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30/06/2021

Consultation on RIIO-2 Strategic Innovation Fund Governance Document and operation

Dear Graeme,

Thank you for the opportunity to respond to Ofgem's RIIO-2 Strategic Innovation Fund – informal consultation on the Governance Document and the operation of the SIF. This response is given on behalf of National Grid Electricity System Operator (NGESO).

Please find our responses to each specific question raised in the consultation document, in the Appendix attached.

We welcome the opportunity to further discuss the points raised within this response. Should you require further information or clarity on any of the points outlined in this paper then please contact me.

Yours sincerely,

Carolina Tortora

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APPENDIX.

Question 1: Do you agree that our proposals to appoint and remunerate UKRI as our delivery partner provide value for money to energy consumers? If not, please explain why.

- UKRI are a clear choice to manage the SIF funding, with their broad experience of running innovation funding competitions.
- We find it difficult to justify the higher end of the estimated cost range of £11.25m to consumers (if UKRI is remunerated as a percentage of total SIF funding being allocated).
- We have found the level of effort required to run an innovation function isn't correlated directly with the size of the funding available, or project costs each year, but is dependent on the number of proposals / projects the function must manage at any given time, and the level of stakeholder engagement required (i.e. more collaborative projects require more effort). Proposals and projects usually require a similar effort to review, track, and disseminate, regardless of the size of a project budget.
- UKRI's renumeration may be more sensibly calculated as a fixed cost (e.g. based on the resources required to manage the forecasted number of proposals each year, or on the value they bring to the process), then adjusted based on the increasing capacity needed to track ongoing projects, and manage related stakeholder engagement activities as the SIF process becomes more established.
- UKRI must ensure the specific aspects of the regulatory environment and requirements on networks are reflected in the delivery of the SIF innovation process. Many of the innovation projects will require involvement of the ESO and networks to ensure they can be successfully implemented, so the UKRI will need to help foster close cooperation between licensees and third parties to develop successful proposals.
- UKRI must ensure the SIF improves upon the shortfalls of the previous NIC funding, responding to feedback to improve the process (where possible) throughout the RIIO-2 period. What must be avoided is to have the same issues that NIC came with (complex application process, excessive documentation needed, difficult application procedure, time consuming etc) and worsening them with SIF inconveniences (short notice to submit applications, hard and fast deadlines which do not take into account business deliverables, and timelines etc).

Question 2: Do you have views on the means by which we can gather stakeholders' insight into strategic innovation priorities before developing a challenge?

- Specific involvement of trade bodies and consumer groups would help reflect the requirements of both in establishing how best to focus funding.
- There should be sufficient opportunities for all potential participants, by creating an equitable playing field. Forums where similar business sizes/types can provide feedback collectively (instead of individually), would help smaller innovators have their views heard. The innovation landscape in energy at the moment is dominated by larger, more established parties who arguably don't need as much support as the newer, potentially more disruptive innovators. These forums could help build the consortiums needed for subsequent, large-scale SIF projects, by aligning the parties which aim to solve similar challenges, or who offer complementary solutions to challenges.

Question 3: Do you consider our proposed three-phase approach suitable to support large-scale strategic network innovation projects, while encouraging learning and mitigating risk? If not, please set out your reasons why.

- While we believe phasing SIF projects will help make sure funding is being used effectively, with clear decision points allowing projects to be reassessed under clear criteria before they move to the next phase (with higher funding commitment), we are concerned that it puts extra hurdle and urgency on business to adapt to the hard schedule.

- A phased approach to innovation projects will allow for greater transparency of approval/rejection processes, ensuring new SIF proposals can build upon these learnings, reflecting the latest research and developments. However it also limits the type of projects into falling into vey specific pattern of development, which may reduce the scope of projects that could participate in SIF.
- Feedback and dissemination is one area that is particularly important throughout the process, especially where multiple projects are exploring different aspects or options for a challenge area. A continually updated strategic direction or narrative by Ofgem or UKRI on these challenges will give networks and industry visibility of when a Research or Alpha project is likely to proceed or fail due to another idea bringing greater benefits to consumers.

Question 4: Do you consider that the indicative value and length of the different Project Phases will accommodate a wide range of network innovation projects to support net zero?

- It is difficult to understand why these phases must have set timeframes to deliver, as imposing conditions like these seems to only introduce restrictions on what projects are eligible, with little apparent upside to encouraging more diverse innovation proposals.
- Although this approach may make it easier to plan resources for reviewing SIF proposals, it will also mean that potentially large numbers of proposals must all be reviewed at the same time, creating significant peaks in workload for UKRI and assessors.
- A more Agile approach would be to have multiple points throughout the year (e.g. every 3 months) where applicants can submit proposals, regardless of type (Discovery, Alpha or Beta), ideally this would smooth out the number of proposals to review at a given time and give innovators flexibility on length of phases, and to progress their projects with less delays (rather than waiting 12 months for the next opportunity, which was a criticism of NIC).
- We believe there should as little limitation on the length of projects as possible. It is unnecessarily restrictive to impose these conditions on innovation projects. Innovation is inherently unpredictable, with unknown variables and higher risks of delay. This will only restrict the range of innovation projects able to participate in SIF.
- The current proposed timelines also leave very little time between completing one phase and applying for the next phase. This assumes outcomes are delivered sufficiently early in each phase, to leave enough time to decide amongst the consortium whether to apply for the next phase, and conclude all necessary negotiations, reviews and approvals before the deadline (which is less likely on larger, more collaborative projects). The parties in consortiums will each have separate legal and technical review processes to complete, which will likely be substantial on >£5M SIF projects.

Question 5: Do you agree with our proposed Eligibility Criteria? If not, please explain why.

- We agree that the proposed eligibility criteria are necessary to ensure appropriate proposals are taken forward which can deliver consumer benefits.
- As mentioned already, there should be minimal conditions on the types of projects allowed, to ensure a wider, more diverse range of innovation can be taken forward. The conditions that do remain should only be there to ensure that funding cannot be used inappropriately, with an understanding that innovation is inherently risky and projects may fail to deliver all their intended benefits.
- Where projects do fail, research often does not and therefore where projects are rejected we would ask Ofgem to detail that rejection and therefore revised project ideas aren't excluded in future funding rounds.

Question 6: Do you have views on which parameters Ofgem should consider defining when setting Innovation Challenges? In particular, the types of organisation that need to participate in a consortium as project partners?

- We believe it would be sensible for consortiums to include parties which will be best suited for the type and intended deliverables of the project. We don't believe it will be necessary to enforce this, as it would become a matter of deciding how a particular party is classified, instead this could be

weighed up in the approval process (i.e. UKRI would assess the merits of consortium members based upon the aims of a project).

- It seems overly restrictive to define the types of organisations that need to participate in a consortium, as this would only narrow the potential solutions put forward, or force certain parties into a consortium where there may not be value in this.
- The only area where we see this as being a necessity, is where projects will require the ESO or a network to implement the solutions to deliver benefits. It makes sense for the relevant network to be involved in assessing the proposal for viability, and then be a part in the project, to ensure any solution is fit for purpose and has a clearly understood route to implementation.
- We do have concerns on the likely number of projects that require the input from the ESO. Consideration should be made for when projects overlap with existing business as usual activities such as the RIIO2 Business Plan.

Question 7: Do you have views on the circumstances in which Ofgem may require a higher level of compulsory contribution towards projects?

- It is reasonable to allow for flexibility in the amount of compulsory contribution on SIF projects.
- This could be based on the expected financial benefit to the parties involved, and should be assessed on a case-by-case basis, rather than by challenge area (unless a challenge is specifically targeted to the roll-out of commercially available technology, or where parties will take lower risk and develop commercial IP which they retain rights to).

Question 8: Do you agree with our proposed requirements to encourage collaboration and share learning? If not, please explain why.

- The ESO supports these requirements to improve collaboration and share learnings from SIF innovation activities.
- It is important that applicants are aware of what data they need up front, and how they can access this. Then consult with the relevant networks and ESO beforehand, to ensure this data can be provided, or the steps (and timeframe) necessary to facilitate this under the SIF project. Some data may include sensitive or commercial IP, which will restrict usage outside of the organisation (regardless of whether this is for an innovation project).
- As many of the SIF proposals will require involvement from the ESO or other networks, they should have the right to accept or decline involvement, based on what they assess to be the viability of the project and their capacity to contribute at the required level. It is unclear whether this position would then need to be justified, and to what level of detail, as this review process would add significant resource requirements on the ESO and the networks.
- It is unclear how this collaboration would extend to other sectors outside of the energy networks, e.g. would transport networks be able to participate in SIF projects alongside the ESO? This type of whole energy innovation (outside of only the energy networks) was previously difficult with NIC, as other sectors had their own innovation funding and were therefore unable to participate in energy-system specific innovation projects. There needs to be a view to enabling innovation across all sectors, and making innovation funding open and complementary to other funding sources available.
- We would ask that terminology in the SIF governance document around project partners, innovators, funding party, licensee is consistent across the document.

Question 9: Do you have views on whether and, if so, how the ENA Smarter Networks Portal and annual innovation conference could be improved better to achieve its aims of effectively disseminating learning and enabling partnerships between licensees and third parties?

- The annual innovation conference is constantly improving. It is important that it keeps adapting to best practice, and any feedback from participants or attendees is actioned. A mix of virtual and physical hosting of the event may be the optimal solution in future, to reflect the needs of a wider audience who may not be able to attend but wish to benefit from these dissemination events.

- More opportunities on the Smarter Networks Portal, and at the innovation conference, for workshops and forums to discuss challenges and potential solutions, would help foster collaboration and identify partnerships, and new project ideas.

Question 10: Do you agree with our proposals on requirements for project applications? If not, please explain why.

- Aside from the points already raised in this response to the proposed SIF governance, the ESO agrees with the requirements for project applications.
- The "quantified benefits case" would need to take into consideration the uncertainty in calculating outcomes of any innovation, and how this would translate to indirect benefits for the system and end consumers. In particular, the ESO undertakes a lot of innovation where benefits are difficult to quantify, due to the nature of the ESO's activities e.g. providing insights, market signals, code changes and balancing actions which lack a counterfactual to calculate the size of resulting improvements, despite the benefits being clear. We hope that the guidance won't be overly prescriptive and deter innovators from participating in SIF, where expected benefits are still clear enough to justify funding, but difficult to quantify at a high level of certainty.

Question 11: Do you agree with our proposals for the assessment process? If not, please explain why.

- Yes, the ESO agrees with the proposed assessment process.
- The process should allow for the most feedback to innovators as reasonable (and a chance for them to respond) prior to a final funding decision. This could be facilitated through workshops or webinars with potential applicants, to define the award criteria for challenges in greater detail and answer questions to help innovators develop their proposals ahead of submission (saving time for everyone involved by reducing the number of unsuitable applications).
- The feedback on unsuccessful applications should be made public (where appropriate) and these learnings used to help form guidance for future SIF applicantions.

Question 12: Do you agree with our proposals on requirements for reporting, and our proposals to monitor projects? If not, please explain why.

- We agree with these proposals.
- In particular we support the appointment of a monitoring officer to provide a single point of contact between SIF project teams and UKRI.

Question 13: Do you agree with our proposed funding arrangements for SIF projects? If not, please explain why and suggest whether there are alternative funding arrangements that may be preferable.

- We agree with the proposed funding arrangements for the SIF should be recovered through 'use of system' charges. However it may be more appropriate to share the SIF funding between TNUoS and BSUoS depending on the expected outcomes from the project and how these expect to provide benefits, only the former is currently mentioned in the governance e.g. will benefits from a SIF project affect the transmission network directly, through better or cheaper assets, or will it reduce costs to balance the system? It would be more appropriate to fund SIF projects from the 'use of system' charges which it will ultimately benefit (i.e. through a reduction in these specific costs).

Question 14: Do you agree with our proposed requirements regarding project administration for SIF projects? If not, please explain why.

- We agree with these proposed requirements.

Question 15: Do you agree with our proposed default rules for intellectual property rights and royalties for SIF projects? If not, please explain why.

- We agree with the proposed default rules for IPR and royalties for SIF projects. We support flexibility in how IPR is allocated between parties, as long as the licensees rights to share the project outcomes, or learnings, remains protected and unrestricted by other parties who share the IPR (while keeping any sensitive or background commercial IP also protected).
- The IPR arrangements for each SIF project will need to be negotiated for each new consortium and may cause the most substantial delay to contracts being agreed. With this in mind, the default treatment for IPR should be as clearly defined as possible, while ensuring it is pragmatic and flexible enough to align with the existing regulatory and commercial interests of the parties involved in a SIF project. This will ensure innovators aren't dissuaded from participating in SIF projects.
- The allocation of royalties based on initial contribution of the parties, should ensure they benefit from any commercial IP developed, by sharing any revenues with consumers in the proportion which reflects the risk they assume to undertake the project.