Guidance

# RIIO-3 Business Plan Guidance

| | |
|---|---|
| Publication date: | 18 July 2024 |
| Document Status: | Final |
| Contact: | RIIO-3 Team |
| Team: | Network Price Controls |
| Email: | RIIO3@ofgem.gov.uk |

OFG1164

# Contents

# 1. Introduction

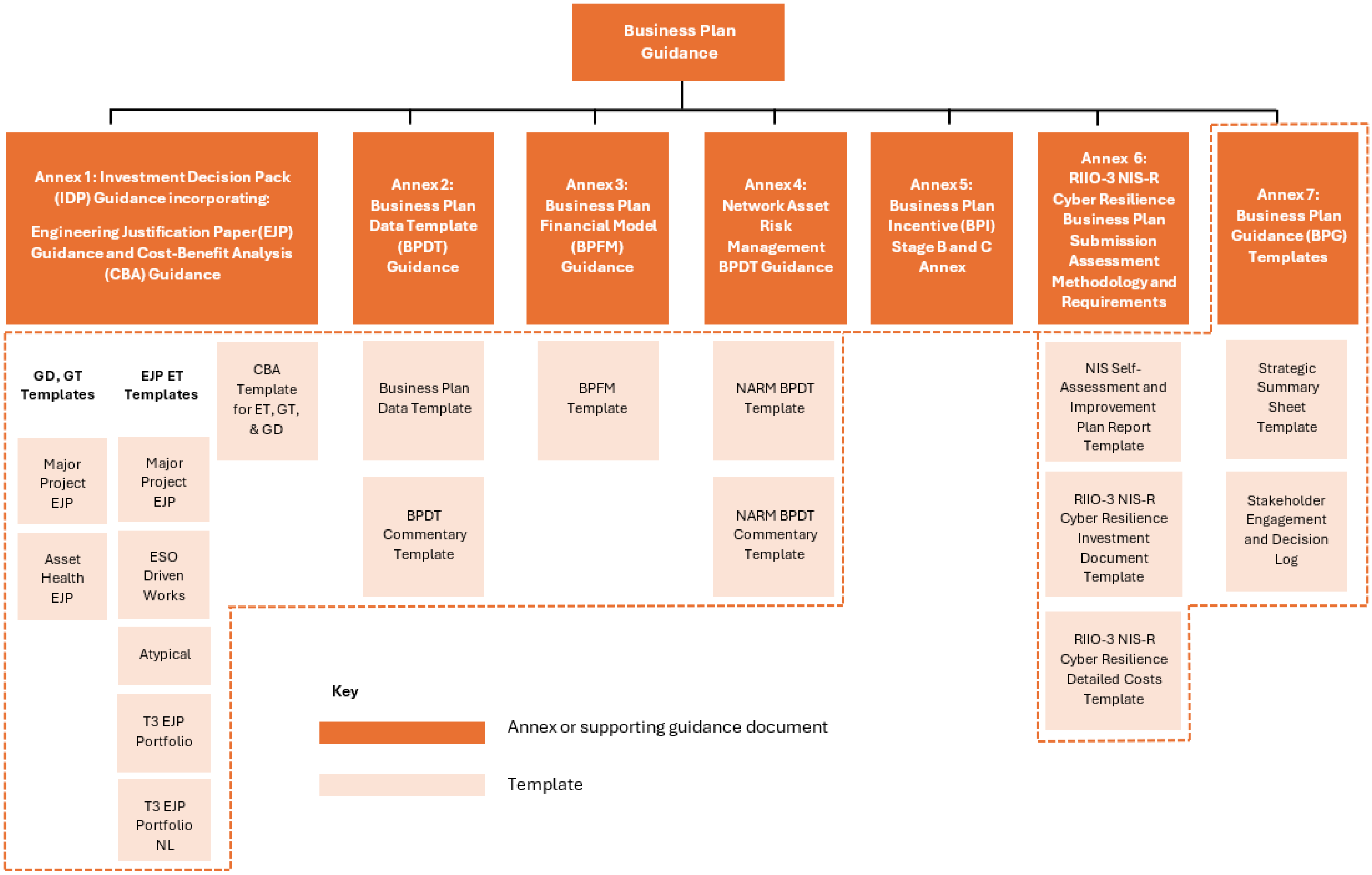
1.1 In the RIIO-3 price control, we will set regulated revenues and required outputs for the gas distribution and gas and electricity transmission network companies. To do this, we need information from the companies on the activities that they intend to undertake in RIIO-3, the outputs that they will deliver, and their associated costs.

1.2 Companies will provide this information to us in the form of a business plan, which we will assess.

1.3 This document sets out the information that should be included in companies' final business plans and how we will assess those plans.

1.4 This document applies to the gas distribution (GD), gas transmission (GT) and electricity transmission (ET) network companies, ie the Gas Distribution Networks (GDNs), National Gas Transmission (National Gas) and to the Electricity Transmission Owners (TOs). Where guidance and requirements are sector-specific, we have indicated these in the chapter/sub-chapter headers, otherwise, the guidance will apply to all of network companies described earlier in this paragraph.

1.5 See below for a document map that outlines the Business Plan Guidance (BPG), associated appendices and key templates.


Business Plan Guidance
Annex 1: Investment Decision Pack (IDP) Guidance incorporating:
Engineering Justification Paper (EJP) Guidance and Cost-Benefit Analysis (CBA) Guidance
Annex 2: Business Plan Data Template (BPDT) Guidance
Annex 3: Business Plan Financial Model (BPFM) Guidance
Annex 4: Network Asset Risk Management BPDT Guidance
Annex 5: Business Plan Incentive (BPI) Stage B and C Annex
Annex 6: RIIO-3 NIS-R Cyber Resilience Business Plan Submission Assessment Methodology and Requirements
Annex 7: Business Plan Guidance (BPG) Templates
GD, GT Templates
EJP ET Templates
CBA Template for ET, GT, & GD
Major Project EJP
Asset Health EJP
Major Project EJP
ESO Driven Works
Atypical
T3 EJP Portfolio
T3 EJP Portfolio NL
Business Plan Data Template
BPDT Commentary Template
BPFM Template
NARM BPDT Template
NARM BPDT Commentary Template
NIS Self-Assessment and Improvement Plan Report Template
RIIO-3 NIS-R Cyber Resilience Investment Document Template
RIIO-3 NIS-R Cyber Resilience Detailed Costs Template
Strategic Summary Sheet Template
Stakeholder Engagement and Decision Log
Key
Annex or supporting guidance document
Template

# 2. Transparency and stakeholder engagement

## Enhanced engagement framework

2.1 Building on positive engagement during RIIO-2, companies should continue to ensure that consumers and stakeholders remain at the heart of their RIIO-3 business planning process, ongoing delivery and decision making.

2.2 Each company should establish an Independent Stakeholder Group (ISG). The ISG will provide challenge and scrutiny to the relevant company both as it develops its business plan and on an enduring basis in the delivery of its plan. The ISG will have a role in ensuring the company engages widely and openly with its stakeholders. It is for the company to identify which stakeholders it thinks are relevant and for the ISG to challenge this. The ISG will represent the interests of consumers and stakeholders and will play an important role in holding the company to account in respect to the delivery of its RIIO-2 and RIIO-3 commitments.

2.3 Each company will be responsible for:

- having in place an ISG and recruiting a Chair that acts in an independent capacity;
- ensuring the ISG is appropriately resourced, eg by providing the necessary secretariat support, information, training and induction for members;
- ensuring the ISG has access to relevant data, information and evidence which will enable it to provide meaningful input and challenge. This will include having access to the company's strategies and plans and to information relating to its performance and culture. This input must be available sufficiently promptly for the ISG to provide effective scrutiny and feedback and for the company to be able to demonstrate how it has considered the ISG's feedback in decision making prior to final submission of the business plan;
- providing the ISG with information and evidence that will enable it to monitor how consumers and stakeholders have been engaged and how any such engagement has affected the delivery of the company's RIIO-2 business plan,

the development of its RIIO-3 business plan and company decision making during the RIIO-3 period;

- providing the ISG with its vulnerability strategy, and social return on investment (SROI) data in respect of activities where baseline funding is sought to address consumer vulnerability (GD only).
- ensuring the ISG has information about the value for money for customers, including but not limited to the provision of clear bill impact data, of specific areas of funding. Companies should set this out in the context of an uncertain future, including (in GD and GT) the longer-term impact on bills of a declining user base;
- ensuring the ISG has access to relevant data, information and evidence that will enable it to provide meaningful input and challenge in the development and/or review of science-based business carbon footprint (BCF) targets as set out in paragraphs 4.53 and 4.54;
- testing the quality and ambition of its business plan with the ISG, using the criteria that we have set out in Stage C of the BPI.
- providing comparative data from other energy network companies (including RIIO-2 performance data) and from companies in other relevant sectors and such other background data as may be reasonably required and requested by the ISG;
- establishing clear terms of reference and governance arrangements for its ISG and publishing them on its website; and
- ensuring that the company’s Board is fully engaged with the work of the ISG, and that this is reflected in the ISG governance arrangements.

2.4 Each ISG is responsible for:

- determining how effectively key areas of concern to relevant consumers and stakeholders have been addressed in the company’s business plan;
- providing challenge and scrutiny of a company's business plan during its development, including the completeness and quality of the business plan as formulated under Stages A and C of the BPI respectively, and monitoring delivery of the commitments in the plan;

- encouraging change towards a culture of more consistent, relevant and more effective stakeholder engagement by the company through scrutiny, challenge and monitoring of its engagement strategy, plans and performance;
- providing insight and feedback to the company to allow it to act on this information and use it to inform decisions early in the process of business plan development; and
- responding to Ofgem's Call for Evidence[1], to be published shortly after the submission of the companies' final business plans. We may decide to request specific information from the ISGs relating to the above responsibilities as part of the Call for Evidence, to support our determinations of business plans.

2.5 In addition, we may ask the ISGs to review specific areas of the business plans if we decide there is a particular need or significant consumer or stakeholder interest.

2.6 The ISG Chair will be responsible for recruiting ISG members that are able to act in the interests of existing and future consumers and stakeholders and have the ability, as a group, to scrutinise and challenge all aspects of the company's business plans (except for specific matters outlined in paragraphs 2.7 and 2.8 below). Members should act in an independent capacity and not solely as a representative of a particular organisation, or group of consumers or stakeholders.

2.7 We do not expect the ISGs to discuss or review specific financial topics, such as the cost of capital, treatment of debt or the level of gearing in the company. The companies should provide sufficient financial, and other information to the ISGs to enable them to understand the overall company risk and reward package proposed in the business plan. We do not expect the ISGs to undertake cost assessment or benchmarking. The companies should provide sufficient cost information to the ISGs to enable them to understand the overall totex package proposed in the business plan, including how efficiency and value for money is being demonstrated.

2.8 In addition, we do not expect the ISGs to scrutinise matters of cyber Information Technology (IT), cyber Operational Technology (OT) or physical security upgrade

[1] RIIO-3 Call for Evidence will be published on Ofgem's website following submission of the RIIO-3 Business Plans.

plans (where relevant) with the company as these may involve sensitive information that it may not be appropriate to share with external parties.

2.9 The ISG does not have decision-making powers nor does it jointly 'own' the business plan that the company submits. The ownership of the business plan sits entirely with the company. Engaging with its ISG is not a substitute for a company's engagement with its consumers, end users and other stakeholders.

2.10 As part of its business plan submission, the company should include a statement, written and signed by the independent ISG Chair, confirming the following, as a minimum:

- That an ISG has been established by the company with clear terms of reference, governance and membership in accordance with this Business Plan Guidance and that the ISG has been fully engaged in the development of the company's business plan.
- That the company has provided the ISG with information and evidence that has enabled the ISG to monitor how consumers and stakeholders have been engaged and how this engagement has affected the development of the RIIO-3 business plan.[2]

2.11 We will adopt a framework within which Ofgem will engage with the ISGs to share insights and to provide feedback on progress.

[2] A summary Stakeholder Engagement and Decision Log is required to be submitted as part of the Business Plan, as described in Table 2 of Chapter 8. We may request further evidence of stakeholder engagement as part of our RIIO-3 determination process.

# 3. High quality of service from regulated firms

3.1 The guidance below sets out some specific areas of output development that should be set out in company business plans. However, this is not exhaustive, and companies should also refer to our Sector Specific Methodology Decision (SSMD), when developing their business plans.

## Vulnerability (GD only)

### GDN Vulnerability Strategies

3.2 In RIIO-GD3, the GDNs will continue to have an important role in addressing consumer vulnerability within their existing areas of competence, activity, and consumer interaction, and where they are best placed to do so. Issues of fuel poverty and carbon monoxide (CO) awareness will remain a priority. The Framework Decision set out that GDNs should also have a role in providing support to those most at risk of being left behind in the transition to net zero.

3.3 The GDNs should submit their up-to-date individual vulnerability strategies and a draft of the joint-GDN vulnerability strategy to us alongside their Business Plans. The GDNs should ensure their vulnerability strategies are up to date and tailored to the needs of consumers. These strategies should be tested with the GDNs' stakeholders, with Vulnerability and Carbon Monoxide Allowance (VCMA) Project Partners, and with their ISGs. To inform their vulnerability strategies, GDNs should work with stakeholders, VCMA Project Partners, and their ISGs to develop common definitions of "most at risk" and a fair "transition to net zero" to consider how best to support these consumers. These common definitions should be included in the vulnerability strategies.

3.4 The GDNs' vulnerability strategies should inform their RIIO-3 business plans, including through their proposed use of the VCMA, as well as how they carry out Business As Usual (BAU) activities and processes which might involve interactions with consumers in vulnerable situations.

3.5 Any GDN baseline funding requests for activities relating to vulnerability should be justified using a common methodology to determine the monetised value associated with their proposals. The common methodology, eg a Social Return on Investment model, should be used by all GDNs.

## Innovation

3.6 Building on innovation activities within RIIO-2, companies should continue to undertake innovation to find new ways of developing and operating their networks to deliver a low-carbon energy system that is reliable, safe and efficient, at a pace in line with our net zero targets. In their Business Plans, companies should provide an overview of the BAU innovation they plan to undertake, alongside justification of companies' planned utilisation of the flexible Network Innovation Allowance (NIA) to explore higher risk areas beyond BAU.

3.7 BAU innovation refers to innovation undertaken in response to incentives and allowances contained in the price control, separate to dedicated innovation funding. BAU innovation may be funded in various ways, including but not limited to the Totex allowance, for example, to continually improve operations, drive efficiency and cost savings for shareholders and consumers, and work towards achieving net zero energy networks more quickly. This should also include activities to deploy innovation previously explored and tested under RIIO-1 and RIIO-2 innovation stimulus frameworks (ie the Network Innovation Competition (NIC), the NIA, and the Strategic Innovation Fund (SIF)).

3.8 For innovation activities going beyond BAU innovation, we strongly encourage companies to use and apply for the ringfenced innovation stimulus funds that are set out within the RIIO-3 SSMD. The funds will firstly include the NIA, based on Business Plans provided, which will be assessed against the eligibility criteria set out in the SSMD. Secondly, there will be a fund focused on experimental development and demonstration of large-scale, high-impact strategic projects (this will continue to be known as the SIF).

3.9 Companies should submit a high-level overview of their Innovation Strategy within their Business Plan, summarising their strategic approach to innovation, including how they will use innovation to achieve the RIIO-3 outcomes and how they intend to utilise the innovation stimuli and other sources of funding to do so. This should firstly provide an overview of the BAU innovation they plan to undertake. Secondly, it should provide a summary of the companies' planned utilisation of the NIA. The Annex, clearly referencing content in the Business Plan where relevant, should provide further supporting details on the Innovation Strategy, such as detailed justifications and examples of projects.

3.10 Companies can also include a case for any additional Totex allowance in RIIO-3 to cover reasonable costs to deploy previously proven innovation. As this could amount to a bespoke output to deploy a particular project(s), the criteria set out in paragraphs 3.27 and 3.28 will inform our assessment. We will also put a particular focus on the following points of the justification:

- Why the activity is not already incentivised through the price control (and why it is appropriate that consumers should provide further funding for deploying proven innovation), including transparency around the commercial benefits or cost savings the company will receive from the deployment, and any resultant benefits to consumers.
- How the proposal is backed by robust evidence and justification, including justification for the proposed costs.
- What benefits consumers and wider network users will receive, and over what time horizon, including carbon reductions and wider environmental benefits, and whole system benefits.
- How companies will monitor the delivery of the anticipated benefits against the incurrence of the proposed cost.

### Innovation outside of innovation stimulus funded work

3.11 Within their Business Plan, companies should set out the high-level BAU innovation activities that they are planning for RIIO-3, using their Totex allowance alongside activities to deploy projects undertaken within RIIO-1 and RIIO-2 that were funded through the innovation stimuli, and the processes they have in place for identifying these areas. Companies should include the following:

- Their planned areas of work to deliver innovation within RIIO-3, for example, to continually improve operations, drive efficiency and cost savings for shareholders and consumers, and work towards achieving net zero energy networks more quickly.
- How they will consider, and mitigate, if necessary, the potential impacts of their innovation activities on consumers in vulnerable situations.
- Plans for third-party involvement in their innovation activities, demonstrating how they will engage a wide range of third parties and ensure full consideration of their ideas.
- How they plan for RIIO-3 work to build on past projects completed by them and by others. This should include the steps that the company is taking to ensure that previously proven innovation is deployed into BAU, and

consideration of lessons learnt from past projects. These plans should also outline how the related benefits and costs are reflected in the company's proposed expenditure for RIIO-3.

- How they propose to monitor the benefits of planned RIIO-3 innovation, including how this innovation will reduce costs in other areas during the course of RIIO-3.

3.12 As BAU innovation will be funded through a range of mechanisms to deliver a wide range of outputs, companies should clearly demonstrate their BAU innovation activities throughout their Business Plan. We are not prescriptive as to where companies showcase this within their Business Plan, but it should be clearly signposted as 'BAU innovation' and a table should also be included in the Business Plan Annex referencing where each of these examples is within the Plan.

### Network innovation allowance

3.13 If companies believe that NIA funding is necessary for RIIO-3, their Business Plan should clearly set out and justify the level of flexible allowance funding requested. As part of this, funding requests should include the following:

- The key areas of focus for NIA spending, including but not limited to problems to be solved, and/or potential solutions to problems to be explored and why these were chosen, and where known, details of individual planned NIA projects.
- How the proposed areas of focus and planned projects meet the NIA eligibility criteria “facilitat[ing] energy system transition and/or benefit[ing] consumers in vulnerable situations”, and guidance on scope of projects, as set out in the SSMD.
- How much funding the networks companies believe is necessary for each of these areas of focus, and a justification of the amount.
- How activities will be delivered.
- The value/benefits the networks companies anticipate these activities may generate.
- How the overall level of funding compares with the level of NIA funding and spending in RIIO-2.
- Plans to collaborate with other network companies to identify and deliver NIA projects.

- The steps that the network companies have in place to ensure that their projects are not duplicative of previous innovation funded work or of work being concurrently delivered by other networks.
- The networks companies' proposals to disseminate learnings from innovation.
- An explanation of why the innovation in question cannot be funded from the Totex allowance.
- The processes companies have in place to roll out proven innovation into BAU, and evidence that they are already doing so.
- Plans for third-party involvement in their innovation activities, demonstrating how they will engage a wide range of third parties, including small and medium sized enterprises, in their innovation activities and ensure full consideration of third-party innovation ideas.

3.14 In determining whether networks will receive NIA funding, and if so, how much, we will consider the evidence provided as part of paragraph 3.13.

3.15 As part of any request for NIA funding, companies should also set out the desired structure of their proposed RIIO-3 flexible allowance and how much risk they are willing to take on against their allowance. For example:

- The compulsory contribution is currently set at a minimum of 10% - companies should provide a basis for the amount that they are willing to make towards their RIIO-3 flexible allowance, with evidence in support of their proposal if higher or lower than the current amount.
- Any other mechanisms they propose to support their flexible allowance funding, such as reopeners to reassess the level of flexible funding needed during the course of RIIO-3.

## Competition

3.16 Guidance is included below for late competition and for early competition.

3.17 Companies should provide information relating to proposed investment projects that are suitable for late competition and for early competition as set out in this section.

### Late competition

3.18 Companies should set out their best view as to which projects identified within their business plan (either through a specific request for baseline funding or via an uncertainty mechanism) meet the late model criteria for competition (new, separable, and high value). Where the company sets out its view that a project in its business plan submission valued at over £100m does not meet the criteria for competition, the company should provide detailed reasoning through additional commentary. Such commentary should be included, or at least cross-referenced in any supporting Engineering Justification Papers (EJPs), or in the case of the TOs, included within the optional 10 page "suitability for competition" section of the "Load related investment plan" explained in Chapter 4. In ET, this identification should not be restricted to projects identified within the NESO's Central Strategic Network Plan.

3.19 In presenting projects in their business plans, companies should also consider and indicate whether any projects that don't meet the separability criteria can be segmented to exclude the elements of work that are not separable (thus creating a re-scoped project that does meet the criteria in full). Companies should also consider whether it is appropriate to consider combining smaller projects that individually don't meet the £100m value threshold to create a larger set of works that does meet the criteria.

3.20 Companies should not split larger, single projects into multiple smaller projects for the purpose of avoiding the high value criterion.

### Early competition

3.21 The criteria for early competition do not have a value threshold, but to allow for a proportionate and targeted approach to facilitating the identification of projects for which early competition may be appropriate, companies are required to flag in their business plans system needs (or projects) which are valued above the threshold value of £50m.

3.22 Of the projects flagged as being over £50m, companies should identify specific reasons or evidence for why they consider that it would not be in the interests of consumers for early competition to be used. For example, it might be the case where the system need, or project is part of a wider programme of work and the separation of one aspect would make the overall programme more expensive for consumers, or where planning consent has already been applied for. This relevant evidence and justification should be provided, or at least cross-referenced in any supporting EJPs, or in the case of the TOs, included within the optional 10 page "suitability for competition" section of the "Load related investment plan" explained in Chapter 4.

## Outputs, incentives and uncertainty mechanisms

3.23 In our decision on Frameworks for Future Systems and Network Regulation (FSNR), published in October 2023, we decided to continue to use outputs and incentives to drive delivery of key outcomes to customers including:

- infrastructure fit for a low-cost transition to net zero;
- secure and resilient supplies;
- high quality of service from regulated firms; and
- system efficiency and long-term value for money.

3.24 For RIIO-3 we will continue to:

- set minimum standards of performance which we will impose through the introduction of Licence Obligations (LOs);
- incentivise service improvements for customers through financial Output Delivery Incentives (ODI-Fs);
- capture outputs directly associated with baseline funding and uncertainty mechanisms (UMs), through Price Control Deliverables (PCDs); and
- apply reputational Output Delivery Incentives (ODIs) where these may be in the interests of broader stakeholders, consumers and other network users.

3.25 In our SSMD, we confirmed the common output and incentive arrangements that will apply to the companies in RIIO-3.

3.26 Companies should set out in their business plans the outputs that they will deliver during the RIIO-3 price control period and whether each output (common or bespoke) that the company will deliver is an ODI, LO or a PCD. The business plan must also set out any additional resourcing requirements associated with the delivery of outputs, where the resource required is clearly identifiable within the business plan and expected to increase significantly from historical levels.

## Bespoke outputs

3.27 Companies are not required to submit bespoke outputs other than in the limited circumstances that we have identified in our SSMD. Where bespoke PCDs are proposed, projects should have a value of at least £15m per project and company proposals should:

- reflect the network services that existing and future consumers/network users and/or wider stakeholders require;
- be as complete as possible in capturing the activities and costs of the company in the relevant area;
- be measurable and reportable;
- allow comparison of performance across companies, where there is sufficient commonality; and
- capture the long-term nature of outputs, with a clear implementation plan setting out how they will deliver, or facilitate the delivery of, benefits within and beyond the RIIO-3 price control period.

3.28 Where bespoke outputs are proposed, companies should address the following points as part of their justification:

- why the activity in question is best dealt with through the RIIO-3 price control;
- how the proposal is backed by robust evidence and justification (such as cost benefit analyses);
- why the output is required in addition to the common RIIO-3 arrangements. This should include companies setting out why the suite of RIIO-3 outputs and incentives will not drive the outcomes to be delivered by the bespoke output proposal;
- what value consumers will receive from a proposed new service level and, by extension, the potential associated reward and/or penalty, and the extent to which these are symmetrical, in terms of value and likelihood of outcome;
- the extent to which an independent measure of the existing level of service that consumers receive is available and the degree to which the target level being proposed represents an improvement on this;
- the level of service that is provided by other companies/comparators (where available) in the area of activity in question;
- the activities (and indicative cost) associated with achieving the targeted level of service;
- the proposed consequences to the company if performance falls below target level; and

- whether any costs associated with the bespoke output have been included elsewhere in the relevant company's expenditure proposals. Any such costs should be clearly identified to avoid double counting.

## GT system operation

3.29 National Gas should include the following areas in its System Operator Annex.

### System Operator Process and Strategy

3.30 National Gas should outline the interactions, risks and costs between the System Operator and Transmission Owner (short- to mid-term activities). The annex should outline at least the following areas:

- System operation process, including providing an overview of the day-to-day and mid-term system operation, interaction and overlaps with Transmission Owner activities, and mitigation of risks arising from this interaction.
- System needs, and in particular, investment needs, and how they are likely going to change during RIIO-3.
- System Operator strategy from now until the end of RIIO-3.

3.31 This annex should also include an overview of green connection policy and acceleration (see biomethane and low carbon gas connections below).

### System Operator Incentives

3.32 National Gas should, for all System Operator incentives, outline the following:

- Purpose of the incentive.
- Value to consumers (quantified and supported by historical data from RIIO-1 and RIIO-2 to the extent possible).
- Performance in RIIO-GT1 and GT2 (applicable to existing incentives only).
- Proposal for GT3, including targets, the incentive strength, caps/collars, cost, needs case and options considered (where relevant).

### Network Capability Assessment

3.33 We want to understand National Gas' assumptions underpinning its Network Capability Assessment (NCA) for the next regulatory period and beyond.

3.34 National Gas will produce an Annual Network Capability Assessment Report (ANCAR) by the end of June, however National Gas should update its NCA and the capability lines, when submitting the Final BPs to reflect the assumptions set out in the FES 2024 Holistic Transition and Counterfactual pathways.

3.35 In an annex to the business plans, National Gas should explain the modelling, the assumptions made and how the outcome of the NCA influences its business plan. National Gas should also explain if it is proposing any changes to Licence Baseline Entry and/or Exit capacity for RIIO-3.

3.36 National Gas should, prior to the final BP submission, engage with the National Energy System Operator (NESO) on its NCA and on the assumptions underpinning the Business Plans and should attach the NESO's view of the underlying assumptions of the Business Plan.

# 4. Infrastructure fit for a low-cost transition to net zero

4.1 The guidance below sets out some specific elements that companies should take into account when developing their plans. Companies should also consider our SSMD, when developing their business plans.

## Planning scenarios and forecasting

4.2 The network companies should develop their RIIO-3 business plans using the FES scenarios and pathways published by the National Grid ESO (soon to be known as the National Energy System Operator (NESO) later in 2024).

4.3 For the draft business plans that network companies are due to submit in July 2024:

- The gas companies should base these on the FES 2023 Falling Short scenario, subject to the specific guidance for the gas sector below.
- The electricity transmission companies should use the FES 2023 Leading the Way, subject to the specific guidance for the ET sector below.

4.4 All companies should develop their Final Business Plans (to be submitted in December 2024) using the FES 2024 Holistic Transition pathway, also subject to the relevant sector-specific guidance below.

4.5 All companies should submit Investment Decision Packs in accordance with Appendix 1 - Investment Decision Pack Guidance.

## Guidance for the gas sector

4.6 A gas company may use alternative data values to those in the 2023 FES Falling Short scenario and the FES 2024 Holistic Transition pathway for the purpose of RIIO-3 business planning only if it can justify why this is necessary and why the alternative value is appropriate.

4.7 A relevant justification for using an alternative data value is that it ensures the company will comply with mandatory or critical requirements from safety legislation and regulations, resilience standards, network planning obligations to provide a safe, resilient and secure network over the RIIO-3 period.

4.8 Appropriate sources of alternative data values could include statutory obligations and standards, industry practices, and relevant information from customers and stakeholders.

4.9 Gas companies must identify and explain all adjustments and/or alternative data that they use instead of the relevant FES scenario or pathway in the RIIO-3 Business Plan Data Template. These adjustments should be clearly labelled, should cite the relevant requirement/key driver, explain why the alternative value is appropriate and reference the source or basis for deriving the alternative data value.

4.10 For final business plans, the gas companies should also provide sensitivity analysis, showing the impact of different FES 2024 pathways on their business plans. The sensitivity analysis should, as a minimum, show the impact on plans between the Holistic Transition pathway (with adjustments) and the Counterfactual (with adjustments) where the financial impact on a cost category is estimated to be greater than £50m over the RIIO-3 price control period. Summary narrative should be provided in the BPDT commentary for each area of work affected.

### Guidance for GT

4.11 To be able to submit its Business Plans on the basis of the FES 2024 Holistic Transition pathway with a sensitivity to the FES 2024 Counterfactual pathway, National Gas requires additional data[3] from NESO. NESO's dataset will only be released late in July 2024, meaning that National Gas will have been unable to complete its probabilistic modelling on the basis of the FES 24 in TobySpace in time for the December submission.

4.12 National Gas has proposed a "macro approach" that will allow it to submit its Business Plans on the basis of the FES 2024 Holistic Transition pathway and FES 2024 Counterfactual pathway. Following its macro approach, key "macro areas[4]" and key zones (Scotland, South East and South Wales) will be based on FES 2024 data, whilst the underlying data in the probabilistic model will use FES 2023 data.

4.13 We accept National Gas' proposed approach for the Final BP submission due to National Gas' unique probabilistic modelling process, however in the interest of fairness, National Gas should run and complete the probabilistic modelling on the basis of the FES 2024 Holistic Transition pathway and FES 2024 Counterfactual pathway and share the results with us by 31 March 2025 by resubmitting the

[3] National Gas is unique among the network companies in having to rely on NESO's dataset to complete its probabilistic modelling, which usually takes 8-9 months to finalise.
[4] Including annual peak demand and capacity commitments across domestic, industry and power demand and forecast supply.

BPDT FES Pathway tab 11.03. National Gas should highlight any material differences resulting from the remodelled data. We will review these differences and take them into account in our Draft Determinations to ensure that we are making our decision with the latest and most relevant data.

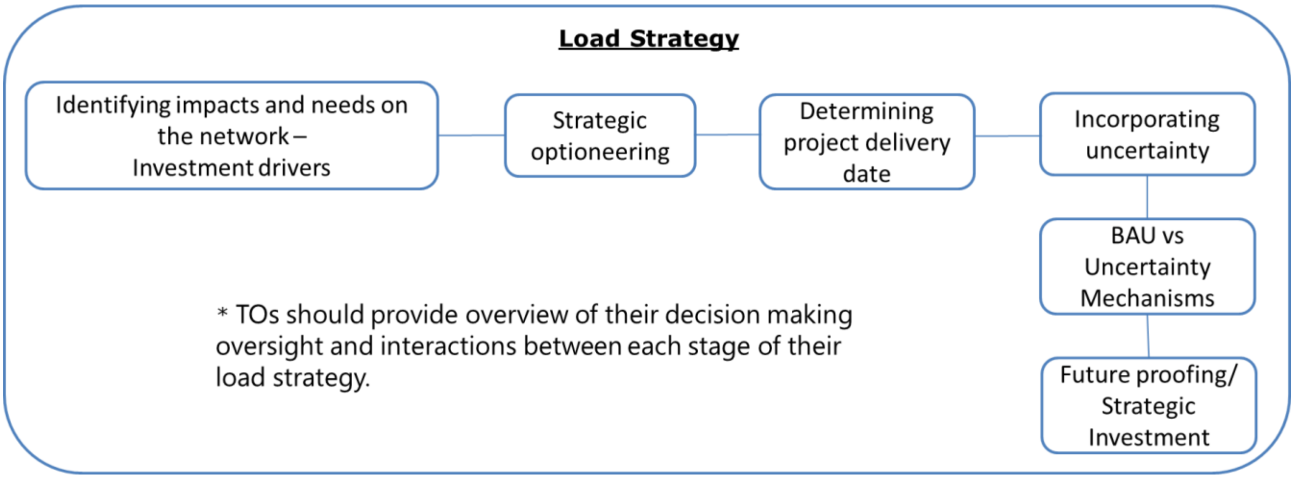
### Guidance for the ET sector

4.14 The ET companies should set out in their load investment plan, consistent with their Load Strategy approach to managing uncertainty (see next section), their best view of the projects they propose to include in their baseline and those that they propose are funded via an uncertainty mechanism.

## ET load related investment plan

### Introduction

Figure 1: Load Strategy




4.15 All TOs should provide a Load Strategy comprising no more than 85 pages alongside their business plans. Figure 1 sets out the broad structure TOs should follow in producing their Load Strategies. However, TOs are free to adapt the structure provided there is a clear justification and explanation for this within the narrative.

4.16 A Load Strategy must set out the TO's overarching methodology underpinning its load related investment plans; from development of forecasts, network assessment and optioneering to decision-making and monitoring of outcomes.

4.17 This section guides TOs in providing an overarching strategic narrative and rationale for their load related investment plan through their Load Strategy, including on how TOs should communicate their overarching approach to:

- Identifying the requirements to reinforce or upgrade the transmission network (through the replacement, augmentation or extension of linear and non-linear assets).
- Strategic optioneering to determine optimal engineering solutions.
- Overall decision-making, including how projects and schemes are given board level sign-off as part of its load related investment plans.
- Managing uncertainty.

4.18 This guidance should be read in conjunction with the Appendix 1- Investment Decision Pack (IDP) Guidance and in conjunction with relevant engineering justification templates:

- Investment Decision Pack (IDP) - ET only.
- IDP templates (EJP / CBA) - ET only.

4.19 In addition to information requested throughout this section, TOs may detail other methodologies and processes that are part of their wider load strategy that have a material effect on their chosen investments.

4.20 TOs should outline the load related expenditure requested through ex ante funding and the potential magnitude of funding that may be required through uncertainty mechanisms within period.

4.21 There will be uncertainty mechanisms in RIIO-ET3 which enable load allowances to flex up or down in a timely, agile manner. These are set out in our SSMD. However, TOs will not need to manage all uncertainty through uncertainty mechanisms, specifically where investments have shared drivers between load and non-load, and there exists opportunities for proactive investments to reinforce infrastructure.

### Decision making process for the load related portfolio

4.22 As part of the Load Strategy, TOs should set out their overarching decision-making framework for their portfolio of load related expenditure. This includes an overview of the corporate governance structure and process. We want to understand how investment decisions are reached, recognising business models, procurement strategies, internal processes may have evolved during RIIO-ET2 to adapt to real world changes. This includes, but is not limited to descriptions of:

- the TO's own engineering framework and stage-gate processes employed by the TO (from needs case/project identification through to option sign-off);
- the contracting strategies and processes in use for design, procurement, delivery and operations (we recognise that certain aspects of procurement strategy could be commercially sensitive; therefore each TO may provide information that it deems as such in relation to its procurement strategy in a separate confidential annex, only available to Ofgem);
- corporate and technical review and sign-off processes for decisions at different project stage-gates (including where responsibility sits at each stage of the process);
- decision stage-gates and process stages;
- internal, board and potential third-party assurance/audit of internal processes; and
- risk management processes.

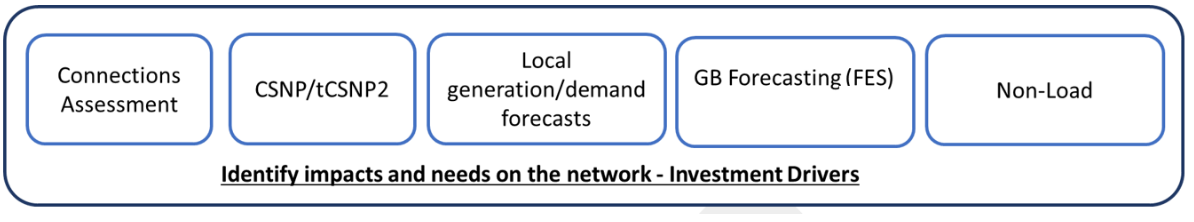
4.23 We want to understand how, at a portfolio level, the TO balances the trade-offs between load and non-load investments that may include but are not limited to:

- levels of risk;
- asset life cycle management;
- project lifespan and operations; and
- resource requirements and flexibility.

4.24 The overall objective is to provide us with comfort that a TO's overall decision-making process is robust and that there are clear stages of sign-off for the portfolio of projects, for those set out in the BPDT and EJPs.

### Identifying impacts and needs on the network: Investment Drivers

Figure 2: Load investment drivers



4.25 TOs should explain how generation and demand forecasts (both national and local) are used in assessments of network impacts, including how any sensitivity to the range of FES pathways is evaluated.

4.26 TOs should provide a high-level explanation of the different methodologies that were explored and the methodology(ies) ultimately chosen and used as part of their network analysis and any pertinent network data which has had a significant impact on identifying investment options (eg a techno-economic CBA - linking to supporting information where relevant).

4.27 The TOs should set out how they assess whether sites warrant Strategic Investment.[5] This may include additional substation works such as sized up assets, spare bays, or increased footprint for anticipated future requirements (eg this may be through the TOs analysis of local connections).

4.28 TOs should set out their overarching framework for how projects in their business plans are linked to clearly identified investment drivers. This includes but is not limited to:

- Consideration of NESO driven projects - eg potential Centralised Strategic Network Plan (CSNP) projects and any projects already recommended by the transitional CSNPs.
- Consideration of any local or national government policies and net zero targets.
- GB wide generation and demand forecasting and pathways to meet net-zero targets (with reference to FES 2024 Holistic Transition pathway).
- TOs assessment of likely outturn connections projects on their own regional networks.
- How TOs have considered the outcomes of the Connections Action Plan[6], and the Target Model Option 4 (TMO4), upon its local network planning.
- Regional network demand/generation forecasting, including local connections applications and forecasts.
- Non-load related expenditure (NLRE) plans and considerations around network resilience (including to increasing climate risks).

[5] Defined in Chapter 3 of the RIIO-3 Business Plan Guidance Appendix 1 – Investment Decision Pack (IDP) Guidance
[6] Ofgem and DESNZ announce joint Connections Action Plan | Ofgem

- An explanation of the feedback loop between optioneering and investment drivers. We want to understand the iterative process between initial needs case analysis and final project sign off.

4.29 For clarity, TOs should clearly set out (in a table, signposts to the BPDT and commentary, or format deemed suitable by the TO) which projects are driven by a standalone strategic programme of work - for example tCSNP2.

### Strategic optioneering approach

4.30 Across the portfolio of RIIO-ET3 projects, we want to understand the methodology for evaluating a wide range of potential options and strategies to determine the most effective and efficient engineering solution for a project. The Load Strategy should set out the principles and factors used in decision making. The principles should also allow Ofgem to cross check the decision-making process within the EJPs. The principles should cover the broad approach to strategic optioneering and project delivery.

4.31 We want to understand how licensees achieve an appropriate balance between competing interests. For example, factors that TOs may consider include but are not limited to:

- Outages coordination: How options are coordinated with the existing network and other infrastructure and outages. For example, how TOs may use or adapt existing infrastructure; could the TO negotiate different commercial arrangements with customers to achieve a need (rather than building new infrastructure); a route that is shorter compared to alternatives; or the chosen option minimises the number of re-interventions/outage slots.
- Regional infrastructure coordination: How network requirements identified at individual sites (or across linear assets) are regionally coordinated and optimised to ensure the most economic outcome in the interest of consumers. For example, for a site replacement at site A, how do TOs take into consideration requirements at site B that is within the same region. TOs should flag relevant EJPs/projects that have been regionally considered?
- Regional connections coordination: How do TOs strategically determine optimal projects, taking into account their assessment of the likely outturn connections on their regional networks?
- Economic: How are options assessed to be the most cost-effective, providing the best value for existing and future consumers. For example, is the whole-

life cost of the asset(s) assessed to determine the financial burden compared to other options.

- Environmental and social considerations: How do TOs assess an option's impact on the environment and local communities, how are the effects minimised (including requirements relating to visual amenity with reference to national and regional statutory requirements), and how do stakeholder inputs factor into the optioneering? This could include signposting to an EAPs.
- Regulatory compliance: How do TOs take into consideration the regulations set by Ofgem and other relevant authorities including system compliance and deliverability, eg compliance with the Security and Quality of Supply Standard (SQSS)?
- Future proofing: How do TOs ensure the requirements of existing and future consumers are efficiently met? For example, can TOs install additional bays in anticipation of expected generation that would be required to meet net zero targets in a faster electrification pathway or ensure additional resilience measures to protect, absorb or respond to increasing climate risks, or economic growth within a region?
- Timings and risks: How do TOs consider the advantages and disadvantages around the delivery timings and risk of different options; and how do TOs consider the impacts of options across multiple price controls?

4.32 At a high-level TOs should also explain the assumptions made about the use of flexibility services, data, monitoring or other non-capex solutions to decide when to invest.

4.33 TOs should set out how they approach weighing up the advantages and disadvantages of all the factors.

4.34 TOs should explain how their strategy affects the long-term planning and delivery of the system. For instance, where investment has been deferred or brought forward and any consequent impact on future deliverability.

4.35 TOs should explain their approach in assessing synergies with other load and non-load network needs.

4.36 We recognise the increasing overlap between enabling works and wider works. We want the TO to explain how it is managing and coordinating works funded by users and those that provide wider system benefits.

4.37 This guidance does not supersede the optioneering guidance for individual projects or schemes set out in the following:

- RIIO-3 Business Plan Guidance Appendix 1: Investment Decision Pack (IDP) Guidance.
- ET3 Major Projects EJP Template.
- ET3 NESO Driven Works EJP Template.
- ET3 Atypical Non-Load, Non-Lead Interventions EJP Template.

### Project delivery

4.38 At a principles level we want to understand the relevant TO's approach to determining project delivery dates and the factors used in deciding the timing for optimal delivery. For example, they include, but are not limited to:

- Wider government targets: Is the project required to meet any governmental net zero targets?
- Design standards: Is the project required to adhere to a specific design standard that dictates development time?
- Planning approval: Does the project need to obtain planning approval before it can proceed?
- Connections dates driven by generation and demand.
- Land rights: Does the project need to obtain specific land access before it can proceed?
- Supply chain and skills: Has the relevant TO secured manufacturing slots and other necessary commercial arrangements and does it have the appropriate workforce in place to deliver the project?
- Equipment and asset purchases: We welcome evidence from companies to provide info on bulk purchase plans for asset that have long lead times and how they expect to manage their supply chain.
- Communities and engagement: Have impacted communities been engaged in the process to develop projects?
- Outage planning: Has the project planned for any potential outages?
- Risk and Contingency: Has the project considered contingency actions to mitigate delivery risk?

4.39 We also want to understand how TOs plan, manage and mitigate project delivery conflicts (eg an outage agreed for one project may prevent outages for one or more other projects). How do TOs optimise their programme of works to necessitate multiple project delivery?

### Suitability for competition

4.40 TOs can use up to a maximum of 10 pages to cover the detail relevant to the suitability of investments for early and late competition that is set out in Chapter 4.

4.41 This should include a table of projects that meet the relevant criteria for early and late competition, and cross-references to where the relevant information set out in the competition section of Chapter 4 is located.

### Incorporating uncertainty

4.42 At a high-level, TOs should explain how they identify and categorise projects that have less confidence and certainty. The driver(s) of uncertainty (eg costs, timing or volumes) identified by TOs should be described, as should factors that they think will materialise to provide greater confidence in the need for investment.

4.43 Where TOs are proposing investments that are anticipatory in nature, this should be clearly identified and justified within the relevant EJP. Such investment may be identified for the purpose of not foreclosing efficient future pathways by ensuring first steps are compatible with options beyond RIIO-ET3. Examples of such activities might include installing additional bays at a substation, sized up assets, increased footprint for likely future requirements or additional resilience measures considering passing thresholds/tipping points on climate risks.

4.44 TOs should set out the key risks and associated mitigations of the load related investment plan. Each TO should articulate how it chooses the balance between baseline funding and the potential use of uncertainty mechanisms in its business plan. In particular, the deliverability of the load related aspects of the business plan should be addressed. This includes how the TO will monitor its progress in delivering its investment plan.

4.45 All uncertainty will not be managed through UMs. Licensees should prioritise using Strategic Investment[7] options in the first instance, until Strategic Investment options are exhausted, particularly for works that have a shared drivers between load and non-load.

4.46 TOs should articulate how they have identified where these risks may materialise and their strategy for mitigating these risks through Strategic Investments. For individual projects, TOs should also articulate the use of Strategic Investments through their EJPs (following the guidance set out in the IDP).

### RIIO-T2-T3 crossover

4.47 For those projects that cross over between RIIO-ET2 and ET3, we require narrative as part of the BPDT Commentary submission in line with guidance set for tab 10.4 'Crossover Projects T2-T3' as set out in the RIIO-ET3 BPDT Instructions and Guidance.

## Environment

4.48 This section provides our view of the minimum level of ambition we would expect should be set out in company business plans in relation to mitigating their environmental impact. Where these initiatives, measures, or templates are not thought to be appropriate or adequate, companies should provide clear justification for why they believe this to be the case in the notes section of the given table.

4.49 Each company should submit an Environmental Action Plan (EAP) alongside its business plan which draws together the direct carbon impacts claimed in Investment Decision Pack submissions (eg leakage, losses, EV fleet) and will include a list of all IDP submissions where:

- carbon reduction is the main driver of the proposal; and
- carbon reduction contributes to a substantial part of the benefits claimed by the projects, eg intervention on the gas network justified mainly on avoided leakage.

[7] Defined in Chapter 3 of the RIIO-3 Business Plan Guidance Appendix 1 – Investment Decision Pack (IDP) Guidance

### EAP

4.50 In the EAP, companies should describe how they will mitigate and improve the environmental impact of their networks. An EAP should encompass activities network companies intend to undertake in RIIO-3 to decarbonise their network and to reduce the wider impact of network activity on the environment. EAPs should explain the methodology that has been used to assess the environmental impacts of the company's network and business plan. The EAP should set out the following:

- Analysis of the significant environmental impacts arising from its network activity.
- The opportunities and challenges for addressing material impact areas.
- An options analysis to identify the value for money of initiatives to reduce its environmental impact.
- Evidence that consideration of impacts is coordinated with the company's wider business planning processes and decisions.
- Evidence that wider stakeholders have been involved in the assessment.
- The company's long-term overall targets/objectives for the network's environmental impacts, beyond the RIIO-3 period.
- Include an assessment of the network's potential environmental impacts in RIIO-3 without intervention, in comparison to its current impacts.
- Set out the role the company envisages playing in supporting the low carbon energy transition.
- Set out the deliverables, outputs and environmental benefits the company proposes to deliver from implementing the EAP over RIIO-3.
- Set out clear links between the impact areas it has prioritised in the EAP, the deliverables and targets in RIIO-3, and how these are linked to the company's long-term environmental targets/objectives.

4.51 A network company's progress against its EAP will be detailed in its Annual Environmental Report (AER). This will comprise of a commentary document and a key performance indicator (KPI) document, as described in our SSMD.

4.52 EAPs should be developed taking into account the baseline expectations set out below. The baseline expectations reflect the minimum level of ambition we expect companies to demonstrate for individual areas.

## Business carbon footprint

4.53 Network companies should:

- adopt or retain an appropriate science-based target[8] to reduce their business carbon footprint (BCF);
- commit to efficient and economic actions to reduce their controllable BCF in RIIO-3;
- report on BCF scopes 1 and 2, and progress towards science-based targets and net zero, using the GHG Protocol Corporate Accounting and Reporting Standard; and
- report on scope 3 emissions on the basis of the GHG Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard.

4.54 Where BCF targets are being developed or reviewed, we expect networks to work alongside their ISG in developing science-based targets in alignment with the Science Based Target Initiative (SBTi) methodology.

## Embodied carbon

4.55 Network companies should:

- report on embodied carbon in new projects (projects beginning in the given price control period);
- set baseline and adopt a target for reducing embodied carbon on new projects during RIIO-3;
- commit to collaborating with the supply chain on addressing challenges to reduce embodied carbon in the network; and
- set out the materiality threshold (ie a £m value) for qualifying new projects that require reporting in this area.

## Supply chain

4.56 Network companies should:

[8] Briefing: Science-based targets | The Carbon Trust

- adopt high standards of environmental management in its supplier code, including requirements for public disclosure of metrics and cascading code to their suppliers that are material to the company's inputs;
- adopt a target of more than 80% of suppliers (by value) meeting the code in RIIO-3; and
- commit to reporting on actual percentage of suppliers (by value) meeting the code.

Resource use and waste

4.57 Network companies should:

- Update procurement processes to embed Circular Economy principles; and
- Adopt targets for:
  - zero waste to landfill by at the latest 20XX;
  - recycle and reuse materials as a percentage of total measurable materials where feasible by at the latest 20XX; and
  - commitments to reporting on actual waste to landfill, recycling and reuse as a percentage of total.

Biodiversity & natural capital

4.58 Network companies should:

- adopt an appropriate tool to assess net changes in biodiversity from different options for new connections and network projects;
- aet out what the materiality threshold should be for new connections and network projects that require reporting on biodiversity;
- regularly report on changes in natural capital and ecosystem services provision (using an appropriate methodology) if a company has an EAP commitment that is directly linked to such measures in its RIIO-3 business plan/price control; and
- in accordance with the National Parks and Access to the Countryside Act 1949 (Section 11A), report on actions taken to assess and remedy the impacts of activities conducted within National Parks.

### Sulphur hexafluoride (SF6) & other IIGs (ET only).

4.59 TOs should use their EAPs to set out their plans and commitments for reducing the SF6 inventory and emissions from Insulation and Interruption Gases (IIGs) on their networks. This should include:

- adopting a reduction target for IIG leakage over the course of RIIO-ET3 consistent with their science-based target for the company's BCF;
- minimising new additions of SF6 inventory on the network in RIIO-ET3 ie only in instances where it is the most cost-effective option on the basis of a life cycle assessment;
- economic and efficient interventions to address the worst-leaking existing SF6 equipment on the network; and
- reporting on total IIG leakage using a common TOs' methodology.

### Transmission losses (ET only)

4.60 TOs should develop and commit to implementing a strategy to efficiently manage both technical and non-technical losses on the TO's network over the long term. This should include specific actions and performance measures to track the impact of actions in RIIO-ET3, including:

- commit to reporting on the progress of implementing the losses strategy and associated performance measures; and
- contribute to the evidence base on the proportion of losses that network companies can influence/control.

### Shrinkage (GD and GT)

4.61 National Gas should:

- commit to working with stakeholders to reduce the volume of Unaccounted for Gas (UAG) and Calorific Value Shrinkage (CVS) in RIIO-GT3;
- develop a transparent methodology to efficiently procure NTS shrinkage energy with a robust target to reduce the cost of the NTS shrinkage energy as a result of National Gas' efficient procurement;
- minimise the cost of NTS shrinkage whilst managing the risk of exposure to short term market movements; and
- adopt appropriate tools to monitor and evaluate procurement decisions.

4.62 GDNs should:

- Include the projected total shrinkage throughput for the RIIO-GD3 period and the amount of leakage through main and service pipes, demonstrating the projected reduction in leakage, attributed to repex.
- Include consistent and accurate reporting of:

  (1) Total shrinkage (in GWh);

  (2) Average pressure (mbar);

  (3) Average monoethylene glycol (MEG);

  (4) Modelled mains / services leakage at Year 5 pressure and MEG; and

  (5) Mains / services leakage at in-year pressure

- Work alongside stakeholders and their ISGs to establish individual stretching targets to reduce shrinkage by the end of RIIO-3. As the shrinkage and leakage model (SLM) is owned by the GDNs, we expect the GDNs to work together to ensure consistency in the processes by which they estimate individual targets to enable comparability and ensure consistency in reporting.
- Report annually in the AER on activities undertaken to help mitigate shrinkage.
- Commit to reporting on shrinkage baseline figures and progress towards the end of RIIO-GD3 shrinkage target in the AERs.
- Commit to reporting on observed measures of leakage alongside the current reporting metrics once leak detection technologies and the Digital Platform for Leakage Analytics (DPLA) becomes available in RIIO-GD3.

Biomethane and other low carbon gas connections (GD and GT only)

4.63 GDNs should

- continue collaborating with stakeholders to identify areas for enhancing connection and injection processes;
- proactively provide information to potential and existing biomethane producers; and
- ensure consistency in biomethane reporting within the AER.

4.64 National Gas should:

- Provide a summary of:

(1) The issue under consideration and objective of accelerating biomethane and other low gas connections (ie "green connections") directly onto the NTS;

(2) Benefits of NTS-direct green gas connections;

(3) The changes (policy, commercial and other) that would be required to facilitate a faster uptake of green connections onto the NTS;

(4) Relevant internal KPIs and costs (including number of connections completed/pa during RIIO-GT3, time to complete connections process, cost per connection).

- Collaborate with stakeholders to identify areas for enhancing the green gas connection process.
- Detail the above in the System Operator Annex.

Greenhouse Gas Emissions (GHG) (GT only)

4.65 National Gas should:

- continue developing a strategy from RIIO-GT2 aimed at reducing emissions levels and endeavour to make all reasonable attempts to progressively lower emissions from compressor venting;
- develop an ambitious target for GHG emissions from venting;
- develop accurate and transparent reporting on venting and emissions related to compressor operations; and
- invest in technologies to reduce the venting of greenhouse gases during compressor shutdowns.

### New environmental incentives (GT only)

4.66 If proposing new incentives in relation to environmental performance, National Gas should:

- justify, in the Incentive annex (see below), why an incentive in this area is required and why improvement cannot be considered part of usual business operations;
- demonstrate that the incentive area is within its control;
- demonstrate the improvements in the behaviours that the incentive might drive;

- be transparent regarding past performance data and data gaps and show how it will address the data gaps going forward;
- develop a measurable and robust target and if/where required a target setting methodology;
- acknowledge the effects that these changes may have on other incentives and provide data to illustrate that there is no risk of 'earning twice' as the result of a new incentive;
- commit to continuous investigation and development regarding the improvements to existing operations; and
- commit to consistent and accurate reporting.

### Statutory Independent Undertakings (SGN only)

4.67 Statutory Independent Undertakings (SIUs) are six remote gas networks that SGN is obligated to support. SGN should submit an SIU annex that, at a minimum, includes the following:

- Forecast of investment including breakdown of capex and opex.
- Refreshed conclusions based on the Enduring Options analysis completed in 2015 and reviewed in 2019.
- Any external factors that are having/will have a material impact on the costs/options for supplying the SIUs.
- Conclusions of the biomethane/hydrogen feasibility studies they were planning to carry out, and any other innovation/decarbonisation initiatives.
- Update on adding Stornoway customers to Xoserve to allow them to switch suppliers.
- Decarbonisation strategy for the 5 SIUs for the next 5 years.
- Decarbonisation strategy for the 5 SIUs to achieve Net Zero by 2050.
- Explanation of how SGN has treated the costs for operating the Stranraer Local Distribution Zone in its business plan.

4.68 The SIU annex should clearly justify the need for new investment. Any proposed work that meets the criteria set out in the IDP should follow the associated guidance.

4.69 The SIU annex should be no longer than 30 pages. This does not include any EJPs.

# 5. Secure and resilient supplies

5.1 The guidance below sets out some specific areas of output development that should be set out in company business plans. However, this is not exhaustive, and companies should also refer to our SSMD, when developing their business plans.

## Network Asset Management

5.2 Each company should submit a Network Asset Management Strategy alongside its Business Plan submissions. The company should submit a Network Asset Management Strategy which sets out what they are doing to ensure best in class asset stewardship.

5.3 The strategy should set out the asset management policy and strategy to promote asset health and long-term operational resilience across its asset including lead and non-lead assets. This should include a summary of the company's approach to the management of NARM and non-NARM assets on its networks, considering safety, compliance and risk management.

### Asset risk and resilience

5.4 Business plans should set out the company’s views on asset health, criticality and replacement priorities for:

- The start of the price control period (the baseline view), effectively reflecting its view on the asset health, criticality and risk of assets on the network.
- The end of the price control period with no intervention, effectively reflecting its view on asset degradation over the period.
- The end of the price control period with proposed interventions.

5.5 We consider that establishing a baseline view of asset health, criticality and replacement priorities at the start of the price control period is essential to Ofgem to take fully informed decisions on a company's proposed asset interventions. This will be supported by the Portfolio asset EJPs.

5.6 Companies should explain their long-term risk objectives and strategy, as well as the long-term benefits delivered by their proposed interventions.

5.7 Monetised Risk objectives should be informed by stakeholder engagement and cost benefit analysis (CBA) and demonstrate that selected investment options both efficiently meet their stakeholder-driven objectives and efficiently deliver sufficient net benefit for existing and future consumers.

## Climate resilience

5.8 Business plans should include a dedicated Climate Resilience Strategy (CRS). We recognise that companies are subject to other climate change reporting requirements, such as the Climate Change Adaptation Reporting Power and IFRS climate disclosure requirements, and therefore, the Climate Resilience Strategies should aim to provide added value by identifying links between their business plan and CRS while avoiding duplication of other reporting mechanisms. In particular, we aim to better understand justifications for investment in climate resilience.

5.9 One Climate Resilience Strategy should be produced per network company.

5.10 We recognise that there is significant work needed to embed climate resilience within the energy sector. This needs to begin as soon as possible, and network companies should develop an iterative approach across the RIIO-3 price control period. Network companies should do as much work as possible within the price control timeframe, and where it isn't realistic, clearly explain why. In the business plans, companies should set out their planned approach and timeline for this work, and then updates will be required as part of their annual reporting.

5.11 Climate Resilience Strategies should clearly signpost to any other submitted documents which relate to climate resilience, such as load strategies, explaining their influence on your business case if requesting additional funding for climate resilience.

5.12 Climate Resilience Strategies should also signpost to any other material relating to climate resilience, such as climate related financial disclosures and ARP reporting.

5.13 Climate Resilience Strategies should outline any other climate resilience work network companies are undertaking or planning to undertake, identifying the steps that they expect to take over the course of RIIO-3 and beyond. This could include:

- Risk assessments.
- Development of rationale for investments in climate resilience.
- Development of adaptive pathways.

- Development of tools, innovations, projects, and technologies.

### Climate Risk Assessment

5.14 Network companies should signpost to their relevant climate change hazards and risk assessment at 2 and 4 degrees as outlined by their most up to date ARP reporting.

5.15 Network companies should outline a breakdown of expenditure (Capex and Opex), relating to a weather event or compound event which has occurred in the last 10 years and has been caused by or exacerbated by climate hazards or risks (eg storm, high winds, temperature change, landslides, soil erosion etc) which caused loss of supply or other detrimental impacts, submitting any supporting evidence, including but not limited to:

- identifying the costs of response and recovery; and
- identifying how this information is being used for future decision-making.

5.16 This event or events does not need to be attributed to anthropogenic climate change. Ofgem is seeking this information in order to better understand potential future costs as the effects of climate change intensify.

### Investment relating to climate resilience

5.17 Each climate resilience strategy should outline the key categories identified in the Business Plan Data Template (BPDT) memo table for climate resilience and provide context as to why this category is affected by climate resilience:

- through current activities and workstreams;
- through new climate resilience projects; and
- the plan for investment until the end of the RIIO-3 price control period.

5.18 In addition, companies should also complete the climate resilience memo table within the BPDT submitting estimates of spend associated with climate resilience. Each category should link to a climate hazard and explanation as to how it affects resilience to the hazard, and how this investment is weighed up against other options, for example, recovery versus protection.

5.19 Explain any alternative financial assessment tools outside of CBAs and EJPs used for climate resilience justification, such as social return on investment.

5.20 Each network company should explain any barriers to making a viable business case for climate resilience projects. If possible, network companies should outline how they might use the Resilience Reopener to mitigate these issues.

5.21 Table 1 summarises the expectations for Climate Resilience Strategies:

Table 1: Climate resilience expectations

| **Expectation** |
|---|
| Signpost to other documents in the business plan submission which relate to climate resilience |
| Signpost to any other material related to climate resilience |
| Outline any other current or planned climate resilience work |
| Signpost to relevant climate change hazards |
| Outline the costs of a recent weather event (or compound event) which cause loss of supply of other detrimental impact |
| Outline the key categories from the BPDT, the plan for investment throughout RIIO-3, and complete the climate resilience memo table |
| Explain any alternative financial assessment tools outside of CBAs and EJPs used for climate resilience justification |
| Explain any barriers to making a viable business case for climate resilience projects, and how the Resilience Reopener might be used to mitigate these issues. |

## Workforce and supply chain resilience

5.22 The company should submit a Workforce and Supply Chain Resilience Strategy which sets out what it is doing in each of these areas to preserve its long-term ability to deliver the work required to fulfil its obligations.

### Workforce resilience

5.23 The Workforce and Supply Chain Resilience Strategy should demonstrate how companies will develop and maintain a modern, diverse, high-quality, well-trained workforce fit for the future. Although we are not prescribing the precise content of these strategies, companies should consider how their approaches will lead to:

- Improving inclusion, diversity and equality.
- Improving workforce satisfaction and retention.
- Improving workforce motivation and productivity.

- Attracting people to the energy sector and developing the skills needed for a technology driven, low carbon energy system.
- Upskilling and multi-skilling the existing workforce.
- Ensuring the health, safety and wellbeing of the workforce.

5.24 The strategies need to identify the resourcing challenges and risks companies envisage they will face in the next price control and beyond. Companies will need to set out the how they expect to mitigate these risks in advance of RIIO-3, such as improving retention, upskilling and increased recruitment.

5.25 Companies should also include in their strategy, any potential forecast of particular skill shortages they foresee beyond the next price control, the potentially associated role at risk, the mitigating steps they would conceivably take now and in the future. Where appropriate, companies should outline how they propose to utilise flexible allowance funding, such as the Resilience Reopeners to tackle these shortages and develop the necessary skill ahead of demand.

5.26 Companies should demonstrate the steps they are taking, or planning to take, to engage with Government over plans, the support they need to increase UK capability for domestic manufacturing, and developing a pipeline of skilled workers. This may include areas such as education, training, housing and immigration.

5.27 The workforce strategy should also set out how the companies would work to develop common metrics for measuring and monitoring workforce resilience. Companies should work with organisations such as trade bodies, to develop common workforce metrics from now (recognising these would not necessarily be finalised for business plan submissions) looking at workforce characteristics, resourcing, skills development and retention. Companies should explore the benefits of quantifying the level of workforce shortage at a sector level, possibly via trade associations. This could also include conducting a holistic skills gap assessment to identify specific high risk roles.

5.28 Over the course of RIIO-3, each company should work towards enabling its own data collection/reporting systems, allowing for the necessary data to assess measurement against all the predefined metrics.

## Supply chain resilience

Creating long-term capacity

5.29 Ensuring that order books allow for long term factory capacity will go a long way to ensuring deliverability of business plans and avoiding cycles of mobilisation and demobilisation that tend to be cost inefficient and prolong investment lead times.

5.30 In developing these strategies, companies will need to take a strategic approach to mitigating supply chain pressures, particularly those arising from long lead times for materials. For example, in the gas sectors, the timely sourcing of essential components, such as pipes, fittings, compressors and monitoring systems, should be coordinated across projects and with company's supply chain partners. For long lead time components, the strategy should go beyond the options to be used at a project level. Companies should, as a minimum, develop an approach to building relationships, slot booking, pre-ordering, buying in bulk and strategically increasing stock levels, to secure sufficient materials in advance.

5.31 Companies should set out collaboration with other industry and government bodies, outlining interaction with initiatives to develop UK supply chain capabilities. For example, ET companies could highlight how they are utilising forums such as UK Supply Chain Council to engage with the electrical equipment supply chain.

Maintaining maximum competitive tension

5.32 In their Workforce and Supply Chain Resilience Strategies, network companies should outline how they will use competition to identify and reveal efficient costs, efficient terms and conditions (particularly with respect to risk allocation), ideas and innovation.

5.33 Network companies should outline the type of information they commit to share throughout the price control, such that we and stakeholders have sight of upcoming competitive processes and can continually assess their performance against their commitments. Where certain information is only intended for us and needs to be kept confidential (eg for commercial reasons), it should be clearly labelled and justified as such.

5.34 The principle of technology agnosticism requires an openness to different ideas. Where appropriate, companies can communicate with the bidding market prior to a formal process or can undertake a phased approach to tendering to identify solutions which best meet need. Companies should consider using their Workforce and Supply Chain Resilience Strategy to publicly commit to an approach which best embeds this principle.

5.35 Companies should commit to a tender design and assessment approach which ensures the best outcomes for existing and future consumers, eg by using explicit considerations of option value, particularly for flexibility solutions.

Worked examples

5.36 Network companies have identified that there are challenging supply chain and workforce conditions worldwide that are making their procurement more difficult since 2021. To illustrate this point, and to illustrate the actions that network companies are undertaking to mitigate those challenges, we want network companies to set out at least two project-specific examples of procurement and contracting challenges being faced now that were not present when setting RIIO-2, the key actions that they are taking as an organisation to mitigate these challenges as far as possible and the consumer benefit. For example:

- How the company is creating maximum competitive tension in a market which it claims is less competitive?
- How it manages key relationships in the market? How it fosters long-term relationships?
- What is its approach to assessing bids is, particularly when very few are received? How it ensures this delivers value for consumers?
- How it is driving greater cost efficiency in the supply chain?
- How the approach to apportioning risk between the company and contractors has changed? How is this impacting cost and cost certainty?
- How it is driving the supply chain to deliver innovation to improve outputs and/or reduce costs?

## Cyber resilience

5.37 We consider there is a significant and continual need for network companies to invest, develop, and undertake activities to reduce risk, improve cyber capabilities, and better align their organisation with the Network and Information

Systems Regulations 2018 ('NIS-R')[9] requirements. To measure the implementation progress of NIS-R, the National Cyber Security Centre's ('NCSC') defined Cyber Resilience Outcomes in the Cyber Assessment Framework ('CAF') in 2018.[10] Network companies have a clear mandate to attain sector profiles for cyber resilience and to ensure compliance with the NIS-R.

5.38 In RIIO-3, we will no longer require network companies to submit separate business plans for 'Cyber Resilience IT' and 'Cyber Resilience OT'. Instead, companies should submit one NIS-R Cyber Resilience Business Plan ('CRBP'). This enables better alignment with the NIS-R, which are agnostic of IT and OT environments. We recognise that network companies review, plan and monitor cyber resilience IT and OT systems and activities holistically.

5.39 Network companies should use the 'RIIO-3 NIS-R Cyber Resilience Business Plan Assessment Methodology and Requirements' supplementary document in developing their CRBP. The CRBP will be assessed against these requirements. Network companies are encouraged to engage with us to assist with the development of their CRBP and to review the Ofgem NIS Guidance for Downstream Gas and Electricity Operators of Essential Services in GB.[11]

5.40 The CRBP submission should be based on the NIS Self-Assessment and Improvement Report submitted to Ofgem in Autumn 2022, updated to reflect any scope changes as reported in the NIS Annual Reports up to and including the report submitted to Ofgem in July 2024. We want to leverage the existing templates used for NIS Self-Assessment and Improvement Reports for the CRBP.[12] We expect alignment between the NIS-R Improvement Plan activities and the funding requested in RIIO-3.

5.41 CRBPs must demonstrate how network companies will reduce the risk of cyber incidents on essential services, to ensure a safe and resilient network that is compliant with the NIS-R. We will assess all economic and efficient investments that network companies propose to improve cyber resilience of assets subject to the NIS-R.

[9] https://www.gov.uk/government/collections/nis-directive-and-nis-regulations-2018
[10] NCSC CAF guidance - NCSC.GOV.UK The CAF provides guidance for operators of essential services. Ofgem, as joint Competent Authority with DESNZ for the energy sector in GB, use the CAF to assess the extent to which a network company is mitigating and managing its cyber risks.
[11] Ofgem, April 2022, NIS Guidance for Downstream Gas and Electricity Operators of Essential Services in GB v2.0.pdf (ofgem.gov.uk)
[12] The NIS Self-Assessment and Improvement Report template is available here: NIS Directive and NIS Regulations 2018: Ofgem guidance for Operators of Essential Services | Ofgem

5.42 General technology refresh or end of life replacements should form part of more general system investment plans, which should already include appropriate cyber protection, rather than be included as part of the CRBP. See the 'RIIO-3 NIS-R Cyber Resilience Business Plan Assessment Methodology and Requirements' supplementary document for more detail.

5.43 Security measures for BAU should form part of more general investment plans. However, we will consider crossover, where an associated risk is highlighted, for example around the interconnection between business IT and NIS-R assets. See the 'RIIO-3 NIS-R Cyber Resilience Business Plan Assessment Methodology and Requirements' supplementary document for more detail.

5.44 The CRBP appendices must include the following standardised NIS-R CRBP templates as a minimum: The NIS-R Cyber Resilience Investment Document ('CRID') template and the NIS-R Cyber Resilience Detailed Costs template. Any other supporting information a network company thinks is pertinent to its RIIO-3 investment requirements can also be included in the appendices eg Cyber Strategy.

5.45 The CRID should include details of the needs case, proposed delivery and the costings either at a programme or project level depending on what is most appropriate for the network company to articulate its investment requirements. Network companies should align each CRID to a primary CAF Principle. This should result in a maximum of 16 CRIDs being submitted.

5.46 The NIS-R Cyber Resilience Detailed Costs should be populated per project with capex and opex costs provided split into people, process and technology. Network companies should align the NIS-R Cyber Resilience Detailed Costs to the relevant CRID.

## IT and Telecoms Strategy

5.47 The Information Technology and Telecoms (IT&T) strategy should clearly set out how the network company plans to use IT&T to enable it to achieve the proposals set out in its Business Plan.

5.48 It should incorporate the application of policies, business strategy, assessment processes and techniques as well as considerations of sustainability and deliverability.

5.49 The strategy should set out how operational IT and telecoms risk reduction will be achieved, how the company will maintain a 24/7 operational telecoms network, how it will improve operational efficiency and how it will improve telecommunications network resiliency.

# 6. System efficiency and long-term value for money

## Cost information and the BPDT

6.1 Network companies should submit cost information as part of their business plans, as set out in this section.

6.2 In proposing costs for operating and developing their networks, companies should explain their costs/workload forecasts, particularly where these diverge from historical trends. In particular, companies should provide information in their business plans on:

- cost drivers;
- consideration of options;
- justification of costs, including the proposed profiling of costs; and
- how efficiency improvements and innovation will be delivered to reduce costs and/or add value for money over the RIIO-3 period.

6.3 Companies should complete the BPDT and tab-by-tab commentary in accordance with the Ofgem BPDT guidance. The guidance below should be read in conjunction with the Ofgem BPDT guidance.

6.4 Business plans should clearly set out the key drivers of expenditure for the RIIO-3 period - for example, growth in demand, conditions of assets/utilisation, legislative requirements, and any other relevant drivers.

6.5 Business plans should clearly justify the need for new investment, including:

- Information on current levels of network utilisation and expected changes to utilisation based on the different forecast FES pathways and other requirements (such as safety standards or contracted positions), in accordance with Chapter 4 and the IDP Guidance. Information on current and forecast network capacity should be published in accordance with Data Best Practice Guidance.[13]
- The different options considered for meeting future network requirements, including the cost of "doing nothing" and of "deferral" options and the associated cost benefit analysis (CBA). These options should include, where

[13] Decision on updates to Data Best Practice Guidance and Digitalisation Strategy and Action Plan.

appropriate, the availability of potential market solutions to the system need, and whether any 'whole system' solutions are available.

- The options discounted by network companies at this stage, full reasoning, detailing key assumptions and selection criteria given for exclusion.
- The reasons for the timing of investment under the different options considered, including expected outputs (eg the delivery of an increment in boundary capacity transfer, the delivery of an electricity link, a gas pipeline) related to the investment and year of delivery.

6.6 If business plans include proposals for new investment (including investment for the replacement of existing assets) that was previously proposed and funded by customers under RIIO-1 or RIIO-2 but was not delivered, details should be provided explaining why it was considered to be in the customers' interest to not deliver such investments during those price controls, why it would be in the customers' interest to fund such investments again and what assurances the company can provide to ensure it is delivered during RIIO-3.

6.7 In support of costs proposed, business plans should include the following:

- Evidence their costs are efficient, for example, when compared to historical benchmarks (including previously contracted costs) and/or benchmarking with national and international comparators (including any recently tendered submissions and costs observed internationally for equivalent pieces of equipment). This evidence should also be supported by the network company's Workforce and Supply Chain Resilience Strategy with respect to how the network company's procurement approach maximises competitive tension to deliver market-frontier levels of pricing and non-price terms and secures long-term capacity to create pricing visibility and stability over at least the RIIO-3 period.
- Details of assumptions and justification for projected changes in the efficient levels of unit costs over time (ie ongoing efficiencies to offset real pricing pressures) generated by improvements in project delivery approach, technological innovation, procurement efficiencies and innovation, etc (refer also to the Ongoing efficiencies section below).
- A clear rationale for any associated assumptions network companies consider we should use when assessing costs. For example, robust and transparent

justification for the extent to which regional and company-specific factors determine material (higher and lower) cost variations/

- Details of the activities and indicative costs that network companies propose are directly funded through totex allowances and that will be associated with achieving the required service levels.
- Details of which categories of expenditure are more uncertain and more difficult to forecast using historical/independent benchmarks. This should include:

  (1) the risk of underutilisation/stranding that new/existing investments might face in the future under a range of plausible forecast scenarios;

  (2) the risk that an alternative solution may be the most efficient means of addressing the network requirement;

  (3) the risk that the investment is premature; and

  (4) where this is the case, we expect companies' business plans to demonstrate consideration of mechanisms that mitigate risk associated with uncertainty, and/or other evidence to justify their submitted costs.

6.8 Network companies should submit a Cost Assessment and Benchmarking Approach Annex to detail all of the above. For the GD sector, this includes considerations around the application of regional factors and robust justification for company specific factors. For all sectors, the Annex should also include a section on frontier shift. We provide more details on the information required in paragraphs 6.12-6.15.

6.9 For new or existing assets that face a risk of underutilisation, business plans should set out the monitoring and mitigation network companies will put in place to reduce this risk. For new assets (ie those assets that companies are planning to invest in and have included in business plans) that face a risk of underutilisation, network companies should ensure before undertaking the investment they have clear evidence of need.

6.10 Where a network company considers an investment is certain under all scenarios, it should provide justification for this view.

6.11 Business plans should demonstrate how network companies' expenditure forecasts map onto relevant ODIs and PCDs.

## Frontier Shift

### Real Price Effects (RPEs)

6.12 Real Price Effects (RPEs) relate to the changes in the price of inputs used by network companies above a general inflation measure. To enable us to assess RPEs appropriately, network companies should provide us with the following information in their Cost Assessment and Benchmarking Approach Annex:

- The input costs for which our measure of general output price inflation (ie CPIH) is a poor proxy, along with justification for why.
- The expenditure categories (eg direct opex) to which these input costs relate, and to what extent. Network companies should consider the practical implications of their proposals, and in doing so to show that each RPE is material relative to both totex and our measure of general output price inflation. This information should align with the data provided in the BPDT.
- Evidence as to what extent our existing RIIO-2 approach is not appropriate for RIIO-3.
- Evidence to support all proposed RPEs and their proposed weighting (or changes to existing RPE weighting), including clear evidence of a sustained and material deviation between input costs and our measure of general output price inflation.
- Proposed indices for any proposed RPEs, along with evidence to support their use in indexation and justification for their selection over alternatives. The plan should include proposed forecasts for any proposed indices, along with evidence of how these have been derived.
- An explanation of any RPE cost profiling effects proposed through the price control.

### Ongoing efficiency

6.13 Our ongoing efficiency assumptions represent the reduction in the volume of inputs required to produce a given volume of output, ie the productivity improvements that we consider even the most efficient company is capable of achieving.

6.14 To enable us to assess ongoing efficiency appropriately, network companies should set out in their business plans the ongoing efficiency assumptions submitted for each expenditure category, along with evidence of how these assumptions have been derived. This could include:

- any proposed comparator industries for the purpose of cost assessment, along with a justification for those proposed;
- an explanation of how any historical data has been used to derive efficiency forecasts, including a justification for the time period selected and how forecasts capture enduring effects from efficiencies generated in previous price controls;
- a comparison of efficiency forecasts against efficiency gains realised in previous periods;
- interactions with innovation stimulus funding and deployed innovation projects (past and future);
- interactions with proposed capex and any benefits to reducing opex (eg through automation or standardisation); and
- interactions between ongoing efficiency forecasts and output quality.

6.15 This information should be included in the Cost Assessment and Benchmarking Approach Annex and should align with the data provided in the BPDT and in the BPDT guidance. All cost forecasts within the BPDT tables should exclude real price effects and ongoing efficiency assumptions apart from the RPEs and OE tab as instructed in the BPDT guidance. For avoidance of doubt, catch-up efficiency should remain embedded in the costs in the BPDT.

## Growth Duty

6.16 The Government has amended the Economic Growth (Regulatory Functions) Order 2017 to extend the Growth Duty to Ofgem. Our new statutory duty entered into force on 21st May 2024.

6.17 The Growth Duty requires Ofgem to 'have regard to the desirability of promoting economic growth’ when exercising our regulatory functions. The Growth Duty Statutory Guidance updates the definition of growth to sustainable economic growth.

6.18 Network companies should therefore explain how their business plan will contribute to sustainable economic growth for the wider UK economy in the medium to long term, both within the energy sector and more broadly.

6.19 Companies should include in their business plans a forecast of the jobs created from their overall plan.

## Data and digitalisation

6.20 We are committed to furthering the digitalisation of the energy sector and to unlocking the value of both demand data and energy system data as a continuation of the approach we took to RIIO-ED2 and the recent RIIO-2 Non-operational IT CAPEX re-opener decisions.[14] In these re-opener decisions, we rejected some spending relating to internal enterprise architecture. We considered the lack of data being made available to licensees' data users meant that many licensees did not receive sufficient data requests to have a clear view of where exactly investment was needed.

6.21 Companies have since progressed on their compliance with Data Best Practice Guidance[15] and making data open to customers, and we believe that companies can now make a stronger case for these investments.

### Justification of investment proposals

6.22 Where companies propose investment in RIIO-3 to deliver digitalisation initiatives or digital actions (this spend should not be for business-as-usual IT upgrades), these should be included in the BPDT, and should be clearly referenced through the business plan. To explain and justify these investments in the business plan, licensees should present objectives that are specific, measurable, achievable, relevant, and time bound.

- Specific: Identify the deliverables which will achieve the desired outputs. It should be clear how these deliverables integrate and interface with existing systems, for example is it a new standalone system, an extension of an existing system or a replacement for an existing system?
- Measurable: Propose relevant performance measures which will enable stakeholders and Ofgem to evaluate the licensee’s progress in digitalisation initiatives or digital actions outcomes. These performance measures will also need to have a specific definition that is available to stakeholders.

[14] Network price controls 2021-2028 (RIIO-2) | Ofgem
[15] Decision on updates to Data Best Practice Guidance and Digitalisation Strategy and Action Plan Guidance | Ofgem

- Achievable: Identify any dependencies on stakeholder engagement or other development works that should be completed before works can start. Where delivery plans and risk assessments are available, they should be referenced.
- Relevant: Identify investments in digitalisation initiatives or digital actions required to meet baseline expectations as detailed in Appendix 5. These investments should be clearly identified and should align to the BPDT. Licensees should identify the outputs arising from the digitalisation initiatives or digital actions and should indicate if additional new funding is required. Outputs should be clearly linked to the Digitalisation Strategy and Action Plan (DSAP) and the associated stakeholder engagement outcomes.
- Time-bound: Deliverables and objectives should have a clear timeframe, linked to the relevant licensee's DSAP.

6.23 In order to support the licensees in establishing a clear articulation of what digitalisation initiatives or digital actions are being proposed, we intend to engage closely with the companies. Licensees should include a specific section in their business plans related to digitalisation investment. We encourage licensees to re-submit rejected re-opener proposals, with improved business cases, alongside new investment in digitalisation as part of their business plans. We do not expect licensees to submit EJPs for digitalisation investments, as this information should be covered by their core business plan submissions. Licensees are encouraged to show the different options that have been considered when proposing an investment in the digitalisation section of their business plan.

### Digitalisation Strategy and Action Plan

6.24 There is a licence obligation on licensees to publish a Digital Strategy and Action Plan (DSAP). The purpose of this licence obligation is to make information publicly available about licensees' intentions and plans for digitalisation of their energy networks and associated Products and Services for data.

6.25 The effectiveness of the DSAP hinges on high quality information and insight about stakeholders and their needs.

6.26 Licensees should identify, learn about, and understand the data-related needs of their staff and external stakeholders. This includes those who currently makes use of Energy System Data, and those who seek to use that data now or in the future. This should then be integrated into regular business activity and the learnings from this have to inform the basis of the DSAP.

6.27 As part of the business plans, licensees should set out how they have approached, and will continue to approach work to develop their DSAP (particularly its identification of the stakeholders who seek to use data controlled by a licensee and how it engages those stakeholders to understand their data-related needs). As part of this, business plans should include:

- a description of a methodology(ies) that the licensee has used to identify its stakeholders and to engage with them to learn their data and digitalisation needs;
- separately, a description of any planned changes to the ongoing use of this methodology;
- the evidence accrued through the application of this methodology, including demonstration of how the Digitalisation Action Plan component of the DSAP has been derived from this evidence;
- evidence of licensee communication and feedback events or activities with stakeholders about how their needs have been interpreted and formed the basis of the DSAP; and
- plans of any future licensee communication and feedback events or activities with stakeholders about how their needs have defined the DSAP objectives and associated actions.

6.28 The approaches referred to in the above paragraph should:

- be strategic and proportionate, taking advantage of recognised practices, for example through defining personas that characterise stakeholder groups and their needs;
- be inclusive of all stakeholders, including inclusivity of hard-to-reach groups and groups which operate in markets outside of the energy sector, as well as the needs of both existing and future consumers; and
- show consideration both of active methods of engagement (such as a mix of direct invites for stakeholders to engage through points of contact and events) and passive methods of engagement (such as integrating learning about data needs into other stakeholder engagements or by speculatively publishing data and making it discoverable to test market interest).

6.29 Licensees should reference their DSAPs published in March 2024 as part of their business plan. These references can then be used to justify spending in the business plan. We consider tying business plan spend to DSAP actions to be evidencing strong justification for the investment, given the levels of engagement with data users and strategic development used to develop a DSAP.

6.30 Whilst tying business plan spend to DSAP actions is valuable, we understand that not all Business Plan spend will be present in the DSAP published in March 2024, due to the long-term nature of the price control. We do not, therefore, expect all spend in business plans to be linked back to DSAP actions.

### Data Best Practice

6.31 Complying with DBP Guidance will ensure day-to-day working with data maximises benefits for its users, whilst also complying with the needs of security, privacy, commercial concerns, and serving the public good. The time and cost burdens associated with working with data will be minimised for the benefit of consumers.

6.32 This LO was introduced on all licensees which operate under the RIIO Price Controls as part of RIIO-2 and RIIO-ED2. As such, DBP Guidance is becoming/is already part of BAU in RIIO-3. We still expect to see spend during the RIIO-3 price control to achieve compliance with DBP Guidance. We understand that each company is at a different level of compliance with DBP Guidance and, therefore, different investments will be made by different licensees. Licensees are required to demonstrate how individual projects within their business plan help further their compliance with the DBP Guidance.

6.33 We carried out a consultation to formalise amendments to the DBP Guidance in Summer 2023. For all business plan submission purposes, licensees should refer to the most recent version of the guidance available on the Ofgem website.

6.34 Business plans should:

- demonstrate how they meet the existing licensee competency at complying with the Data Best Practice Guidance under the current price control period;
- the plan for how any gaps in this competency will be covered before the start of RIIO-3; and
- developing and enhancing existing competence during RIIO-3.

6.35 The demonstration of existing competency should include specific examples of the most mature and advanced data work licensees have carried out with respect to their ability to comply with the DBP Guidance. This will help to provide assurance to us about the current capability each licensee has in place. Compliance with the DBP Guidance is a process that is individual to each licensee - companies should indicate whether and when full compliance with the DBP will be reached through proposed investments in RIIO-3. If full compliance is not likely to be reached, licensees should indicate where future investments will still need to be made.

6.36 When providing examples about the existing competency and compliance with DBP, the following is a guiding list of the types of information companies should submit:

- Examples that span meeting the needs of users of the data which are both internal and external to the licensee.
- A demonstration of how these examples do and do not yet meet the Data Best Practice Guidance principles.
- Relevant supporting work (for example a licensee's chosen framework for conducting open data triage, the data standards it is adopting).
- A range of data triage outcomes, showing instances of the licensee determining data to be classifiable as fully open, shared and closed.
- Cases where data has required sensitivity mitigation as part of its open data triage and details about this process (such as examples of how the utility of the data has been maximised, within the constraint of mitigating the associated sensitivity).
- Evidence from the direct users of data about how their needs have been met.
- An interoperable data platform, as required in the August decision on updates to DBP,[16] with examples of datasets triaged as suitable for publication.
- Use of Dublin Core 15 fields in metadata.
- Use of the most recent iteration of either Open Government Licence (OGL) or Creative Commons Licence (CCL) in licencing data.

6.37 Regarding information on the plan for how any gaps in competency are being addressed, duplicated information that is already available to us in the licensee's published DSAP need not be submitted. This is an optional opportunity for licensees to share additional information with us, where the licensee believes that

[16] Decision on updates to Data Best Practice Guidance and Digitalisation Strategy and Action Plan Guidance | Ofgem

the examples of its current competency at meeting Data Best Practice and its published Digitalisation Strategy and Action Plan do not fully explain how the licensee will become compliant with the DBP Guidance.

6.38 Our guiding comments regarding this planning are that the depth of information a licensee provides should be proportionate in the context of the overall business planning process and that the information should be directly relatable to the principles of our Data Best Practice guidance.

6.39 Where companies propose investment in RIIO-3 to adopt or improve compliance with the DBP Guidance, these should be included in the BPDT, and should be clearly referenced through the business plans. To explain and justify these investments in the business plans, companies should;

- Identify the outputs arising from the investment which should be clearly linked to closing identified gaps against the Data Best Practice Guidance principles.
- Identify the deliverables which will achieve the desired outputs, deliverables should be specific, time-bound, and relevant. It should be clear how this investment integrates with existing systems. For example, is it a new standalone system, an extension of an existing system, or replacement for an existing system. Consideration should be given to interoperability and future-proofing compliance; for example, not using vendors with licence terms incompatible with Open Data Licences, if there is a possibility of the data being triaged as Open.
- Identify any dependencies on stakeholder engagement, or other development works, which should be completed before works can start. Where delivery plans and risk assessments are available, they should be referenced.
- Propose relevant performance measures which will enable stakeholders and Ofgem to evaluate the licensee’s progress against Data Best Practice Guidance.

### Data Sharing Infrastructure

6.40 A Data Sharing Infrastructure (DSI) is a means to facilitate the secure, trusted, and efficient exchange of data between different systems, organisations, or entities. This in turn enables greater collaboration and innovation across the energy sector. In our FSNR decision, we outlined the context behind, and constituent components of a DSI.[17]

6.41 Many of the broader digital investments that will be made as part of RIIO-3 will have an enabling effect for connecting to, and using, the DSI. Licensees should signpost in business plans their expectations of what spending is needed to connect to the DSI, including indirect investments that will improve general capability and direct investments explicitly for connecting to a DSI. These will include investments in; enterprise architecture, security, internal data models, data quality tools, and improving data pipelines.

[17] Future Systems and Network Regulation: Framework Decision Overview (ofgem.gov.uk)

# 7. Financial information

## Financial BPDTs and Business Plan Financial Model (BPFM)

7.1 Companies should provide financial information as set out in this section.

7.2 We will provide financial tables in the BPDT to gather relevant information. This includes information on tax, pensions, asset disposals and debt etc. Companies should use the financial BPDTs and the Business Plan Financial Model (BPFM) to submit business plan information, including any analysis presented in the plan such as financeability or investability analysis, scenarios or tables of values.

7.3 Companies may provide two versions each of the BPDT and BPFM. One version will reflect Ofgem's parameters as outlined in the SSMD. The second version allows companies to provide their specific plans with alternative scenarios and inputs. If companies submit a second, bespoke, BPDT, changes must only be made to the finance-related (F) BPDT tabs.

7.4 If any other models or tools are used to produce alternate or supplementary analysis, such as bill impacts or alternate financeability scenarios, then these should be submitted with, and clearly cross-referenced to, the business plan. Where applicable, inputs to the BPFM should be linked to the corresponding BPDT.

7.5 Companies may provide additional BPFM commentary in an appropriate form if they feel additional context would be beneficial.

7.6 We will pre-populate the BPFM with all relevant parameters set out in the SSMD Finance Annex. These represent our working assumption for those parameters at the date of the SSMD and remain subject to change in accordance with our Draft Determination and Final Determination. The BPFM will allow companies to populate it with their plans to calculate expected allowed revenues. It will also be used for assessing the financeability of the business plan and will include a suite of commonly used financial metrics.

7.7 Consistent with RIIO-2, the BPFM will primarily be set up to reflect the notional capital structure. However, worksheets will be included to allow analysis of the actual company financing costs, structure and performance.

7.8 Companies should complete the BPFM in accordance with the guidance set out here and the BPFM Guidance at Appendix 3, including incorporating our working assumptions for cost of capital returns and regulatory depreciation. Companies should also include a financeability assessment (using our working assumptions for cost of capital returns) for both the notional and actual capital structure, including target ratings.

7.9 Business plans should clearly set out:

- Financial projections for each year of the RIIO-3 period under the specified regulatory finance framework, on a notional and actual company basis. The financial projections should consist of the model outputs listed in the BPFM Output Sheet of the BPFM, as well as the results of any stress tests that the licensee considers to be appropriate. Note that this is a requirement for final business plans only.
- A clear explanation of any additional stress test scenarios, including rationale, results and commentary of results.
- The company's target ratings (including consideration of the trade-offs of different target rating levels) and the key financial ratios and qualitative factors used to assess maintenance of those target ratings.
- The results of any future Ofgem-prescribed set of common stress test scenarios (as described in the SSMD) with results clearly explained.
- A clear explanation of the company's proposed capitalisation rates and regulatory depreciation rates and the basis for these proposals (for example, whether proposed capitalisation rates match accounting treatment of opex and capex). However, for the purposes of completing the BPFM and financeability assessment, companies must use the pre-populated assumption for capitalisation and regulatory depreciation.
- If any adjustments to capitalisation rates or depreciation rates are proposed for financeability, networks should include evidence for these adjustments and a well-evidenced demonstration that it is in customers' interests.
- Any proposed alteration of the profile of revenue and the purpose and level of support for the proposed profile.
- Clear explanation of the company's dividend and equity issuance policy and strategy and how this influences assumptions in the BPFM.

7.10 Business plans should clearly demonstrate, on a notional company and an actual company basis:

- A clear understanding and assessment of the financial risk in the business plan and evidence of risk management measures. This should include:

(1) a clear explanation of the assumptions underpinning company risk;

(2) risk scenario analysis;

(3) a description of how financial risk analysis takes into account company actions for mitigating downside risks;

(4) consideration of different gearing levels including consideration of cost and benefit trade-offs of different gearing assumptions; and

(5) realistic and well-explained proposals for gearing.

- Justification for any proposed company-specific alternative cost of capital estimates, including a well-evidenced demonstration that it is in customers' interests.

7.11 Business plans should also include licensee Board assurance that the Board is satisfied that the licensee is financeable on both a notional and actual capital structure basis (using our working assumptions for cost of capital allowances and other pre-populated parameters). This should cover the baseline level of totex as well as the 'best view' level of totex (ie including forecast re-opener spend) as described in the BPDT guidance. Alternatively, if any financeability challenges are identified, the Business Plan should clearly set out:

- details of what these financeability challenges relate to (for example, servicing equity or debt);
- what management efforts or mitigating actions could reasonably be made to address them;
- what regulatory measures should be taken alongside the management efforts or mitigating actions;
- that all other applicable measures to aide financeability have been considered; and
- that statements and conclusions are supported by evidence and justification.

## Financial modelling assumptions (financeability assessments)

7.12 For the purposes of modelling both the notional capital structure base case and the actual capital structure base case, companies should use the assumptions:

- Allowed return on capital as set out in the SSMD Finance Annex.

- Totex allowances are assumed to be equal to licensee totex cost forecast for RIIO-3, ie no over- or under-spend.
- Opening RAV to be based on totex forecasts for RIIO-2 as provided in the BPDT submission, and inclusive of any known logged-up adjustments (eg the impact of any anticipated close-out adjustments).
- Capitalisation and Regulatory Depreciation rates stated in the BPFM Guidance.
- Capitalisation rates to be proposed by the licensee reflective of the accounting distinction between opex and capex, and therefore assumed to be the 'natural rate'.
- An approach to inflation indexation as described in the SSMD Finance Annex.

7.13 Assumptions specific to modelling the notional capital structure base case:

- Gearing levels assumed to be in line with those set at the end of RIIO-2.
- Net debt is reset to the working assumption notional gearing level at the start of RIIO-3, with any opening de-gearing assumed to be achieved by an equity injection or re-gearing assumed to be achieved by debt issuance.
- Debt costs are assumed to equal the forecast average efficient debt costs set out in the SSMD Finance Annex.
- 30% of the licensee's debt is assumed to be CPIH linked (with a scenario test showing an alternative of 30% RPI-linked debt).
- Tax allowances are equal to tax costs, as calculated using the BPFM.
- Lagged revenue impacts arising from RIIO-2 are excluded (eg the ADJ and K terms).
- Dividend yield working assumption for modelling purposes as specified in the BPFM Guidance.
- Equity issuance transaction costs working assumption of 5% of any amount forecast to be issued.

7.14 Assumptions specific to modelling the actual company base case:

- Opening net debt to reflect actual company forecast net debt position as completed in the finance tables of the BPDT, with ongoing net debt over the course of RIIO-3 calculated by the model.

- Debt costs forecasts to reflect actual company debt costs for embedded debt and working assumptions for new debt.
- Proportion of inflation linked debt and proportion of interest expense that is principal inflation accretion in each year to reflect actual company forecast, as set out in the finance tables of BPDT.
- Modelled forecast actual tax costs, incorporating forecasted financial information in accordance with the BPDT.
- Lagged revenue impacts arising from RIIO-2, where these are expected, should be included if relevant (eg ADJ or K from RIIO-2 revenues).
- Dividend and equity issuance to reflect actual company dividend policy and forecast equity issuance, as set out in the finance tables of the BPDT.
- Equity issuance transaction costs to reflect actual company costs by licensee for forecast equity issuance.

# 8. Presentation and submission requirements

8.1 Business Plans should be concise and no longer than 100 pages excluding annexes and other submission documents listed in Table 2, with the emphasis on keeping the core text as succinct as possible, while presenting proportionate evidence and justification for the proposed expenditure and outputs. Emphasis should be made on making Business Plans as visually accessible as possible (ie font sizes should be no smaller than 10 and appropriate margin spacing should be maintained).

8.2 Companies should only provide annexes for the policy areas stated in the table below. Each annex's page limit is set out in Table 2 below and this will not count towards the core business plan page limit. Annexes should be clearly cross referenced within the core business plan text.

8.3 Each company should submit a Strategic Summary alongside its final business plan detailing the key data and information contained within its plan. Companies should use the common reporting template published alongside this Business Plan Guidance.

8.4 Although we do not prescribe a particular structure that the business plans themselves should follow, it is important to ensure that we can easily identify material contained in the plans and any annexes that will be relevant to our assessment.

8.5 Where companies have commissioned reports from consultants to support their business plan submission, companies should provide executive summaries within the relevant parts of their submission, with full reports included as additional annexes to the business plan. The executive summaries should cross refer to the relevant annexed reports.

8.6 Subject to paragraph 8.5, companies should submit only the documents set out in Table 2 below as part of their business plan.

Table 2: List of business plan submission documents

| Document name | Page count limit | Sectors |
|---|---|---|
| Business Plan Main Document | 100 | ET, GD, GT |
| Strategic Summary | Template provided | ET, GD, GT |
| Environmental Action Plan | N/A | ET, GD, GT |
| Climate Resilience Strategy | 50 | ET, GD, GT |
| Workforce and Supply-Chain Resilience Strategy | 50 | ET, GD, GT |
| NIS Self-Assessment and Improvement Report | Template available here | ET, GD, GT |
| NIS-R Cyber Resilience Investment Document | Template provided | ET, GD, GT |
| NIS-R Cyber Resilience Detailed Costs | Template provided | ET, GD, GT |
| Digitalisation Strategy & Action Plan | No change to regular submission | ET, GD, GT |
| Statement from ISG Chair | N/A | ET, GD, GT |
| Stakeholder Engagement and Decision Log | 5 (Template provided) | ET, GD, GT |
| ET Load Strategy | 50 | ET only |
| Innovation Strategy | 50 | ET, GD, GT |
| Network Asset Management Strategy | 50 | ET, GD, GT |
| Assurance Statement | 25 | ET, GD, GT |
| Finance annex | 50 | ET, GD, GT |
| System Operator annex | 120 | GT |
| IT & Telecoms Strategy | 25 | ET, GD, GT |
| Cost Assessment and Benchmarking Approach (including RPEs and OE) | 100 | ET, GD, GT |
| Investment Decision Packs (IDPs) | Refer to IDP Guidance | ET, GD, GT |
| Business Plan Data Templates (BPDT) | Template provided | ET, GD, GT |
| Business Plan Data Templates (BPDT) Commentary | Template provided | ET, GD, GT |
| Network Asset Risk Metric (NARM) BPDT | Template provided | ET, GD, GT |
| Network Asset Risk Metric (NARM) BPDT Commentary | Template provided | ET, GD, GT |
| Business Plan Financial Model (BPFM) | Template provided | ET, GD, GT |
| Statutory Independent Undertakings Annex | 30 | SGN only |
| Draft Joint-GDN Vulnerability Strategy | N/A | GD only |
| Vulnerability Strategy | N/A | GD only |

## Cross referencing and duplication

8.7 In order for us to navigate the plans successfully, companies should effectively cross reference between different sections of the plans. Wherever possible, companies should use hyperlinks when referencing any of the data tables, annexes or any further detail which is explored elsewhere in the plan.

8.8 Data tables produced by companies should be clearly numbered and any data in the narrative should, where possible, be clearly linked to the relevant data table number (using hyperlinks wherever possible). For each data table there should also be a link to where in the core text this data is discussed. For some data tables there may be more than one part of the plan that describes the data.

## Track record and business plan commitment

8.9 In assessing business plans, we will consider how deliverable the plans are in the context of past performance and the level of commitment provided for delivering the activities and outcomes set out in the plan.

8.10 Business plans should be prepared in accordance with the requirements set out in this document and in accordance with all associated appendices and templates.

## Assurance and governance

8.11 Robust assurance and governance of business plan submissions is vital if stakeholders, including Ofgem, are to have confidence in the information presented in them. The submission can only be complete and of high quality where there are assurance checks on the systems and processes for developing and producing the business plan, and when stakeholders have confidence that a company's board has been integral to the governance surrounding the submission.

8.12 It is for the companies and their boards to determine the precise role that assurance plays in this process. We expect company boards to own and be accountable for their submissions and the business planning processes that underpin all aspects of the business plan.

8.13 All assurance processes undertaken by the company should be clearly set out in the company's Assurance Statement. The Assurance Statement should include a statement from sufficiently independent directors that they are satisfied that the business plan and the associated proposed costs and financial package have been appropriately challenged for accuracy, ambition, efficiency and customer interest.

A sufficiently independent director is as described in SSC A42 (Requirement for sufficiently independent directors) of the GD and GT licences and SLC B22 of the ET licence.

## Publication and redaction requirements

8.14 Companies must publish their complete business plan, in a prominent place on their website, in such a manner that it can be easily located by relevant stakeholders, on the same date that the submission is sent to Ofgem.

8.15 Companies must publish their business plans in their entirety, making only necessary redactions for the following reasons;

- commercial confidentiality; and
- security.

8.16 The reasons for such redactions must be clearly and comprehensively set out in an explanatory statement published alongside the plan. For example, if information is redacted on grounds of commercial confidentiality, we would expect to see an explanation of the particular commercial interest that the company considers would be prejudiced by disclosure.

## Business Plan templates

8.17 To The following templates are included in Annex 7:

- BPDT Templates
- BPDT commentary template
- BPFM Templates
- CBA Templates
- EJP Templates
    - EJP GD/GT templates
        - Major Project EJP - GT3 & GD3 Template.docx
        - Asset Health EJP - GT3 & GD3 Template.docx
        - Non-Load Capex EJP – GT3 & GD3 Template.xlsx
    - EJP ET Templates
        - Major Projects EJP - ET3 Template.docx

        - ESO Driven Works - ET3 Template.docx
        - Atypical Non-Load, Non-Lead Intervention - ET3 Template.docx
        - T3 EJP Portfolio - Template.xlsx
        - T3 EJP Portfolio NL - Template.xlsx
- NIS-R Cyber Resilience Templates
    - NIS-R Cyber Resilience Investment Document Template_v1.0.docx
    - NIS-R Cyber Resilience Detailed Costs Template_v1.0.xlsx
- Strategic Summary Sheet - Template.xlsx
- Stakeholder Engagement and Decision Log
- NARM workbooks
- NARM workbooks commentary template

# 9. Business Plan Incentive

9.1 This section describes how we will assess business plans for the purposes of the Business Plan Incentive (BPI).[18]

9.2 The purpose of the BPI is to overcome information asymmetries between Ofgem and the companies and to motivate companies to develop high-quality, ambitious, business plans that embed efficiency and represent value for money for consumers.

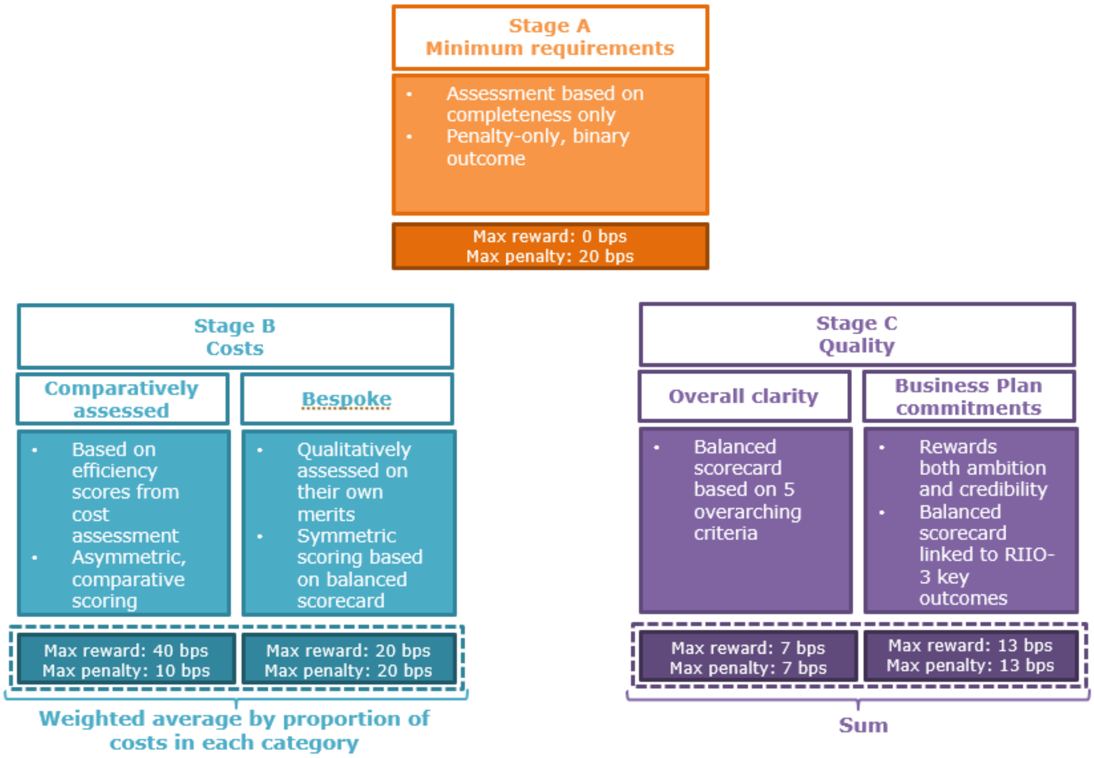
9.3 The monetary value of the BPI shall be calculated at Final Determinations and applied annually. The annual values shall be calculated ex ante as the assessed total reward or penalty measured in basis points of Return on Regulated Equity (RoRE) (capped at ±60 basis points), multiplied by the equity portion of the forecast Net Present Value (NPV) neutral Regulatory Asset Value (RAV) for the respective year, based on the relevant notional gearing assumption for each licensee.

9.4 The NPV neutral RAV for the purpose of the BPI shall be derived from the baseline RIIO-3 totex set at Final Determinations, excluding RIIO-3 re-openers, RIIO-2 re-openers (eg ASTI, LOTI and MSIPs), UIOLIs, opex escalator, ongoing efficiency and RPEs, but including volume drivers with baseline volumes. The total monetary value of the BPI, for the RIIO-3 price control period shall be the sum of the respective annual values.

9.5 We provide an overview of the BPI framework in Figure 3 below.

[18] In RIIO-2 Ofgem used a four-stage BPI as an asymmetric information incentive. In RIIO-3, we have decided to use a modified and streamlined 3-stage BPI.

Figure 3: Overview of the RIIO-3 BPI




9.6 In RIIO-3, the BPI will consist of three stages:

- Stage A - we will assess whether a business plan contains the minimum amount of information required for us to set the price control effectively, in line with the guidance issued in this document. It will only focus on the completeness of the submission. This assessment will result in a penalty of 20 bps of RoRE if any minimum requirements are not met.
- Stage B - we will assess whether the costs submitted as part of the business plan are adequately justified and efficient. We will use two separate assessment methodologies, one for costs which are assessed comparatively, and one for more bespoke costs. This assessment will result in a maximum reward of 40 bps of RoRE or a maximum penalty of 20 bps of RoRE, calculated as a weighted average between the two methodologies.[19]

[19] The weighted average will use the proportion of costs assessed with each methodology as the relative weighting.

- Stage C - we will assess the quality of the business plan in the round with regards to i) its overall clarity and ii) the ambition of the commitments contained within it. The assessment of clarity will account for a maximum of ±7 bps of RoRE and the assessment of commitments will account for a maximum of ±13 bps RoRE. This assessment will therefore result in a maximum reward or penalty of ±20 bps of RoRE.

9.7 Stages A and Stage C will be assessed using the business plan and supporting information submitted by the relevant network company. Where a network company is responsible for more than one network, Stage B will be assessed and calculated at the level of each network, consistent with the cost assessment process.

9.8 We will make our decision on the BPI with regard to the principles of transparency, accountability and proportionality and other principles of best regulatory practice. At Draft Determinations we will publish a summary of our assessment, including, for each company, the proportion of costs that have been assessed comparatively and on a bespoke basis and the scores for the two parts of Stage B, the scores for the two parts of Stage C and whether or not a company has failed to meet the minimum requirements at Stage A.

9.9 The remainder of this section sets out how the assessment will be carried out for each stage. The rationale for our approach is set out in Chapter 7 of the RIIO-3 Sector Specific Methodology Decision Overview document.

## Stage A: Minimum requirements

9.10 In Stage A of the BPI we will assess whether a business plan meets the minimum requirements set out in Table 3 below. We will assess the fulfilment of each minimum requirement individually on a pass/fail basis. The failure of a single minimum requirement will result in the failure of Stage A as a whole and the company will receive a penalty of 20 bps of RoRE.

9.11 We will assess the fulfilment of the minimum requirements solely on completeness, ie whether all of the necessary submissions requested as part of the minimum requirement have been provided. We will assess the quality of the business plan submission separately, as part of Stage C.

9.12 We will assess the fulfilment of the minimum requirements on the information provided in the first submission of the business plan. Any subsequent information provided by the companies, even if requested by Ofgem, will not be included in our assessment of Stage A of the BPI.

9.13 Companies who fail Stage A will still be assessed for a reward or penalty under Stages B and C of the BPI.

9.14 For the avoidance of doubt, where we decide that a business plan has successfully met the minimum requirements at Stage A, that does not imply acceptance of all aspects of the plan (or relevant underlying evidence). Companies still have the potential to face a penalty under Stages B or C of the BPI. Ahead of reaching a decision on the BPI, we will consult in our draft determinations.

**Table 3: BPI minimum requirements**

| Min Req. Ref | Business Plan Area | Sector | Minimum Requirement |
|---|---|---|---|
| 1 | Load and regional strategies | ET | The electricity TO must provide evidence through its 'load strategy' that its load related investment plan has been informed by multiple factors. These factors must include the transitional CSNPs, local contracted connections (including expected attrition rates), the condition of existing assets, interfaces with the electricity distribution network and supply chain constraints (including setting out what actions are being taken to manage relationships with suppliers and contractors).<br>The electricity TO must provide evidence of how it has used strategic investment to manage uncertainties considering those factors set out above. |
| | | GD<br>GT | Where applicable, the gas network company must provide evidence of how any proposals included in its business plan for investment to prepare the network for decommissioning, repurposing for hydrogen or CCUS, or other hydrogen-related costs are justified to be funded through RIIO-3, including explaining why the costs reflect the decisions we set out in the Future of Gas chapter of our SSMD Overview Document. |
| | | All | The network company must develop its business plan using FES 2024 Holistic Transition pathway in accordance with the requirements of the relevant sector-specific guidance in Chapter 4 of the Business Plan Guidance. |
| 2 | Secure and resilient supplies | All | The network company must provide evidence of how its RIIO-3 business plan ensures the continued resilience of the network through its non-load related expenditure. This must include plans to effectively manage the impact of asset age and condition, extreme weather events, cyber-attacks and the physical security of its network. |

| Min Req. Ref | Business Plan Area | Sector | Minimum Requirement |
|---|---|---|---|
| | | ET | The electricity TO must provide evidence of how its plan for load-related expenditure has been influenced by, and consistent with, its non-load expenditure plan. |
| | | GD | For non-mandatory repex workload proposals, the GDN must provide evidence that it has considered alternative options and deferral of investment. |
| | | GT | National Gas must provide evidence of how its network capability analysis underpins its RIIO-GT3 business plan, including analysis of physical capabilities for each zone and the level of capability that can economically and efficiently be delivered through commercial tools. |
| | | GT | National Gas must engage with National Energy System Operator (NESO) on its network capability analysis and on the assumptions underpinning its business plan and submit the NESO's view of the underlying assumptions of the business plan. |
| 3 | Managing uncertainty | All | The network company must provide evidence of how it decided which projects or programs should be included in its RIIO-3 baseline funding request, and which should be subject to an uncertainty mechanism, with reference to cost confidence, the level of project development and delivery implications of seeking later project approval. |
| 4 | Quality of service | All | The network company must provide evidence of how its RIIO-3 business plan will deliver a high quality and reliable service to consumers and network users, including through the provision of a reliable supply and excellent customer service. |
| | | GD | The GDN must provide evidence that its business plan has been informed by its vulnerability strategy, particularly in relation to how it will deliver customer service activities and other activities to support consumers in vulnerable situations. The GDN's vulnerability strategy must have been developed and maintained based on engagement with stakeholders. |

| Min Req. Ref | Business Plan Area | Sector | Minimum Requirement |
|---|---|---|---|
| 5 | Environmental Impact | All | The network company must provide an Environmental Action Plan, in a manner prescribed by the relevant guidance, containing evidence of how its planned activities mitigate the environmental impact of its network. |
| | | ET | The electricity TO must provide evidence of how its environmental impact will be affected by the construction and operation of new and upgraded network infrastructure during RIIO-ET3. |
| | | GD | The GDN must provide evidence that it has worked with stakeholders to develop targets to reduce shrinkage by the end of RIIO-3, and the EAP must explain clearly how the GDN will deliver against these targets. |
| 6 | Stakeholder Engagement | All | The network company must include a summary, using the template provided, demonstrating how it used engagement with key stakeholders (eg connection customers, consumer groups, local communities) to inform the development of its business plan, and must provide evidence where this engagement has had tangible impacts on the contents of its business plan, including (where applicable) where decisions have been taken in a manner contrary to the stakeholder feedback. |
| | | All | The network company must include a statement signed by the relevant ISG Chair, in accordance with the requirements of para. 2.10 of this business plan guidance. |
| 7 | Innovation Strategy | All | The network company must provide examples and evidence of how its RIIO-3 business plan leverages new technologies or innovative practices, including the deployment of solutions, to achieve the overall RIIO-3 outcomes (as set out in the RIIO-3 SSMC para. 2.1). |

| Min Req. Ref | Business Plan Area | Sector | Minimum Requirement |
|---|---|---|---|
| 8 | Workforce and Supply Chain Planning | All | The network company must provide evidence through its Workforce and Supply Chain Resilience Strategy of how its RIIO-3 business plan meets workforce and supply chain needs and will manage the challenges presented by the energy transition and associated investment requirements. |
| 9 | Cost | All | The network company must provide information in their business plans on:<br>- cost drivers;<br>- consideration of options;<br>- justification of costs, including proposed profiling of costs. Evidence should be provided showing how the network company produced its cost forecasts, including justification of costs, any considerations of alternative options to the one submitted and why it submitted a certain profiling of costs, especially where the latter deviates from historical trends; and<br>- how efficiency improvements and innovation will be delivered to reduce costs and/or add value for money for consumers over the RIIO-3 period. |
| 10 | Cost | All | The network company must complete the Business Plan Data Templates (BPDTs) and tab-by-tab commentary in accordance with the Ofgem BPDT guidance. |
| 12 | Engineering | All | The network company must provide Engineering Justification Papers (EJPs) which include the information requested in the IDP guidance. |

### Stage B: Efficient and justified costs

9.15 In Stage B of the BPI we will assign a reward or penalty based on our assessment of:

- the efficiency of the costs submitted within company business plans; and
- the justification provided to support those costs.

9.16 Both these areas are relevant to the assessment for all costs. However, we will use a different methodology to assess comparatively assessed costs and bespoke costs.

9.17 We will determine which costs should be treated as comparatively assessed or bespoke based on the cost assessment approach we consider most appropriate, following review of the business plans, rather than by using an ex ante categorisation. We will assess which approach to use based on the following principles. Costs will be comparatively assessed if the assessment of their efficiency relies primarily on cost information from other companies. In other words, where costs from across a sector (or even multiple sectors) are directly compared against each other in order to derive a common efficient benchmark, we will consider them to be comparatively assessed.[20] On the other hand, costs will be considered bespoke if they are primarily assessed on their own merit, without a robust ability to directly compare the same cost between different companies on a like-for-like basis.

9.18 Comparatively assessed and bespoke costs may be assessed or benchmarked using a variety of different methodologies during the cost assessment process. The chosen methodology does not mechanically determine which category we will consider costs to fall into. For example, costs that are assessed using a combination of sector-wide and external benchmarking, or top-down and bottom-up benchmarking methods which are then combined, would still count as comparatively assessed as long as they result in a like-for-like comparison with

[20]Note that while comparison can be undertaken at a sector level (ie including all companies in a given sector), it is also valid that specific costs are benchmarked across multiple sectors (for example between ET and GT). This includes where some companies in a given sector may be excluded from the comparison to make it robust.

associated efficiency scores across the sector. On the other hand, a company's costs could be assessed with a form of quantitative benchmarking which only uses external benchmarks (eg international benchmarks), rather than comparative benchmarks against other companies in the price control. In this instance, we would consider that cost to be bespoke for the purposes of the BPI Stage B.

9.19 The methodology (set out below) for comparatively assessed costs focuses on the relative efficiency of cost submissions, while the methodology for bespoke costs will focus on the justification of costs on their own merit.

9.20 Submitted costs for the purposes of Stage B of the BPI will only comprise of costs to cover activities for which companies will receive baseline allowances as part of RIIO-3, as defined in para 9.4. We will consider costs after any normalisations applied to ensure a like-for-like comparison between different companies but before any efficiency-related adjustments are applied.

9.21 The overall maximum reward for Stage B is +40 bps of RoRE, while the maximum penalty is -20 bps of RoRE. The reward/penalty will be calculated by taking a weighted average between the reward/penalty for comparatively assessed and bespoke costs, using the proportion of total submitted costs falling into each category as weights. For example, if 80% of the costs of a company are comparatively assessed, while 20% are bespoke, 0.8 and 0.2 will be the respective weights used in the weighted average.

9.22 The maximum reward and penalty for comparatively assessed costs are +40 bps and -10 bps of RoRE, multiplied by the relevant weight, respectively. The maximum reward and penalty for bespoke costs is ±20 bps of RoRE multiplied by the relevant weight. The maximum reward for Stage B as a whole (+40 bps of RoRE) could therefore only be attained by a company with 100% of its costs falling into the comparatively assessed category. Similarly, the maximum penalty (-20 bps of RoRE) could only be attained by a company with 100% of its costs falling into the bespoke category.

9.23 Business Plan Guidance Annex 5: Business Plan Incentive provides more details and practical examples of how the overall reward for Stage B will be calculated.

9.24 Below we outline the methodologies used for comparatively assessed costs and bespoke costs.

Comparatively assessed costs

9.25 For comparatively assessed costs we will base our reward for Stage B on the outcome of the cost assessment. Our approach will be as follows:

- The company with the lowest efficiency score (the frontier company) will receive the maximum reward.
- The company with the highest efficiency score (the most relatively inefficient company) will receive the maximum penalty.
- Companies with lower costs than the efficient benchmark will receive a reward proportionate to their (negative) catch-up efficiency challenge, with the maximum set by the frontier company.
- Companies with higher costs than the efficient benchmark will receive a penalty proportionate to their (positive) catch-up efficiency challenge, with the maximum set by the most relatively inefficient company.[21]

9.26 For all above steps we will rely on the average efficiency scores, as well as the average efficiency benchmark, across all years in the price control period.

9.27 As stated above, the maximum reward for comparatively assessed costs in Stage B will be +40 bps of RoRE multiplied by the proportion of total submitted costs falling into this category. The maximum penalty will be -10 bps of RoRE multiplied by the same proportion.

9.28 We will consider adjustments to the maximum size of the cap and penalty if the maximum levels appear disproportionate to the overall effects on our efficiency analysis and the impact on consumers. We would only do so if we felt that the incentive value was no longer proportionate. This may arise if the cost information provided in companies' business plans has limited importance in our assessment of efficient costs, or if the cost assessment suggests there is limited differentiation between companies.[22] In this case, the same assessment

[21] As an illustrative example, suppose that the efficient benchmark is set at an efficiency score of 0.90, the frontier company has an efficiency score of 0.80, and the most relatively inefficient company of 1.20. A company with an efficiency score of 0.85 would receive a reward equal to half of the maximum reward (as its efficiency score is halfway between the benchmark and the frontier company's efficiency score). A company with an efficiency score of 1.00, on the other hand, would receive one third of the maximum penalty (as its catch-up efficiency challenge is one third of that of the most relatively inefficient company).

[22] Examples could include (but are not limited to) cases where all cost submissions less efficient than the benchmark were clustered very closely around the benchmark itself.

methodology would be followed, but using a lower maximum reward and/or penalty.

9.29 In some companies or sectors comparatively assessed costs may be assessed separately for different cost areas, without then being aggregated together in a way that produces a single comprehensive efficiency score for all comparatively assessed costs for each company. In such instances, we will carry out this methodology separately for each separate comparative assessment. The overall reward or penalty for comparatively assessed costs will then be the weighted average between the rewards/penalties of the different assessments, using the proportion of comparatively assessed costs covered by each assessment as weights. This overall reward or penalty will then, in turn, be used in the weighted average with bespoke costs to determine the overall reward or penalty for Stage B.

Bespoke costs

9.30 For bespoke costs, the Stage B reward or penalty will be based on an in-the-round assessment of the level of justification underlying the estimates of bespoke costs.

9.31 Where a proposal or commitment put forward in a company's business plan has not been accepted, the costs associated with it will not be assessed for the purposes of Stage B. Poorly justified commitments or activities may affect Stage C of the BPI, but are not intended to impact Stage B.

9.32 For activities that companies are expected to carry out during the price control period, the efficiency of submitted costs underpinning them will be assessed on their own merit, taking the activity to be funded as a given. This assessment is separate from the needs case assessment for the activity: the purpose of Stage B is to assess whether the costs to deliver a certain output or volume of work are well justified, not to determine whether the output or volume of work itself should be delivered.

9.33 The in-the-round assessment of the justification of bespoke costs will be based on the following three criteria, with equal weights:

- **Quality of cost evidence**: whether the type of evidence provided to justify costs in this area is appropriate. What evidence would be considered appropriate will depend on the specific context of the activity that is being funded. Chapter 7 of this BPG and the BPDT commentary template provide guidance around the type of evidence that companies should provide to justify costs.

- **Justification of unit cost efficiency**: the extent to which the information which has been provided adequately supports the submitted unit costs in this area, taking the activity which is being funded as a given. Unlike the previous criterion, this is not about the type of evidence provided to justify costs, but rather about the extent to which that evidence justifies the stated unit costs.
- **Justification of volume efficiency**: the extent to which the information which has been provided adequately supports the submitted volumes in this area, taking the activity which is being funded as a given. This is distinct from assessing the justification of output volumes for given cost categories. Instead, this criterion assesses the justification of volumes associated with inputs used to derive total costs, taking the output volumes as a given.

9.34 For each cost area used in the cost assessment, bespoke costs will be assigned a score for each of the three criteria above.

- **Quality of cost evidence**: comprehensive (reward), fair (no reward or penalty), or poor (penalty).
- **Justification of unit cost efficiency**: robust justification (reward), adequate justification (no reward or penalty), or poor justification (penalty).
- **Justification of volume efficiency**: robust justification (reward), adequate justification (no reward or penalty), or poor justification (penalty).

9.35 The maximum reward or penalty for this part of Stage B is ±20 bps of RoRE.

9.36 The reward or penalty for each of the three criteria, for each cost area, will be ± one third of 20 bps of RoRE, multiplied by the proportion of costs falling into that cost area.

9.37 The overall score for bespoke costs will be the sum of the (weighted) rewards and penalties falling into each cost area. This overall reward or penalty will then in turn be used in the weighted average with comparatively assessed costs to determine the overall reward or penalty for Stage B.

9.38 Annex 5 provides more details and practical examples of how the reward for Stage B will be calculated, including examples relating to bespoke costs.

### Stage C: Quality of the business plan

9.39 In Stage C of the BPI we will assign a reward or penalty based on our assessment of:

- the overall clarity of the business plan as a whole; and
- the ambition of the commitments included in the business plan.

9.40 We will assess both elements qualitatively in the round using balanced scorecards. The assessment of clarity will account for up to ±7 bps of RoRE and the assessment of commitments will account for up to ±13 bps RoRE. This assessment will therefore result in a maximum reward or penalty of ±20 bps of RoRE.

9.41 Below we outline the methodologies used for both overall clarity and business plan commitments.

<u>Overall clarity</u>

9.42 As part of Stage C we will assess the overall clarity of the submitted business plans. We will issue rewards for outstanding business plans that are presented in a clear and coherent manner, with consistent overarching goals running through the different parts. By contrast, we will issue penalties for business plans that are considered poor, where content is not presented clearly or coherently.

9.43 We will use the following criteria to assess the overall clarity of each business plan:

- Layout and structure.
- Accessibility and conciseness.
- Relevance of the information provided.
- Clarity of information that supports the demonstration of value to consumers.
- Coherence and justification.

9.44 The maximum incentive for the clarity component of Stage C will be ±7 bps of RoRE, ie approximately one third of the maximum for Stage C as a whole.

9.45 We will carry out a qualitative, in-the-round assessment of clarity of each business plan using the balanced scorecard in Annex 5, which provides further detail on how we will assess each criterion.

9.46 The assessment of clarity will apply to the full business plan submission, including all annexes but not to any further information that is subsequently provided, even where that information is requested by Ofgem.

Business plan commitments

9.47 For the purposes of Stage C of the BPI, by "business plan commitment" we mean any proposed target or activity contained in a business plan which is expected to deliver value for consumers. This includes but is not limited to PCDs, ODIs, and LOs, as well as suggested targets for them. It also includes proposals related to UMs associated with the delivery of an output or activity.

9.48 As part of Stage C, we will assess the proposed business plan commitments. We will reward commitments which are ambitious ie they deliver value for consumers over and above what is currently delivered under RIIO-2, demonstrate a clear link with what consumers value for RIIO-3 and where these commitments are underpinned by a credible needs case and delivery plan. Poorly justified commitments, or commitments with limited additional value or credibility, will incur a penalty.

9.49 We expect each commitment in each business plan to be associated with the delivery of at least one of the following three overarching RIIO-3 outcomes:

- Infrastructure fit for a low-cost transition to net zero;
- Secure and resilient supplies; and
- High quality of service from regulated firms.[23]

9.50 Each new commitment should be clearly mapped to at least one of these three outcomes, although it could be mapped to multiple outcomes. Companies should provide evidence that their commitments lead to the delivery of the RIIO-3 outcome(s) that they are intended to deliver, in a credible and additional way.

9.51 For each of the three outcomes listed in 9.49 we will carry out a qualitative, in-the-round assessment of commitments based on the high-level balanced scorecard in Annex 6.  While this balanced scorecard will be used across all sectors, the level of ambition and the type of evidence we expect to justify

[23] The fourth overarching RIIO-3 outcome ("System efficiency and long-term value for money") is excluded from the above list as we expect it to be delivered through overall efficiencies rather than specific individual commitments.

credibility and additionality of commitments will vary by sector. We will therefore apply the high-level scorecard in the context of the sector-specific guidance included throughout the Business Plan Guidance.

9.52 Commitments under each of the three outcomes will be rated either outstanding, acceptable, or poor. An "outstanding" rating will be associated with a reward of +13 bps of RoRE multiplied by the weight for the relevant outcome. An "acceptable" rating will lead to no reward or penalty, while a "poor" rating will lead to a penalty of -13 bps of RoRE multiplied by the weight for the relevant outcome.

9.53 We will set the relative weights for each of the three outcomes based on our in-the-round view of their relative importance after having reviewed the business plans. As a result, the weighting may differ across sectors. However, the overall maximum reward or penalty for the Stage C assessment of business plan commitments will remain ±13 bps of RoRE, ie approximately two thirds of the overall Stage C maximum reward or penalty.