

## GDQ36 – Annex 1:

### Updated Cadent data on Reinstatement and Plant Hire proportions

In our Business Plan, we proposed a Nature of Streets (NoS) adjustment to replace Ofgem's existing urbanity adjustments.<sup>1</sup> Our proposed NoS adjustment is a simple, single adjustment to account for the additional costs we incur to construct and maintain assets located under the street surface in London, as compared to GDNs operating elsewhere.

In its Draft Determination, Ofgem proposes to retain its existing urbanity adjustments for RIIO-GD3, for reasons that we show to be flawed in our response to GDQ36.

In the Draft Determination, Ofgem based its adjustments for Repex Reinstatement and Repex Plant Hire on the average of values from the RIIO-GD2 price control, as newer data was not contained within BPDTs. Ofgem also stated that it wanted to work with GDNs to explore whether updated figures were available prior to the Final Determination.<sup>2</sup>

The purpose of this appendix is to:

1. recap the reasons from the main body of our response to GDQ36 showing why Ofgem has applied its urbanity adjustments inconsistently at the Draft Determination; and
2. to provide updated information so that Ofgem can use more recent data to apply Reinstatement and Plant Hire adjustments, should it continue with its flawed approach from the Draft Determination in the Final Determination.

### Inconsistent application of Ofgem's urbanity adjustments across networks and activities

In our response to GDQ36, when remedying Error 1 in relation to Ofgem's application of its urbanity adjustments, we noted that should Ofgem persist with their use (as opposed to accepting the clearly superior NoS approach):

- Connections and reinforcement activities require underground working, reinstatement, and plant hire. Ofgem's framework accepts the impact on the productivity of connections and reinforcement *labour* costs, but ignores the extra plant and equipment costs that will be needed to complement the extra labour, due to lower productivity in London. Our Business Plan argued that, for consistency, Ofgem should extend its plant hire adjustment to connection and reinforcement activities, following similar logic that it applied to repex plant hire at RIIO-GD2.
- For the same reason, logical consistency requires that the reinstatement adjustment should apply, not only to opex and repex as at GD2, but also to connections and reinforcement activities. Both connections and reinforcement receive an urbanity productivity adjustment for the additional labour cost involved in underground working. However, underground work also requires reinstatement activity. These reinstatement costs would face the same external cost pressures as for opex and repex and so an equivalent urbanity reinstatement adjustment would be needed for connections and reinforcement, which Ofgem does not account for.

We also noted that our East of England (EoE) GDN should receive all urbanity-related adjustments, proportional to the area of the London ITL it covers. For RIIO-GD2, Ofgem applied each of its urbanity-related adjustments to the EoE GDN, except for the repex plant hire and repex reinstatement adjustments (owing to data availability at the time). As a result,

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<sup>1</sup> Cadent (2024), "RIIO-GD3 Business Plan – Appendix 3: Cost Assessment and Benchmarking Approach", pg.45-51.

<sup>2</sup> Ofgem (2025), "RIIO-3 Draft Determinations Gas Distribution Annex", para. 5.98.

for logical consistency, there is no logical reason that the EoE GDN should not also receive equivalent urbanity adjustments to its other cost areas consistent with this.

### **Updated Proportions of Reinstatement and Plant Hire for investment activities**

The percentage of repex and capex activities made up of Plant Hire and Reinstatement costs is not separately specified within the RRP. Having recognised this, in 2024 we carried out a programme of work, separately for capex and repex, to determine what proportions of these activities were accounted for by labour, reinstatement and plant hire.

#### *Repex proportions*

Previously, for RIIO-GD2 we had carried out a specific exercise to split out our repex costs because all repex contractor payments were treated as labour costs for accounting purposes, including those related to Plant Hire and Reinstatement.

For RIIO-GD3 we repeated this exercise, for two years, 2021/22 and 2022/23, taking an average of the results for each network. Starting with the General Ledger, we found that 73% of costs needed significant analysis to attribute to the relevant cost element. Of these, we gave most attention to the largest cost items, being for the Contract Management Office (CMO) – making up around 13% of costs, being very largely labour – and Local Delivery Partner (LDP) costs – making up around 53% of costs, being broadly spread between cost elements. We split LDP costs between elements using the result of our Year 4 repex tender exercise, which covered the vast majority of mains replacement work for that year in each of our networks. The tenders follow a standard format, with all labour recorded as labour, plant hire as plant hire etc, which enabled the split of LDP costs to be robust.

#### *Capex proportions*

We had not split out our capex costs in this way at RIIO-GD2, so this one-off exercise was new for RIIO-GD3. Where possible we sought to reflect aspects of our approach to assessing proportions for repex given we had previously undertaken this work at RIIO-GD2.

We started with the General Ledger for the year 2022/23, which attributed costs into each RRP capex activity, including Connections and Reinforcement. We found that 62% of costs needed significant analysis to attribute to the relevant cost element, such as Reinstatement or Plant Hire, for which we used a number of approaches. For some we sampled a selection of larger projects, analysing tender documents, invoices and compensating event claims to find how costs were broken down between elements, including Reinstatement and Plant Hire. For others we reviewed the entries made in the relevant General Ledger to assess which were likely to contain material amounts of Labour, Reinstatement and Plant Hire, where appropriate reading across from the cost splits of similar projects already encountered in either our capex or repex cost splits work. Given the number of RRP capex activities, we carried out this analysis at the Cadent level.

## Results

The results of our analysis, showing the proportion of activities relevant to Plant Hire and Reinstatement adjustments for the GD2 and GD3 periods, are shown in the table below:

### Proportion of activities relevant to GD2-style urbanity regional factor adjustments<sup>3</sup>

		RIIO-GD2 / 3	
		Plant Hire	Reinstatement
Eastern GDN	- Connections	22.3%	18.3%
	- Reinforcement	15.2%	21.0%
	- Repex	19.5%	11.4%
London GDN	- Connections	22.3%	18.3%
	- Reinforcement	15.2%	21.0%
	- Repex	19.1%	9.3%

To apply the results of this analysis to generate revised regional factors adjustments, Ofgem need to multiply the total activity cost by the percentages shown above, to find the amount of cost for that activity made up of Plant Hire or Reinstatement. From that point, dividing by 1+ the relevant Regional Factor percentage calculates the Normalised cost, from which the amount of the Regional Factor can be found by subtracting the cost pre-Normalisation.

In the main body of our response, the “Cadent Error-Corrected Draft Model with Corrected Urbanity Adjustments” results reported have applied the proportions shown above to calculate Regional Factors, with the exception of those for London GDN’s repex activity. We did not update these from the figures in the Draft Determination, representing the average of the GD2 period, because they do not represent an error present in Ofgem’s Draft Determination that needs correction, but rather old data that needs to be updated before Ofgem’s Final Determination. For Final Determination, we would expect all data to be updated.

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<sup>3</sup> For Connections & Reinforcement this represents the proportion of the activity made up of the whole cost of reinstatement - labour, plant & materials. For Repex, because we have included reinstatement labour within labour costs, and plant within plant costs, this represents only the materials element of reinstatement.