adopt Cadent’s proposal and apply it as a common re-opener because the same uncertainty existed for all the GDNs.

4.9 At [RIIO-2 Final Determinations](#), we decided to widen the scope of this re-opener to include MOBs safety related maintenance. We considered this appropriate as “the purpose of the re-opener is to enable an increase in allowances in response to additional safety related activities in MOBs”.⁵ The “additional” wording here refers back to the original policy intent, which was to implement a mechanism to allow the GDNs to claim back additional incurred costs as a result of new requirements. We also add that it will “facilitate the funding of programs of work where there was insufficient certainty over workload or unit costs to provide all the baseline funding requested at Final Determinations”. The workload uncertainty discussed here refers to the wider uncertainty over whether there would be new requirements that the GDNs would have to implement, which would increase workload and costs.

4.10 We have therefore decided to maintain our Draft Determinations position that Cadent has not demonstrated changes to an Approved MOB Safety Works

⁵ page 148

Programme and therefore the application is out of scope. Cadent has not provided any evidence to demonstrate a change to the programme in its application or consultation response, therefore we are unable to award funding for an out-of-scope application.

- 4.11 As highlighted in our Draft Determinations, PSR requires Cadent to keep pipelines in efficient working order and in good repair. Cadent has received funding for this work at RIIO-GD2 Final Determinations and we maintain our expectation for Cadent to fully comply with its PSR obligations and to carry out any remediation work in RIIO-GD2 that is needed to appropriately mitigate MOB's safety risks.

5. New Large Load Connections Re-opener

Summary of our Draft and Final Determinations

5.1 **Table GD8** below highlights summaries of our Draft and Final Determinations.

**Table GD8: Summary of our New Large Load Connections Re-opener
Draft and Final Determinations (£m, 18/19 prices)**

Network	Company request	Ofgem's DD allowances	Ofgem's adjustment from DD to FD	Ofgem's FD allowances
Cadent	18.23	12.93	0	12.93
WWU	10.75	10.75	-2.56	8.19

Cadent

5.2 **Table GD9** below highlights summaries of our Draft and Final Determinations.

**Table GD9: Summary of our Draft and Final Determinations for Cadent's
New Large Load Connections Re-opener (£m, 18/19 prices)**

Cadent network	RIIO-GD2 Delivery Years	Company request*	Ofgem's DD allowances	Ofgem's adjustment from DD to FD	Ofgem's FD allowances
Eastern	Years 1,2	1.89	5.59	0.00	1.90
Eastern	Years 3,4,5	8.66	1.90	0.00	5.59
North West	Years 1,2	1.61	4.19	0.00	1.25
North West	Years 3,4,5	6.07	1.25	0.00	4.19
Total		18.23	12.93	0.00	12.93

*Cadent brought to our attention an error in our Draft Determinations corresponding to the Company Request column in Cadent's application, however noting that the overall cost request was correct. We have amended **Table GD9** above to reflect this, but have kept our Draft Determinations allowances as per what we consulted on. We have amended our Final Determinations allowances to reflect this correction.

Our Draft Determinations

5.3 Two of Cadent's four networks (Eastern and North West) incurred costs which exceeded the Materiality Threshold under this re-opener mechanism. We proposed to assign a PCD in relation to the total project costs of £12.93m. We also proposed a downwards adjustment of £5.30m for the following:

- Overheads rates.

Cadent's response to our Draft Determinations

- 5.4 Cadent disagreed with our overheads rate reduction to 11% as, in Cadent’s view, we have misinterpreted all overheads costs to be in addition to direct costs.
- 5.5 Cadent stated that its estimated overheads uplifts include both attributed and allocated overheads, with costs categorised as “attributed overheads” actually being direct costs.

Our Final Determinations

- 5.6 We have decided to maintain the allowances set out in our Draft Determinations.
- 5.7 For reinforcement work, Cadent has stated its 40% overheads rate is made up of:
- 15% attributed overheads rates – overheads directly relating to a specific work activity; if the activity stopped, there would be no need to incur these costs. This can cover things such as project management, site supervision and work planning,
 - 25% allocated overheads rates – covers costs incurred within back office functions, which are split across business activities.
- 5.8 We have decided to maintain our Draft Determinations position and reduce Cadent’s attributed overheads from 15% to 11% in line with WWU’s New Large Load overheads rate. Cadent did not provide sufficient evidence to demonstrate that our Draft Determinations rate of 11% omitted any activities for which it will incur additional costs as a direct result of additional New Large Load connections reinforcement work.
- 5.9 We have decided to disallow Cadent’s 25% allocated overheads rate. Cadent has indicated that allocated overheads relate to central business functions such as IT, HR and finance. These central business functions are funded through baseline allowances. While Cadent has explained how it allocates these central business function costs to its operational activities for accounting purposes, we have not seen sufficient evidence of a direct relationship between additional New Large Load connections reinforcement work and increases in the costs associated with these central business functions. We are therefore unable to award additional funding for allocated overheads costs.

PCDs

- 5.10 We have decided to assign the following PCD to protect consumers against under-delivery:
- Reinforcement projects costs – Associated allowances: £12.93m.

WWU

5.11 **Table GD10** below highlights summaries of our Draft and Final Determinations.

Table GD10: Summary of our Draft and Final Determinations for WWU’s New Large Load Connections Re-opener (£m, 18/19 prices)

	WWU submitted costs	Ofgem’s DD allowances	Ofgem’s adjustment from DD to FD	Ofgem’s FD allowances
Total	10.75	10.75	-2.56	<u>8.19</u>

Our Draft Determinations

5.12 We proposed to make no adjustments to WWU’s costs and proposed a PCD to protect consumers against under-delivery.

WWU’s responses to our Draft Determinations

5.13 WWU confirmed that three projects, with combined value of £2.56m, are no longer proceeding and requested that these are removed from the Re-opener application.

5.14 As described in paragraph 3.61 above, WWU is requesting recognition that some of the spend allowed under this re-opener may be spent in the GD3 price control period. WWU will update Ofgem of any timing differences as part of the annual regulatory reporting pack and PCD reporting required.

Our Final Determinations

5.15 We have removed £2.56m from the funding allowance given WWU has confirmed these projects are no longer proceeding. WWU has not disputed our Draft Determinations position and we have decided to maintain our Draft Determinations to make no adjustments to WWU’s costs.

5.16 We acknowledge that funding awarded in RIIO-GD2 may be spent in RIIO-GD3. In this scenario, an under-spend would be reported for RIIO-GD2 and an over-spend for RIIO-GD3. This will be considered when evaluating the PCD.

PCDs

5.17 We have decided to assign the following PCD to protect consumers against under-delivery:

- Reinforcement projects costs – Associated allowances: £8.19m.