

Interested parties

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Decision on the operational arrangements for the RIIO-2 Strategic Innovation Fund (SIF) and the SIF Governance Document

RIIO-2 will prepare the regulated network companies to support the delivery of net zero greenhouse gas emissions in line with Government targets. Ofgem's approach will ensure that this is achieved at lowest cost to consumers, while maintaining world-class levels of system reliability and customer service and ensuring that no consumer is left behind in the transition to a low carbon energy system.

Innovation is a key part of meeting carbon reduction targets and achieving net zero ambitions. Accordingly, we made the decision in our RIIO-2 Final Determinations to introduce the SIF in the first tranche of RIIO-2 price controls for the Electricity System Operator (ESO), Electricity Transmission, Gas Transmission and Gas Distribution sectors.¹

The SIF supports network innovation that contributes to the achievement of net zero, while delivering real net benefits to network consumers. It facilitates collaboration with other public funders of innovation so that activities appropriately funded by network consumers are coordinated with activities funded by Government, and funding gaps are avoided.

We have made the decision to modify licences held by network companies and the ESO to introduce SIF licence conditions.² Additionally, we have confirmed our Innovation Challenges for round one of the SIF, subject to the direction of the SIF Governance Document, to provide licensees with extra time to develop the first set of SIF projects.³

¹ RIIO-2 Final Determinations – Core Document, pages 99-105:

https://www.ofgem.gov.uk/system/files/docs/2021/02/final_determinations_-_core_document_revised.pdf

² <https://www.ofgem.gov.uk/publications/decision-proposed-licence-condition-modifications-riio-2-strategic-innovation-fund>

³ <https://www.ofgem.gov.uk/publications/strategic-innovation-fund-innovation-challenges>

Following on from our consultation of 2 June,⁴ we are now deciding on the operational arrangements for the SIF and directing the SIF Governance Document.

Annex 1 to this letter considers key themes in the responses to our consultation questions and contains our decisions on the SIF operational arrangements. Alongside this document, we have published:

- the issues log considering both substantive policy issues and specific drafting points raised by respondents in relation to the SIF Governance Document.
- a track change copy of the SIF Governance Document, marking changes we have made since our consultation.
- a clean copy of the SIF Governance Document.
- our direction to issue the SIF Governance Document.⁵

Next steps on round one of the SIF

The table below provides details on the planned timeline for the operation of round 1 of the SIF over coming months. In line with our decisions contained in annex 1, UK Research & Innovation (UKRI) will support this as our delivery partner for the SIF.

Milestone	Date
Notification of licence modification (thereafter 56-day standstill period before licence comes into effect)	8 July 2021
Confirmation of SIF round 1 Innovation Challenges	23 July 2021
Direction of RIIO-2 SIF Governance Document	25 August 2021
Opening of UKRI application portal	31 August 2021
UKRI briefing webinars	7-8 September 2021
Deadline for receipt of SIF round one bids	17 November 2021
Assessment of bids	Late 2021 – Early 2022
SIF funding decisions	Early 2022
SIF Project Directions	Early 2022
First SIF Funding Direction	Early 2022
SIF project delivery – discovery phase	March – May 2022

Additionally, in coming weeks, UKRI plan to host two briefings events:

1. A general Strategic Innovation Fund launch event between 10:30–12:00 on 7 September 2021 for all organisations wanting to participate in the SIF.⁶ This event will introduce the SIF, focusing on the Innovation Challenges, the eligibility criteria, the application process, and how interested parties can get involved.
2. A Strategic Innovation Fund networks briefing event between 10:30–12:00 on 8 September 2021 for the energy networks that are eligible to apply to the SIF this

⁴ <https://www.ofgem.gov.uk/publications/consultation-sif-governance-document>

⁵ All of these document are accessible here: <https://www.ofgem.gov.uk/publications/sif-governance-document>

⁶ Participants can register for the event here: <https://eur.cvent.me/xvqBR>

year.⁷ It will focus on the eligibility criteria, the application process and the support available through UKRI and others.

Learning from round one of the SIF to inform future SIF operation

As stated in our June consultation, we will continue to reflect on the experience gained this year from round one of bids for SIF funding. Following this round of funding, we will consider any necessary changes to the operation of the SIF and the SIF governance arrangements that are consistent with a strategic fund that can address challenges on the path to net zero and that has the ability, where appropriate, to align with other public funders' programmes. We may also consider how best to maximise third party involvement in the SIF within any applicable regulatory constraints. Furthermore, but without fettering our discretion in relation to future policy initiatives or creating any expectations as regards such initiatives, we may consider reviewing the arrangements for the RIIO-2 Network Innovation Allowance (NIA) and strategic alignment as between the SIF and the final RIIO-ED1 Network Innovation Competition in 2022.

If such changes prove to be desirable, we will engage with stakeholders and consult on them, as necessary.

Yours sincerely,

Steven McMahon

Deputy Director, Electricity Distribution & Cross Sector Policy, Networks

For and behalf of the Authority

⁷ Participants can register for event here: <https://www.eventbrite.co.uk/e/sif-innovation-challenge-briefing-for-applicants-tickets-163971279511>. The password for registration is 'OfgemIUKSIF2021'

Annex 1 – consideration of responses to consultation questions

1. There were 11 written responses to our consultation on the operational arrangements for the SIF and the SIF Governance Document. These came from network companies and the ESO. Overall, these responses were generally supportive of our aims on the SIF, although they had various comments on substantive policy issues and the detailed operation of the SIF as set out within SIF Governance Document. We received no responses from third party innovators which were critical of our proposals.
2. This annex sets out our consideration of these responses to our consultation questions, our decisions on the SIF operational arrangements and the rationale for them. It sets out the overarching substantial concerns raised by stakeholders and our responses. The issues log published alongside this document considers both substantive policy issues and specific drafting points raised by respondents in relation to the draft SIF Governance Document.⁸

Arrangements for appointing and remunerating the third party delivery partner

3. We proposed to appoint UKRI as the SIF delivery partner and remunerate UKRI via network charges. We also detailed the function of UKRI as our SIF delivery partner.

Summary of responses

4. Most of the responses agreed to our proposal to appoint UKRI because that would help to align SIF funding with other UKRI funds. There was also wide recognition that UKRI is well placed to fulfil the role detailed in our proposals because UKRI has good experience in managing innovation funding and has robust systems to run the application and assessment process. Some of these responses also based their support on their belief that UKRI has sufficient technical expertise and will provide value for money to consumers.
5. However, there were two responses that did not expressly agree with our proposals and expressed reservations on the cost of UKRI's appointment and value for money for consumers, in the absence of either detailed benchmarking or a competitive tendering process. There was also disagreement amongst respondents to the consultation about

⁸ The issues log can be found here: <https://www.ofgem.gov.uk/publications/sif-governance-document>

whether we could justify the UKRI costs if they were at the higher end of our estimated cost range.

Decision

6. We will appoint UKRI as our delivery partner for the SIF and remunerate UKRI via network charges. The functions of the role will be as specified in our consultation document. In summary, the role will involve:
 - a. Administering the funding programme
 - b. Monitoring the delivery of SIF projects and acting as secretariat for Expert Assessors
 - c. Make recommendations to Ofgem on the operation of the SIF, such as the timeline for setting Innovation Challenges
 - d. Provide support to licensees to develop project proposals, develop partnerships with third parties and disseminate knowledge from innovation projects
 - e. Ensure benefits are delivered to consumers by establishing a route to market service.

Rationale

7. We think UKRI is a logical choice as it is a non-ministerial UK Government department with a statutory role delivering public innovation funds.⁹ In particular, we note that UKRI is itself the largest public funder of research and innovation in the UK. The appointment was supported by most respondents. UKRI's role in relation to the SIF will complement its existing role managing other public innovation funds and we think it will help to maximise the consumer benefits from SIF funding. We agree with feedback from respondents that the 'route to market' service will be particularly beneficial as it will help SIF projects to be rolled out and realise benefits for consumers.
8. Although there were some respondents who questioned the cost of appointing UKRI to run the SIF, we are satisfied that the arrangement with UKRI will represent value for money for energy consumers. Based on significant engagement with other public bodies who run innovation funds, we believe UKRI's forecast costs are comparable to that of other efficiently run bodies who could fulfil a similar role. The approved costs for UKRI will be subject to controls set out in a commercial contract between UKRI and Ofgem and will be transparent.

⁹ UKRI was established under Part 3 of the Higher Research and Education Act 2017

9. Recognising the need to scrutinise UKRI's actual costs, we will approve UKRI's costs on an annual basis which will enable us to ensure their approved costs are reasonable and represent value for money. The basis on which actual costs will be calculated has been set out in advance in the contract to ensure transparency.

Identifying innovation priorities and setting strategic Innovation Challenges

10. We proposed to set Innovation Challenges under the SIF as frequently as they arise and proposed a process to engage with stakeholders before confirming these. This proposed process included the use of a special network innovation subcommittee of the cross-Government Net Zero Innovation Board (NZIB) to gather insight from stakeholders across Government and the devolved administrations. It also included gathering views from the potential direct and indirect recipients of innovation funding (innovators, network companies and the ESO), from network licensees' regular innovation strategies and via wider surveys and engagement activities run by UKRI.

Summary of responses

11. Most respondents agreed with our proposal but stated that they would like to see more information on the pre-Innovation Challenge setting process and called for Innovation Challenges to be consistent with wider policy objectives. Stakeholders also welcomed our proposal to draw on licensees' joint Gas and Electricity Innovation Strategies and to engage with network companies to test our ideas once we had developed a proposal for an Innovation Challenge.
12. However, some respondents had reservations about whether the proposed process offered sufficient opportunities for all potential participants to feed in, and whether it created a level playing field. It was proposed that Ofgem should include a route for local authorities to participate in challenge-setting. Another respondent said that there was a risk that joint Gas and Electricity Innovation Strategies would not be given due attention, and that there should either be a pre-determined role for the Joint Gas and Electricity Innovation Strategies in informing the decision making of the NZIB sub-committee, or that the sub-committee should carry out stakeholder engagement directly. Finally, several network companies called for Ofgem to set Innovation Challenges at least once a year to prevent resourcing shortages in licensees' and project partners' teams.

Decision

13. We will adopt the process we proposed in the consultation whereby we will engage with stakeholders before and after setting Innovation Challenges, setting Challenges flexibly as the need arises.

Rationale

14. We recognise the desire for stakeholders to be involved in the setting of future Innovation Challenges. There are multiple forums and routes for stakeholders to engage with Innovation Challenge setting outside of the NZIB sub-committee, which we will use, and we welcome respondents' suggestions about appropriate forums. For example, where appropriate, we will also seek to engage with the Ofgem Net Zero Advisory Group (NZAG)¹⁰ and in innovation forums organised by the ENA. We will continue to develop the operational process and gather feedback on it to ensure that all stakeholders have an appropriate route to engage and provide input to the setting of Innovation Challenges. UKRI will soon mobilise stakeholder engagement ahead of Ofgem setting the next Innovation Challenge(s), which will enable us to gather the views of local government and take account of their interests in the process.
15. We disagree with responses that suggested that Ofgem would need to set Innovation Challenges at least annually, rather than flexibly as the need arises for network companies, to resource innovation adequately. We believe that setting challenges as the need arises will ensure the SIF can operate quickly, flexibly and support coordination with other public funders of innovation. We also believe that this flexible approach will allow a suitable response from licensees and the market because network licensees and the ESO will be able to work with third parties who could alleviate resource constraints within network companies.¹¹ Although the involvement of third parties will have to comply with the constraints of the eligibility criteria (consistent with subsidy control rules, the requirement for third party access to a network is a pre-condition of the funding of third party contributions to projects out of the SIF), we think there is scope for networks to put forward innovation ideas presented to them by third parties.

¹⁰ Further detail on NZAG can be found here: <https://www.ofgem.gov.uk/energy-policy-and-regulation/engagement/forums-and-working-groups/net-zero-advisory-group-nzag>

¹¹ We note to comply with subsidy control rules, third-party innovators can only access SIF funding when Projects involve access to network assets or data.

16. Additionally, there is a period of three months between issuing an Innovation Challenge and receiving applications, which will give enough foresight to resource the submission of an application to the SIF.

Three-phase approach for SIF projects

17. We proposed a three-phase approach when funding SIF projects, breaking down projects into feasibility studies within the discovery and alpha phases, and large-scale demonstration at beta phase. We proposed that the parameters of each phase in terms of length and monetary value would be confirmed when Innovation Challenges are issued.

Summary of responses

18. Most respondents were generally supportive of the intent behind the three-phase approach to support learning, testing of assumptions, and to mitigate risk for consumers.

19. However, network companies and the ESO were concerned about some aspects of the detailed design of the three-phase approach. Several respondents considered that the approach will introduce delays because of the gaps lasting between project phases to accommodate assessment, which could in turn impact on the speed in which networks can take forward activities which help achieve net zero carbon emissions. They stated that these gaps would introduce delivery risk, and that the stop-start nature of SIF would bring challenges from a contracting, resource and management perspective.

20. Some of the feedback supported our proposals regarding the illustrative project phase monetary values and time periods. However, a majority were critical, and some contended that the proposed illustrative parameters appeared to be more restrictive and complex than those of other UKRI projects, in which they had been involved. Another response questioned whether the illustrative monetary values and time periods for each project phase would be able to accommodate the scope of necessary innovation projects. The respondent suggested that illustrative maximum duration of phases seemed short while the maximum budgets seemed high. They suggested that these choices would mean projects would have to start out with a very high level of resource investment, then stopping during the process which respondents noted is often difficult to achieve in practice.

21. Additionally, several respondents called for the approach to be tested in practice and kept under review, with close engagement with stakeholders, including those implementing projects.

Decision

22. We will adopt the three-phase approach to funding projects that was set out in the consultation document. Requirements relating to the maximum monetary value and length of project phases will be defined in the Innovation Challenge documentation.

Rationale

23. We agree with responses suggesting that the approach needs to be flexible and disagree with responses that suggested that the approach proposed is rigid. The parameters stated in the consultation issued alongside the draft SIF Governance Document were indicative only and in our response to points raised in the issues log we confirm that, where appropriate, administrative and decision-making processes will remain agile. Remaining flexible will allow us to define, considering stakeholder views, appropriate lengths and monetary values for project phases when setting Innovation Challenges. Experience gained this year operating the SIF and engagement with stakeholders will inform any changes in the process for setting Innovation Challenges that prove necessary for the future.

24. We agree with those stakeholders who responded that funding projects in stages reduces the risks associated with large-scale innovation projects. We consider that the benefits of this approach also include the opportunity to shape projects as they move from one phase into another during application and assessment, which supports our aim, articulated in Final Determinations, to target innovation activities towards strategic priorities. We have decided to adopt the three-phase approach to realise these multiple benefits which we believe outweigh the potential negative effect of delays arising during assessment and decision periods between phases.

Projects eligible for SIF funding

25. We proposed that projects receiving SIF funding would have to satisfy the eligibility criteria set out in Chapter 2 of the SIF Governance Document, as well as any specific requirements set within the Innovation Challenge. As part of this, we proposed that the Innovation Challenge-specific requirements could include variations to the level of compulsory contribution required by parties bidding in for SIF funding.

Summary of responses

26. Most of the respondents were in favour of the use of the proposed eligibility criteria. However, as detailed in the issues log, there were some comments questioning whether some of the eligibility criteria themselves could constrain innovation (such as the requirement for projects not to undermine competitive markets). Other comments requested the elimination of any subjectivity inherent in the eligibility criteria to make it clear what is and is not eligible for funding.
27. There was a varied response on the parameters that should be included within the Innovation Challenge. Some responses suggested that the Innovation Challenges could specify the necessary technical focus and desired outcomes from the projects, such as the production of evidence to support policy decisions. Others suggested that Ofgem take a holistic and flexible view on Innovation Challenge parameters and that requiring specific project partners could be useful. However on the same point, several other network companies noted it is not possible at the application stage to provide certainty on the project partners who will be involved in the project because such collaborations are dependent on commercial agreements which are only executed after funding decisions are published.
28. One respondent was supportive of our proposal to be flexible with the compulsory contribution requirement. However, all other responses did not agree with a higher level of compulsory contribution towards projects. One suggested a fairer approach would be to revert to the initial NIC mechanism where the contribution would be returned upon meeting the project's success criteria. Others simply suggested they were not in favour of any increase in the compulsory contribution required and suggested variable contribution requirements could give rise to uncertainty that will discourage involvement in the SIF.

Decision

29. We confirm that projects must satisfy eligibility criteria as set out in Chapter 2 of the SIF Governance Document, as amended to address comments in the issues log, as well as any specific requirements set within the Innovation Challenge. We also confirm that various parameters, such as the involvement of specific project partners and the level of compulsory contribution required by parties will be confirmed in the Innovation Challenge.

30. In a change to our consultation position, our decision is that we may require a minimum level of compulsory contribution which is either more than or less than the 10% default compulsory contribution specified in the SIF Governance Document. Any variations to the level of compulsory contribution required will be considered on a case-by-case basis and take account of the risk and benefits associated with the Project.

Rationale

31. As detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document are necessary to clarify what is or is not eligible for funding.

32. We disagree with responses that the eligibility criterion that projects must not undermine competitive markets is not appropriate. The drafting emphasises that we will be proportionate in applying this criterion, but we do not think we should remove it altogether because innovation funding provided as part of a network price control must not enable monopolies such as network companies to undermine wider competitive markets. Additionally, we disagree we should significantly expand on the eligibility criteria and replicate the detail provided in the NIC Governance Document. As indicated in our Final Determinations, we have taken the NIC as our starting point but the SIF will operate in a different policy environment, to which the eligibility criteria, as amended, are in our view well suited. The eligibility criteria permit a degree of flexibility in our approach to project funding that is consistent with the scale of the challenge that lies ahead and the pace of change required to meet challenge, whilst providing applicants for SIF funding with sufficient information about what is or is not eligible.

33. We agree with feedback that the parameters of the Innovation Challenge should recognise the commercial reality of collaborations with project partners. However, we do not believe that this should prevent us from requiring that submitted projects have certain project partners involved, subject to the conclusion of commercial arrangements between them. We agree with other feedback that the Innovation Challenge should detail the technical focus of projects, the desired outcomes from the project and project partners.

34. Our intent is that the compulsory contribution is a minimum amount that the network company or project partners are required to make towards a project to share the risk and benefit associated with that project. We disagree with those responses from network companies that suggested that all SIF projects should have a standard compulsory contribution and that this should not be changed for any project because

this would not account for the fact that the risk and benefit associated with different projects may vary. However, on this basis, considering feedback and in a change from our consultation position, we think that we should have flexibility to specify a lower level of compulsory contribution for projects that may not financially benefit network companies or project partners, or for those projects that may not be particularly risky.

35. We continue to believe in some circumstances it may be appropriate to require higher levels of compulsory contribution for projects. In support of this, we note that the SIF and other RIIO price control innovation funds are a rare example of public innovation funds providing 90% of project funding - requiring a higher contribution upfront from recipients of funding is common practice for other public funders of innovation funds. For example, the Prospering from the Energy Revolution fund administered by UKRI effectively funds 33% of projects (once requirements for matched funding are accounted for).¹²
36. As an overarching point, we disagree with responses which argued that network companies should not contribute more up front because network companies share the benefits after projects have completed. We disagree because the upfront compulsory contribution share the risk before a project begins and the post-project totex incentive mechanism shares the reward after a project is rolled out – neither of them require companies to take all the risk or share all the benefit. Sharing a percentage of risk and benefits with consumers who ultimately fund project before and after projects is fairer.
37. We would seek to require a higher compulsory contribution in two instances. This is where projects have the potential to deliver significant financial benefits to the network companies or project partners, or where projects entail a significant element of non-network activities and benefits. Here we will look to share the costs and benefits of projects between network consumers, shareholders of network companies and other private third parties who stand to benefit from the innovation project.
38. In a change from our consultation position and in response to feedback, we no longer seek to have an additional provision to vary compulsory contribution requirements to solely align with other sources of public funding. Although our policy intent is to coordinate with other public funders, we agree with responses that any variations to compulsory contribution are most appropriately considered according to the risk and benefit associated with the project. For instance, if activities are funded by both Ofgem and BEIS, whether a higher compulsory contribution is required for projects funded by

¹² More detail of the Prospering for the Energy Revolution fund can be found here: <https://www.gov.uk/government/news/prospering-from-the-energy-revolution-full-programme-details>

Ofgem should depend on the risk and benefit associated with the Ofgem funded project. The determination of risk associated with an Ofgem project may, however, be informed by the fact that other public bodies are funding related projects.

Encouraging collaboration and sharing learning

39. We proposed requirements to encourage collaboration and learning in Chapter 3 of the SIF Governance Document, which build upon the requirements in the RIIO-1 NIC Governance Document and the RIIO-2 NIA Governance Document.

Summary of responses

40. Most responses agreed with our proposals to encourage collaboration and share learning. One response partly supported our proposals but requested the redaction of sensitive data before information was externally shared.

41. There were other comments, captured in the issues log, that the proposed requirements have practical implications for licensees to manage and that activities need to be cost recoverable. Other comments queried the requirement to maintain the ENA Smarter Networks Portal when it is unclear how such costs can be recovered via the SIF.

42. In response to our question on improvements that could be made to improve knowledge dissemination, one response suggested that the existing use of Smarter Networks Portal and annual innovation conference was satisfactory because they had evolved through feedback over the years. Various other suggestions were provided to improve knowledge dissemination, which included:

- A mix of virtual and physical hosting of the event in future years
- Actioning of feedback from participants or attendees at the innovation conference
- Continual development of the Smarter Networks Portal as a single point of reference for network innovation.

Decision

43. We confirm the requirements we proposed in Chapter 3 of the SIF Governance Document, which build upon the requirements in the RIIO-1 NIC Governance Document and the RIIO-2 NIA Governance Document.

Rationale

44. We have confirmed our proposals because there is agreement amongst most respondents with the requirements to collaborate and share learning. However, as detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document are necessary to clarify requirements (such as the ability to redact information before it is shared and the ability for licensees to recover the cost of using the ENA Smarter Networks Portal for SIF projects).
45. We have also retained the requirement to run an annual conference to disseminate learning from SIF projects. However, we agree with feedback that, now that we have moved from the NIC to the SIF, the conference could be improved to help maximise its benefits and support our objectives of coordinating with other public innovation funds and increasing third party involvement in innovation projects. Therefore, we are tasking UKRI to support energy networks in organising future innovation conferences.

Project application

46. We proposed that, when applying to the SIF, applicants would be asked to explain and demonstrate how projects meet the eligibility criteria set out in Chapter 2 of the SIF Governance Document by answering a set of standard questions. The application questions that we proposed that applicants answer are set out in Chapter 4 of the SIF Governance Document.

Summary of responses

47. There was general agreement among respondents with our proposals. In addition to the various comments detailed in the issues log, one response expressed a concern regarding certain constraints on applications (ie a 400 word limit, use of eight questions and the need for seven separate supporting documents). This response suggested that such applications will require significant effort and may limit the number of applications that companies submit. Another response suggested that there should be more realistic expectations regarding the number of applications that will be made through the scheme, recognising the resourcing constraints faced by networks.

Decision

48. We confirm our decision to implement the project application process as outlined in the draft SIF Governance Document, with minor adjustments to drafting aimed at addressing respondents' comments, as outlined in the issues log.

Rationale

49. General agreement amongst respondents confirms our view that the process that we proposed works well. However, as detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document are necessary to clarify requirements (relating, for example to the content of the applications for various phases).
50. We have opted to retain word limits for applications because we believe this will help to limit the burden for applicants, lower the barriers for entry and make project assessment easier. However, we note that supporting documentation and annexes can be used flexibly. We believe that will enable licensees to express their ideas clearly. We recognise that the process for applying for funding does inevitably require resource. Although we are encouraging companies to submit applications in response to our Innovation Challenges, there is no requirement for them to do so.

Project assessment and funding decision

51. We proposed a process to assess projects and issue a funding decision as set out in chapter 5 of the draft SIF Governance Document. The proposals implement the decisions taken in our RII0-2 Final Determinations to use experts to assess projects and issue a recommendation to Ofgem as decision-maker in relation to whether to fund projects.

Summary of responses

52. There was general agreement among the responses with our proposals. Some responses did, however, comment that they thought that there should be a faster assessment and decision-making process for SIF projects, and stricter parameters around the supplementary question process to help licensees manage resource. One of the responses did not expressly agree or disagree with our proposals but sought further detail on how Expert Assessors would be appointed.

Decision

53. We confirm our decision to implement the process for assessing and deciding on funding for SIF projects, as described in the draft SIF Governance Document, with minor drafting adjustments aimed at addressing respondents' comments as outlined in the issues log.

Rationale

54. General agreement amongst respondents confirms our belief that the process that we proposed works well. However, as detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document are necessary to clarify requirements (such as the intended frequency of supplementary questions).
55. In response to feedback that assessment and decision-making on projects should be faster than the 12 weeks specified in the draft SIF Governance Document, we note that drafting indicates decisions will take 'up to 12 weeks'. We believe it is appropriate to adopt this flexible approach because the time needed to assess projects and reach a funding decision will vary from project to project. However, our intent is to work with UKRI to maximise the efficiency of the process for issuing Ofgem's decisions.
56. UKRI's function includes acting as a secretariat for the Expert Assessors – we will work with UKRI over coming months to appoint appropriate Expert Assessors capable of making funding recommendations to Ofgem. Our intent is to publish the recommendations from Expert Assessors to ensure the transparency of their assessment of projects.

Project delivery

57. We proposed reporting requirements for project delivery and monitoring projects, as set out in Chapter 6 of the draft Governance Document.

Summary of responses

58. All respondents agreed with our proposals. As detailed in the issues log, there were several suggestions made on where further information and clarification could be added to the SIF Governance Document.

Decision

59. We confirm our decision to implement reporting requirements and monitoring arrangements as outlined in the draft SIF Governance Document.

Rationale

60. Respondents were supportive of our proposals and agreed that they allow potential concerns with ongoing projects and their progress to be addressed in a timely manner, which reduces risk to customers and project partners. As detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document were necessary to clarify requirements.

Funding arrangements for SIF projects

61. We proposed arrangements for funding SIF projects in chapter 7 of the draft SIF Governance Document. Our proposals for the arrangements to fund SIF projects largely mirrored those adopted for the NIC in the RIIO-1 NIC Governance Document. Ofgem would only direct National Grid Gas Transmission and the ESO to distribute SIF funds once a year and all payments would be made in 12 equal instalments over the course of the Regulatory Year.

62. Additionally, our default proposal, consistent with our RIIO-2 Final Determinations is that approved projects will be funded via use of system charges collected by the ESO and NGGT. However, we proposed that we would consider on a case by case basis and consult on alternative arrangements for funding high-value projects which have a significant short-term impact on network charges.

Summary of responses

63. Some respondents agreed to our proposed default funding arrangements for SIF projects and noted that the funding arrangements for the NIC in RIIO-1 worked well. However, some responses noted that the proposed distribution of SIF funds did not align with the policy intent for the SIF to be flexible and suggested that it did not work well for discovery and alpha phase projects which are likely to be shorter than 12 months. Additionally, several respondents requested further detail on the practical operation of SIF funding in RIIO-2 and queried whether we sought to allow NGGT and the ESO to set and raise their own forecast costs for the SIF ahead of the start of the Regulatory Year. In addition to written consultation feedback, we have also discussed the SIF funding arrangements with NGGT and the ESO to develop our understanding of the practical implications for them of raising and distributing SIF funds in RIIO-2.

64. One response suggested that, rather than all electricity SIF funding coming from TNUoS, it may be more appropriate to share SIF funding between TNUoS and BSUoS, depending on the expected outcomes from the project.

65. In response to our proposal to consider alternative funding arrangements for high-value SIF projects, most respondents highlighted the need for further work in this area. There was a suggestion that work on this could be done ahead of the identification of specific projects to ensure that any alternative arrangements, if they are needed, can quickly be mobilised.

Decision

66. We have confirmed arrangements for funding SIF projects and UKRI as detailed in chapter 7 of the SIF Governance Document, subject to the following amendments to our consultation position:

- a. Clarification that NGGT and the ESO can raise forecast costs for the SIF ahead of each Regulatory Year.
- b. Addition of the ability for Ofgem to issue SIF Funding Directions more than once within a Regulatory Year.
- c. Addition of the ability for Ofgem to direct that SIF funds are distributed in one lump sum or in multiple payments over the course of the Regulatory Year.

Rationale

67. Our amendments to the draft SIF Governance Document respond to feedback from respondents that clarification was needed as to whether National Grid Gas Transmission and the ESO can raise forecast costs for the SIF ahead of each Regulatory Year. This will mean that SIF funds can be distributed in a more flexible and responsive manner during the Regulatory Year, consistent with the SIF's policy intent.

68. Additionally, amendments to provide Ofgem with the flexibility to direct the distribution of SIF funds more than once a year, and either as lump sums or in multiple payments aligns consultation feedback and our policy intent for the SIF to be a flexible funding mechanism. The frequency at which payments will be made will be confirmed within individual SIF Funding Directions, but, for example, these changes could enable Ofgem to direct that SIF funding for discovery phase and alpha phase projects be distributed in one lump sum, which would enable funds to be distributed quicker and reduce the related administrative burden for NGGT and the ESO when distributing funds and for those receiving funds.

69. However, we disagree with suggestions that electricity SIF funding should be split between TNUoS and BSUoS charges. We want the default approach for funding SIF

projects to be simple and think that splitting costs between TNUoS and BSUoS would add complexity and make it harder for stakeholders to follow the flow of SIF funds. We believe it is desirable to retain the default arrangements for all electricity SIF funding to come from one source and, consistent with the approach adopted in the RIIO-1 NIC, we believe that TNUoS should be the default source of electricity SIF funding.

70. We agree with respondents that further work is needed to identify the circumstances in which we may seek to deviate from the default SIF funding arrangements to fund some high-value projects and we have not confirmed these arrangements within the SIF Governance Document. Although some initial work can be done to scope options here, we continue to believe that it will not be possible to confirm the most appropriate route for funding such high-value projects before the specific projects are identified and therefore this will need to be considered on a case-by-case basis to ensure that the most appropriate funding arrangements are identified.

Project administration

71. We proposed requirements for project administration as set out in chapter 8 of the draft SIF Governance Document, which replicate the requirements of the RIIO-1 NIC Governance Document.

Summary of responses

72. The limited number of responses to the question agreed with our proposal. Respondents cited positive experiences with how the NIC was administered and supported replicating these arrangements, noting they were tried and tested.

Decision

73. We confirm our decision to introduce the requirements previously proposed, with minor drafting adjustments aimed at addressing respondents' comments, as outlined in the issues log.

Rationale

74. We agree with respondents' views that the arrangements in RIIO-1 worked well and have decided to build on these successful arrangements. As detailed in our responses to comments in the issues log, we agree that some drafting changes within the SIF Governance Document were necessary to clarify requirements.

Intellectual property rights and royalties

75. We proposed default arrangements for dealing with intellectual property rights (IPR) and royalties as set out in chapter 9 of the draft SIF Governance Document. These requirements replicate the requirements in the RIIO-1 NIC Governance Document.

Summary of responses

76. There was a mixed response to this question. Some responses agreed with the proposed default rules for IPR and royalties, noting their use in RIIO-1. There was a consensus among responses that pre-existing IPR arrangements should be used for the SIF. However, some responses noted that the default IPR requirements differ from those adopted for the NIA and proposed that default arrangements replicate those of the NIA to allow network companies to own foreground IP generated within projects. They suggested it would create additional complexity having different funding streams with their own IPR requirements, and instead suggested it would be beneficial if default IPR were aligned across SIF and NIA.

Decision

77. The default intellectual property rights arrangements for SIF projects will be consistent with those arrangements used for the RIIO-1 NIC.

Rationale

78. We believe the default intellectual property arrangements for the RIIO-1 NIC are appropriate for the SIF because they enable consumers to share the benefits of SIF projects.

79. We disagree with suggestions that the SIF intellectual property arrangements should replicate the arrangements we have in place for the NIA. Although NIA IPR arrangements allow networks to own all foreground IP within NIA projects, we do not believe the default SIF IPR arrangements should allow networks to own all foreground IP within SIF projects. In contrast to the NIA, SIF projects are individually assessed and approved by Ofgem and networks' proposals to own all foreground IP can be considered on a case by case basis, when applicants apply for funding. We also note that very few, if any, bids to the NIC in RIIO-1 sought to deviate from the default IPR arrangements, which suggests the arrangements are appropriate. However, if we become aware of problems with the IPR arrangements in future years (for example, if they prevent the

commercialisation and rollout of innovation within business as usual activities), then we can revisit the arrangements in the SIF Governance Document, if necessary.