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Date: 15 December 2021

Dear Stakeholders,

## **Decision on the Electricity System Operator Business Plan: IT Investment Plan Guidance**

This letter sets out the Authority's<sup>1</sup> decision to modify the Electricity System Operator Business Plan: IT Investment Plan Guidance (the "IT Investment Plan Guidance").

It explains our proposals and the changes we have made in response to the views stakeholders shared with us through our recent consultation.<sup>2</sup> The IT Investment Plan Guidance will take effect from 15 December 2021. For the avoidance of doubt, this means that the information submitted regarding IT investments as part of the Electricity System Operator's (ESO) Business Plan for the 1 April 2023 – 31 March 2025 period (BP2) should comply with the IT Investment Plan Guidance.

### **Background**

In November 2021, we published the ESO Business Plan Guidance,<sup>3</sup> which built on previous guidance set out for electricity and gas network companies on the information that should

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<sup>1</sup> The "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Office of Gas and Electricity Markets (Ofgem) supports the Authority in its day to day work.

<sup>2</sup> Consultation on IT Guidance for ESO Business Plan Guidance:

<https://www.ofgem.gov.uk/publications/consultation-it-guidance-eso-business-plan-guidance>

<sup>3</sup> ESO Business Plan Guidance: <https://www.ofgem.gov.uk/publications/eso-business-plan-guidance>

be included in companies' RIIO-2 business plans.<sup>4</sup> The ESO Business Plan Guidance provides the ESO with specific guidance on our expectations for the second Business Plan of RIIO-2, covering the BP2 period. In the ESO Business Plan Guidance, we stated we would provide further detailed guidance on the information we require from the ESO to assess its IT investments and that we would do this in 2021, before the ESO submits its draft Business Plan for BP2 in April 2022.

The IT Investment Plan Guidance provides that additional guidance for the ESO on its BP2 IT investments. It sets out the additional governance and the process by which the ESO must submit information to the Authority relating to its IT investments as part of its second Business Plan. It also sets out the governance and process by which the Authority and the ESO Performance Panel will assess the IT investments included in the second Business Plan.

The IT Investment Plan Guidance requires the ESO's submission to comply with the Technology Business Management (TBM) taxonomy.<sup>5</sup> A TBM-compliant IT Investment Plan submission will provide transparency about the current (as-is) and future (to-be) states of the ESO's IT, as well as the specific means by which the as-is state will be evolved and adapted into the planned to-be state. This information will enable Ofgem to undertake analysis of the ESO's existing IT and planned IT investments for assurance that the ESO's IT investments will economically and efficiently enable delivery of the overall ESO Business Plan.

## **Stakeholder responses**

We received one response to our consultation on the IT Investment Plan Guidance from the ESO. We have published the ESO's response on our website alongside the consultation.<sup>6</sup>

The ESO's response was broadly supportive of our proposals, highlighting that Ofgem and the ESO share an ambition to drive greater cost transparency and improved cost management through the application of the TBM taxonomy for the purposes of assuring the ESO IT investment portfolio. The ESO also welcomed the early engagement and collaborative approach taken to develop the guidance.

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<sup>4</sup> RIIO-2 Business Plans Guidance September 2019: <https://www.ofgem.gov.uk/publications/riio-2-business-plans-guidance-document>

<sup>5</sup> The TBM Council publish the TBM taxonomy. The TBM taxonomy provides a structured approach to explaining investments from three different "views" (Business, IT and Finance). The TBM taxonomy accomplishes this using four different "layers" (Business, IT Solutions, IT Towers and Cost Pools), with the IT Solutions and IT Towers layers together forming the IT view. At the time of writing, version 4.0 is the latest version of the TBM taxonomy: <https://www.tbmcouncil.org/learn-tbm/tbm-taxonomy/>

<sup>6</sup> Consultation on IT Guidance for ESO Business Plan Guidance: <https://www.ofgem.gov.uk/publications/consultation-it-guidance-eso-business-plan-guidance>

However, the ESO sought a change to the IT Investment Plan Guidance due to concerns that the Unified Cost Allocation Methodology (UCAM) limits its ability to achieve a full and accurate TBM breakdown for shared IT investments and Run the Business (RtB) IT costs.<sup>7</sup>

The ESO's response also stated that it will not produce any new or additional underlying justifications or expression of costs for UCAM-aligned cost elements.

## **Our decision**

After considering the stakeholder feedback we received to our consultation, we have finalised the IT Investment Plan Guidance (which is published alongside this letter).

We have outlined below the decisions we have made on certain areas of the guidance in response to stakeholder feedback.

### TBM data model requirements for shared IT investments and RtB IT costs

The ESO raised concerns that the UCAM limits the ESO's ability to achieve a full and accurate TBM breakdown for shared IT investments and RtB IT costs. The ESO argued that any cost allocation data provided at level 3 or 4 for shared IT investments and RtB IT costs would be too dependent on assumptions to provide additional value. In the case of shared IT investments, this information covers only those investments that met the Ofgem-agreed materiality threshold of £1m for a cost breakdown to be provided.

Therefore, the ESO suggested that it could only provide at least level 2 detail for material shared IT investments and RtB IT costs for the Cost Pools layer and that these costs could only be mapped through the other TBM layers to at least level 2 detail.

We understand the limitations presented by the UCAM allocation data for shared IT investments and RtB IT costs. Recognising that these costs were approved for the full 5-year RIIO-2 period, we have modified the guidance such that the ESO must provide:

- at least level 4 detail for all shared IT investments and RtB IT architecture for the Business, Solutions and Towers layers of the TBM;

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<sup>7</sup> The ESO's IT is composed of four different cost elements: direct IT investments, shared IT investments, Run the Business (RtB) IT costs and cyber resilience IT costs. Direct IT investments are fully funded by the ESO and designed to build new, or enhance existing, business capabilities. Shared IT investments are provided centrally by National Grid Group and composed mostly of IT infrastructure. RtB IT costs are ongoing ESO IT opex costs to support operations including resourcing, licencing and ongoing IT infrastructure spending. Cyber resilience IT costs relate to cyber resilience IT investments.

- at least level 2 cost detail for material shared IT investments and RtB IT costs for the Cost Pools layer of the TBM; and
- at least level 2 cost detail for mapping these costs through the Business, Solutions and Towers layers.

The ESO must undertake best endeavours to provide further levels of detail on shared IT investments and RtB IT costs. We require the ESO to provide level 4 detail for all shared IT investments for the Business, Solutions and Towers layers but understand that it may not be possible to provide detail beyond level 2 for non-material shared IT investment costs.

For the avoidance of doubt, our requirements for direct IT investments, including the additional Projects layer,<sup>8</sup> are unchanged from our consultation position.

We have also provided additional guidance on how the IT Investment Plan Guidance applies to each of the four cost elements that comprise ESO IT costs (direct IT investments, shared IT investments, RtB IT costs and cyber resilience IT costs).

#### Information submitted for shared IT investments and RtB IT costs

The ESO's response stated that it will not produce any new or additional underlying justifications or expression of costs for UCAM-aligned cost elements. Therefore, the basis of all information submitted for shared IT investments and RtB IT costs will be the exact documents that met the requirements for approved baseline funding as part of the RIIO-T2 Determination process.

We agree that the UCAM presents limitations for providing detailed TBM-aligned cost information for the purposes of the TBM data model submission by April 2022. However, should producing the required level 4 detail for the Business, Solutions and Towers layers of the TBM require information not provided in the information originally submitted for shared IT investments and RtB IT spend, then we expect the ESO to produce this additional information for the April 2022 TBM data model submission.

Furthermore, we do not agree that the ESO is unable to provide further information on shared IT investments and RtB IT costs if requested to do so as part of our review of the IT Investment Plan. As part of our BP2 Determination process,<sup>9</sup> we use Supplementary

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<sup>8</sup> As part of the requirement to submit a TBM taxonomy-compliant data model as part of the BP2 IT Investment Plan, we require the ESO to include an additional "Projects" layer that lists the ESO's IT investment projects. The information included in the Projects layer must be relatable to all other layers of the TBM data model.

<sup>9</sup> Our Determination process for the ESO in BP2 is set out in Chapter 2, ESO Business Plan Guidance: <https://www.ofgem.gov.uk/publications/eso-business-plan-guidance>

Questions to request any additional information that we need to inform our Determinations on the ESO's Business Plan.

Therefore, we may use Supplementary Questions to request more detailed information on the ESO's shared IT investments and RtB IT costs where this information will enable us to reach an informed view on the cost efficiency of the ESO's proposed direct IT investments.

### **Next steps**

The IT Investment Plan Guidance will come into effect from 15 December 2021.

We greatly appreciate the input stakeholders have contributed to the development of this specific guidance for the ESO's IT investments as part of the ESO's BP2 Business Plan submission.

If you have any questions on the contents of this letter, please contact us at the email address above.

Yours sincerely,

Adam Gilham

**Senior Manager, ESO Regulation**