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5<sup>th</sup> December 2024

Dear Catherine

### Tier 1 Stubs Repex Policy Re-opener Draft Determinations<sup>1</sup>

We welcome the opportunity to respond to Ofgem’s consultation in relation to the above Tier 1 Stubs Repex Policy Re-opener Draft Determination<sup>2</sup> published on 7<sup>th</sup> November 2024.

The following table summarises Ofgem’s initial assessment of SGN’s re-opener application as per the draft determination, and includes SGN’s updated re-opener values and total requested allowances:

**Table 1 – Summary of SGN’s re-opener costs, Ofgem’s initial assessment, and SGN’s updated re-opener request**

Network £m 18/19 prices	SGN re-opener costs	SGN baseline allowance Ofgem final determination, Yr1-2	Ofgem adjustments	Ofgem assessed efficient costs	SGN updated re-opener 5 years	SGN Total Request Y3-5, excluding baseline
Scotland	1.81	1.16	-0.65	0.00	1.58	0.42
Southern	5.63	2.53	-3.10	0.00	4.05	1.52
<b>SGN</b>	<b>7.44</b>	<b>3.69</b>	<b>-3.75</b>	<b>0.00</b>	<b>5.63</b>	<b>1.94</b>

In order to facilitate the ease of comparison with other consultation responses, we have responded to the specific consultation questions in our attached detailed annex.

To summarise our position: SGN does not support Ofgem’s initial assessment of our re-opener application.

At the point of RIIO-GD2 business plan submission, stubs were acknowledged to be an emerging issue, with the potential population, associated costs, and proposed remediation strategy all subject to ongoing external assessment. As such, the unit rates defined in the GD2 business plans, and awarded in Ofgem’s final

<sup>1</sup> [RIIO-2 Tier 1 Stubs Repex Policy Re-opener draft determinations 2024 | Ofgem](#)

<sup>2</sup> For clarity, in this consultation response, references to “draft determination”, “re-opener draft determination”, “RIIO-GD2 draft determination” or “consultation document” refer specifically to the Ofgem publication on 7<sup>th</sup> December 2024 “Tier 1 Stubs Repex Policy Re-opener Draft Determinations”, as opposed to the draft determinations associated with the original GD2 business plan.

determination, were known to be estimates which would be subject to later refinement.

As expected, SGN submitted a re-opener application in line with Special Licence Condition 3.18<sup>3</sup> in January 2023 in relation to both our Scotland and Southern networks. This application was further refined during the Ofgem-directed additional re-opener window in October 2023, maintaining a consistent application but with an updated forecast based on the inclusion of GD2 year-2 actual costs incurred.

In Ofgem's re-opener draft determination, both our needs case and optioneering assessments were supported, demonstrating that our application was within scope and sufficiently well-developed.

As such, maintaining allowances based on the GD2 final determination unit rates is not conducive to a productive stubs remediation programme, as our re-opener application has already robustly demonstrated the requirement for costs to be amended.

We are grateful for Ofgem's engagement with SGN throughout this consultation period and hope the below detailed responses to the consultation questions will provide sufficient clarity to support a re-assessment of our application. Should you wish to discuss this response or our application any further, please do not hesitate to contact me.

Yours Sincerely,



**David Handley**  
Director of Regulation and Strategy  
SGN

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<sup>3</sup> [Southern - Special conditions\\_030222.pdf](#)

## Annex: Detailed SGN Response

This annex contains further information in support of SGN's summarised position above and includes our detailed responses to Ofgem's specific consultation questions.

### **Q1: Do you agree with our assessment of applications under the Tier 1 Stubs Repex Policy Re-opener and our Draft Determinations? Please include your views on our assessment of the needs case, optioneering and draft allowances.**

SGN does not agree with Ofgem's assessment of our re-opener application. Ofgem's adjustment is based on unit rates<sup>4</sup>, with the draft determination stating that the baseline allowance using unit rates as at the RIIO-GD2 business plan would be sufficient to deliver the re-opener workload<sup>5</sup>.

The scope of this re-opener was to ensure a full assessment of workloads and costs. We welcome the acknowledgement within the draft determination that SGN's projects are within scope of the re-opener and are necessary under the IMRRP<sup>6</sup>, as such confirming that our application has satisfied the needs case. Similarly, we are pleased that the draft determination also states that Ofgem is "satisfied that appropriate optioneering has been considered to address the needs case"<sup>7</sup>.

However, SGN does not support Ofgem's assessment of the draft allowances. We do not consider that the required programme of stubs remediation is deliverable under the original RIIO-GD2 final determination allowances. While our re-opener application included a reduced proposed workload, it also demonstrated more up to date costs, which are further refined in this consultation response to now include three years of actual data. These updates should be taken into full consideration when awarding tier 1 stubs allowances.

### Background

The following section summarises the context and timelines associated with the process of forecasting and refining SGN's Tier 1 stubs workload, from RIIO-GD2 business plan through to our re-opener submission. Detailed information can be found in our January 2023 and October 2023 re-opener applications and as such is not repeated in this consultation response.

#### Context and Timings of Business Plan Submission

At the point of RIIO-GD2 business plan submission, Tier 1 stubs were a GDN<sup>8</sup>-wide emerging issue, as the stubs population and locations were not fully understood. As such the required remediation, any consequent engineering difficulties and therefore the associated costs were also not fully granularized. SGN's stubs submission in the GD2 business plan was based upon estimated workloads and estimated unit rates, based on desk-top information available at the time. At the time of submission, the uncertainty around these costs and volumes was made clear, and at the final determination Ofgem agreed to maintain a re-opener to enable a full evaluation of both when more complete information became available.

As acknowledged in the re-opener draft determination, in 2019 DNV undertook a study<sup>9</sup> led by SGN on behalf of all GDNs to understand;

- The risk posed by stubs
- The circumstances under which any could remain in situ (pending HSE<sup>10</sup> approval), and

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<sup>4</sup> 4.2, P12, consultation document

<sup>5</sup> 4.5, P12, consultation document

<sup>6</sup> Iron Mains Replacement Programme

<sup>7</sup> 3.4, P11, consultation document

<sup>8</sup> Gas Distribution Network

<sup>9</sup> Further details of the study and its conclusions are provided in SGN's original re-opener submission

<sup>10</sup> Health and Safety Executive

- Potential interventions, using current and innovative solutions.

The DNV study was completed after RIIO-GD2 business plan submission. Based on the above considerations, the study was able to confirm the population of stubs eligible for remediation, which would become our updated programme workloads.

#### SGN's Stubs Approach in RIIO-GD2

At RIIO-GD2 final determinations, SGN were awarded a baseline allowance equivalent to two years of our proposed programme, based on the GD2 business plan (pre-DNV) estimates of workloads and unit rates. An uncertainty mechanism in the form of the Tier 1 Stubs Repex Policy re-opener was also included, in acknowledgement that a programme of remediation work would be required throughout the price control irrespective of the limited cost granularity available to GDNs at the point of business plan submission.

During the first two years of GD2, SGN, informed by the DNV study, undertook a stubs trial, originally comprised of 30 stubs in each network in a range of locations with different interventions planned. The objective was to understand the complexities in undertaking the work and provide robust cost evidence to inform the rest of the programme. All planned projects included a detailed engineering pack which collected:

- Location and asset details
- Original planned intervention
- Situation as found
- Implemented intervention
- Costs to complete the work (full breakdown and collected costs)

Packs included map extracts and photographic evidence of the situation on site.

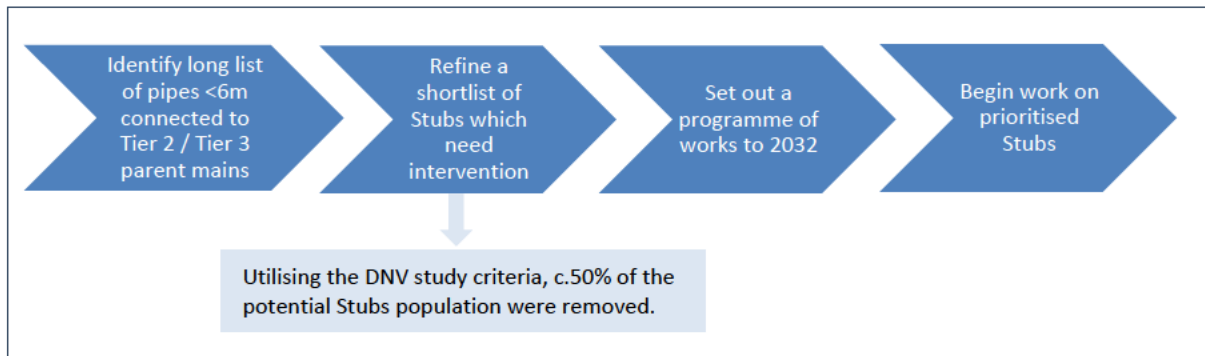
The trial concluded that a stubs programme would need to be agile, as it established various influencing factors on the most appropriate remediation approaches in addition to highlighting complexities which could emerge when undertaking physical works – for example variations in the stub as found, difficult to access locations, or areas of high traffic areas which might be particularly sensitive to road closure.

Crucially, the trial highlighted that it was not uncommon for the full details of the stub in question, including the remediation work and the practical delivery requirements, to emerge only once initial work had begun and the stub could be physically accessed and assessed. The trial therefore demonstrated that work undertaken, and therefore the associated unit rates, varied significantly from the original estimates, and were primarily influenced by factors outside of the GDNs' control.

Given the indications that unit rates were likely to be higher than originally estimated, and informed by the DNV study and our own trial, SGN's stubs programme was therefore designed to ensure that we only undertake work which is necessary, and to employ a prioritised approach, as follows;



**Figure 1 - SGN Stubs Programme Design**



In refining our original long list of candidate pipes and in compiling our shortlist of stubs requiring intervention we were able to remove approximately half of the potential population from our programme. These stubs were removed on the basis of compliance with the findings in the DNV study and could be considered fittings of the parent main. As the HSE has accepted the findings of the study, where stubs fall within an acceptable assessment of risk they can be left in situ beyond 2032<sup>11</sup> and no longer need to be decommissioned in full. As such, they do not need to form part of our programme.

In designing our programme, SGN opted to employ a data strategy based on asset records indicating the presence of a stub, which were then assessed against the criteria outlined by DNV. While past industry practices may have impacted legacy records, extending our programme to include data which does not positively confirm the presence of a stub at the point of desktop assessment was not considered to be a proportionate or economically efficient approach. This approach has enabled us to minimise the costs of our programme to the consumer.

This decision was taken mindful of the potential unit rate variabilities discussed above. Our strategy of ensuring remediations are targeted at stubs which have been pre-validated as being present ensures that we do not undertake work beyond that required, and therefore has the positive impact of preventing SGN from incurring costs beyond those necessary. Our strategy is one of remediation, rather than investigation.

However, this does result in SGN's programme excluding excavations where little to no remediation would likely be required (on the basis of the stub either being compliant, or potentially not even being present), and as such removes the proportion of work which would attract a minimal unit rate. From a statistical analysis perspective, this removes the anchoring effect which would otherwise bring our average stubs unit rate to an overall lower position. As discussed above in Figure 1, our shortlisting approach removed approximately half of the potential stubs population, and therefore were our programme based upon a population closer to the long list described in Figure 1, our average unit rates would be materially lower.

We recognise that variances in the GDNs' approach to stubs, including the degree to which programmes align with the DNV study, may create challenges for Ofgem when seeking to assess unit rates on a comparable basis. Despite the impact of our targeted approach on average unit rates from an optics perspective, when comparing RRP<sup>12</sup> returns from other networks which have undertaken similar work, our unit costs are comparable to the outturn workload already completed elsewhere. As such, we consider our strategy optimal as it ensures that costs incurred are a true reflection of necessary work, rather than costs which appear lower on a per-unit basis due to a less focussed approach.

<sup>11</sup> Target end-date of the Iron Mains Replacement Programme (IMRRP) as defined by the HSE

<sup>12</sup> Regulatory Reporting Pack

## Context of Re-opener Submission

Our original re-opener application was made in January 2023, with a second submission during the adjusted re-opener window in October 2023.

Our re-opener application was based on our established stubs programme described above, informed by the DNV study and our own trial. As such it included detailed information in relation to projects undertaken, resourcing approaches, engineering options and management of risk. Our re-opener was therefore able to provide robust updates against our GD2 business plan and Ofgem’s final determination, in two key areas;

- Updated workloads, showing a reduction in the population of stubs requiring remediation, as a result of DNV’s study and our subsequent prioritisation approach; and
- Updated unit rates, informed by the results of our own trial and GD2 year 1 actual costs.

Table 2 below demonstrates the refinement of our programme workloads throughout the submission journey.

**Table 2 - Workload Trace**

<b>Tier 1 Stubs Workload</b> (5 year totals)	<b>SGN RIIO-GD2 Business Plan</b>	<b>Ofgem Final Determination Baseline</b> (GD2 Years 1&2)	<b>SGN Re-opener Application</b>	<b>SGN Re-opener Draft Determination Consultation Response</b>
Scotland	345	147	152	152
Southern	711	300	225	225
<b>SGN</b>	<b>1,056</b>	<b>447</b>	<b>377</b>	<b>377</b>

As shown above, by virtue of our re-opener application being based upon the results of the DNV study and also our own trial, we were able to refine our anticipated workload, proposing a reduction in total stubs volumes in comparison to both the GD2 business plan and also Ofgem’s final determination baseline. This again demonstrates our commitment to only undertaking work which is necessary from a safety and risk perspective, remaining within scope of the remediations recommended by the DNV study, with our targeted and prioritisation approach minimising otherwise undue costs to the consumer.

Our updated re-opener application submitted in October 2023 maintained the workloads from our original application, with the focus being the provision of updated unit rates based on the inclusion of GD2 year 2 actual costs to again enhance the robustness and confidence of our cost calculations.

As shown in Table 2 above, in this response to the re-opener draft determination, our projected programme workload remains consistent with our original and updated re-opener applications.

## Unit Rate Assessment

The key principle upon which we do not support Ofgem’s assessment of our re-opener application is in relation to the allowances awarded. These allowances are driven by the unit rates associated with undertaking stub remediations.

The draft determination consultation highlights the reduction in proposed workloads between the GD2 final determination and SGN’s re-opener application, and concludes that the baseline allowance (based on unit



rates awarded under the GD2 final determination) is therefore sufficient to deliver the re-opener workload.

However as discussed above, GD2 business plan unit rates were known at the time of submission to require further refinement. Significant work has since been undertaken which has enabled SGN to gather detailed project information and to build well-evidenced anticipated programme costs. Furthermore, actual costs are now available for the first three years of the price control, demonstrating costs incurred against the remediations required and therefore improving the robustness of our forecasts for the remaining programme.

There are four leading factors which broadly determine the cost of a stub intervention;

**Stub material:** If a stub is made from ductile iron, then we have a very limited number of interventions.

**Network topography:** If the stub is still in use within the network, or if its capped.

**Diameter (Parent and stub):** If a stub is connected to a parent main that is greater than 12" and we also need to work on the parent main. If the stub is less than 3" then they are typically e-sealed, and no further work is required.

**Location of asset:** For example, if the stub is in a heavily trafficked road this may necessitate increased traffic management arrangements, which can create additional costs. Alternatively, if the nature of the network infrastructure itself prevents access (for example, not enough room to utilise the necessary equipment), then an alternative intervention may be required.

Other factors may also include the length or material of the stub, and if the stub needs to be wrapped. The physical location of the stub may also vary from expectations.

The above factors can contribute, and may even combine, to result in significant variations in unit rates between remediations. As discussed above, SGN has designed our stubs programme with a key objective of undertaking work only where it is truly required, and to prioritise that work based on a calculated risk profile. This approach is independently verified by virtue of being based on the DNV study and is then further informed by our own trial activities. However, the increased level of data now available unfortunately demonstrates that anticipated unit rates are higher than the initial estimates included in the RIIO-GD2 business plans and awarded at final determination, and therefore even the amended workloads proposed in our re-opener application are not deliverable within the current baseline allowances.

Detailed information in relation to how our unit rates are calculated is available in our original re-opener submission. Our forecasts are built bottom-up, with unit rates calculated based on completed work, informed by the detailed information gathered as part of the engineering packs discussed above. As demonstrated by the acceptance of the needs case and engineering options in our re-opener application, there is now a solid foundation of well-evidenced data from which SGN is able to work. This information is then used to forecast future project costs, based on available data in relation to the anticipated volumes, locations and details of the planned workloads.

Since our re-opener application, SGN has continued to refine unit rate information based on the latest data available, including that submitted under our RRP's. Table 3 and Table 4 below demonstrate the further adjustments which we are now able to propose, in relation to our Scotland and Southern networks respectively.



**Table 3 - Updated Average Unit Rates: Scotland**

Scotland	2021_22	2022_23	2023_24	2024_25	2025_26
£	Actual costs	Actual costs	Actual costs	Forecast	Forecast
Original Re-opener Application Average Unit Rate	████	████	████	████	████
Updated Actual and Forecast Unit Rate	████	████	████	████	████

**Table 4 - Updated Average Unit Rates: Southern**

Southern	2021_22	2022_23	2023_24	2024_25	2025_26
£	Actual costs	Actual costs	Actual costs	Forecast	Forecast
Original Re-opener Application Average Unit Rate	████	████	████	████	████
Updated Actual and Forecast Unit Rate	████	████	████	████	████

The above tables demonstrate an overall decrease in our anticipated unit rates across both networks, in comparison to the re-opener applications made in 2023. These reductions are made on the basis of increased availability and granularity of data, including three years of actual costs and completed programme workloads. These updated unit rates are also aligned with our RIIO-GD3 business plan, in acknowledgement that the stubs programme continues beyond the current price control.

While our unit rates represent a reduction in comparison to our re-opener application, due to the factors described above, they are higher than those estimated in our GD2 business plan. This is unfortunately unavoidable as, as discussed above and during re-opener design, there was little certainty as to the nature and requirements of the stubs programme at the point of business plan submission and final determinations. An increasing trend also remains observable in years 4 and 5, primarily driven by the composition of the workload in the remainder of the price control, which is increasingly likely to relate to more complex remediations. Despite these observations, as part of SGN's commitment to demonstrating cost efficiency wherever possible, we are proposing these latest refinements to our unit rates within this draft determination response to ensure that our anticipated expenditure is as low as possible.

**Q2: Do you agree with our proposal to fund Cadent's on-site assessment activities, given there is a variance in approach between licensees?**

SGN does not have any comments in relation to Cadent's re-opener application.



**Q3: Do you have any views on the draft directions contained in Appendix 1?**

We do not support the draft directions contained in Appendix 1 of the consultation document. We recommend that the draft direction should be updated to take into account the information provided above and the unit rates should be adjusted accordingly, as proposed in Table 5 and Table 6 below.

**Table 5 - Updated Draft Direction: Scotland**

Scotland	2021_22	2022_23	2023_24	2024_25	2025_26	Total
£m	Actual costs	Actual costs	Actual costs	Forecast	Forecast	
Costs	■	■	■	■	■	■
Less GD2 final determination baseline						■
<b>Total updated re-opener request</b>						<b>■</b>

**Table 6 - Updated Draft Direction: Southern**

Southern	2021_22	2022_23	2023_24	2024_25	2025_26	Total
£m	Actual costs	Actual costs	Actual costs	Forecast	Forecast	
Costs	■	■	■	■	■	■
Less GD2 final determination baseline						■
<b>Total updated re-opener request</b>						<b>■</b>