

Decision

SHET Non-Operational IT Capex Re-opener Final Determination

Publication date:	5 October 2023
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This document sets out our decision on SHET Non-Operational Information Technology (IT) Capex Re-opener submission.

As part of the RIIO-2 price control, network companies can apply for additional allowances via the Non-Operational Information Technology Capex Re-opener uncertainty mechanism.

In the 23 January 2023 to 30 January 2023 Re-opener window, we received a submission from SHET for additional allowances. We consulted on our Draft Determination and associated draft direction between 22 May 2023 and 24 June 2023. Having considered all responses to our consultation, this document sets out our decision on what allowances, if any, to award. This document also includes the formal direction used to implement our decision into SHET's licence.

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1. Introduction

Section summary

This section explains SHET's submission, our assessment and consultation process, and how we came to a decision.

Introduction to RIIO-2

- 1.1 Network companies are natural monopolies. Effective regulation of privatised for-profit monopolies is essential to ensure they cannot unfairly exercise their monopoly power to the detriment of their customers. This is particularly important in the case of essential utilities, such as energy, where consumers have no choice on whether or not to pay what they are charged. It is therefore crucial that an effective regulator protects energy consumers by controlling how much network companies can charge their customers. Ofgem does this through periodic price controls that are designed to ensure network companies are properly incentivised to deliver the best possible outcomes for current and future energy consumers. This includes ensuring that consumers only pay for investments that are needed and do not overpay for those investments.
- 1.2 The current price control model is known as RIIO (Revenue = Incentives + Innovation + Outputs). RIIO-2 is the second price control under the RIIO model for electricity transmission, gas transmission and gas distribution, and runs from 1 April 2021 until 31 March 2026. It includes a range of Uncertainty Mechanisms (UMs) that allow us to assess applications for further funding during RIIO-2 as the need, cost or timing of proposed projects becomes clearer. This ensures that consumers fund projects only when there is clear evidence of benefit, and we have clarity on likely costs and cost efficiency. These mechanisms also ensure that the RIIO-2 price control has flexibility to adapt as the pathways to Net Zero become clearer.
- 1.3 Where possible, we have set automatic UMs, such as the Generation and Demand Connection Volume Drivers, which provide Electricity Transmission Owners with immediate funding when they are required to undertake new customer connection works. In other areas, where the degree of uncertainty is too great to allow for an automatic mechanism, we set 're-openers' which will allow us to assess proposals robustly once information with sufficient accuracy is made available.

1.4 The Non-Operational IT Capex Re-opener provides network companies with specific windows within the RIIO-2 period where they can request additional funding for new and replacement IT assets, including hardware, infrastructure, and software development projects, some of which may be critical for achieving Net Zero.

What did we consult on?

1.5 We¹ consulted on adjusting SHET's Non-operational Information Technology (IT) Capex² outputs and allowances under the RIIO-2 Non-operational IT Capex Re-opener.

1.6 In accordance with Special Condition 3.7 (Non-operational IT Capex Re-opener), SHET applied to Ofgem to add additional allowances for Non-operational IT projects into its RIIO-2 price control framework. SHET applied for five projects within its submission:

- Project 1: Integrated Project Management
- Project 2: System and Network Planning
- Project 3: RIIO-T3 Strategy and Planning
- Project 4: Small IT Changes
- Project 5: Project TReNDS

1.7 Following its submission in January 2023, SHET also provided additional information to us through a combination of bilateral meetings and Supplementary Question (SQ) responses.

1.8 We considered SHET's proposals and its justification for the funding requested in accordance with our principal objective and statutory duties. In line with the Re-opener Guidance and Application Requirement Document³, our assessment covered the following three areas for each project:

- the needs case
- the options assessment and the justification for the proposed project
- the efficient costs for the proposed project

¹ The terms "we", "us", "our", "Ofgem" and "the Authority" are used interchangeably in this document and refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

² Expenditure on new and replacement IT assets, including Hardware & Infrastructure and Application Software Development

³ [Re-opener Guidance and Application Requirements Document: Version 3 | Ofgem](#)

We combined this information to create our Draft Determination on what additional allowances, if any, should be provided to SHET to undertake the project.

- 1.9 We issued a consultation on our Draft Determination⁴ for stakeholder feedback, alongside a draft of the direction that would be used to implement the Draft Determination. Only one stakeholder, SHET, responded to the consultation. A summary of this consultation response is included in Chapter 2. Having considered the response, our Decision is set out in Chapter 3.
- 1.10 Throughout this document all monetary figures are in 2018/19 prices, to align with the original RIIO-2 price base.
- 1.11 Appendix 1 sets out our direction that will implement this decision in to SHET's licence.

Context and related publications

- 1.12 The scope of this document is limited to SHET's Non-operational IT Capex Re-opener. This document is intended to be read alongside:
- SHET Non-Operational IT Capex Re-opener Draft Determination (May 2023)⁵
 - SHET's Licence Special Conditions 3.7
 - RIIO-2 Re-opener Guidance and Application Requirements Document
 - RIIO-2 Draft Determinations – Core Document⁶
 - RIIO-2 Final Determinations – Core Document (REVISED)⁷

⁴ [RIIO-2 Non-operational IT Capex Re-opener Draft Determination: SHET | Ofgem](#)

⁵ [RIIO-2 Non-operational IT Capex Re-opener Draft Determination: SHET | Ofgem](#)

⁶ https://www.ofgem.gov.uk/system/files/docs/2020/07/draft_determinations_-_core_document_redacted.pdf

⁷ https://www.ofgem.gov.uk/system/files/docs/2021/02/final_determinations_-_core_document_revised.pdf

2. Project 1: Final Determination

Section summary

This section summarises Project 1 (Integrated Project Management): our Draft Determination, SHET's response to it and our Final Determination.

Summary of our Draft Determination

- 2.1 In its submission, SHET explained that its ambition is to become a digital company and that this ambition covers all aspects of the business from project delivery to operational decisions. SHET considers that, based on its current level of digital maturity in capital asset delivery and the growing portfolio of assets requiring connection to the transmission system, that there is a risk of not delivering its programme of capital works.
- 2.2 To address this need, SHET has planned an Integrated Project Management (IPM) project, which would entail the digitalisation of the key management processes underpinning its capital delivery programme, such as schedule, cost, risk, and issue management. SHET plans that this standardisation would help ensure best practices are embedded in complex capital delivery.
- 2.3 In its optioneering SHET explored three options:
- Do nothing
 - Deliver the IPM project now – preferred.
 - Deliver the IPM project later
- 2.4 In our Draft Determination we agreed with SHET's needs case and agreed that delivering the IPM project now was the right option to meet the needs case. However, we were concerned by the level of cost uncertainty because the main procurement exercise for the software had not been undertaken by the time of submission.
- 2.5 We concluded that SHET should resubmit the project in the next Re-opener window (September 2023) for a final decision. This would provide SHET with the time necessary to:
- Finalise the product selection activity and, having selected the product, undertake an analysis of the solution to determine the scope to be delivered (with final cost estimates) in the remainder of the T2 period.

- Once the scope is determined, work with us to develop proposals for PCDs that are measurable, achievable and that help to mitigate remaining risks and uncertainties.

SHET's response to our Draft Determination

2.6 SHET responded to our consultation and agreed with our Draft Determination for the project. SHET equally agreed to consider our feedback carefully ahead of its submission in the September 2023 re-opener window.

Our Final Determination

2.7 Given SHET's positive response, we confirm that we are provisionally satisfied with the needs case and optioneering, subject to final costs. But we are rejecting the proposal until we can assess a re-submitted proposal with the elements in paragraph **2.5** above included.

3. Project 2: Final Determination

Section summary

This section summarises Project 2 (System and Network Planning): our Draft Determination, SHET's response to it and our Final Determination.

Summary of our Draft Determination

- 3.1 In its submission, SHET explained that consumer needs are changing due to changes in the supply and demand profiles on its network. Shifting demand such as electric vehicle charging and heat pumps alongside local energy generation such as solar photovoltaic are changing power flows.
- 3.2 SHET explained that to better manage this changing flow and minimise expensive network reinforcement activity there is a need to upgrade its systems and tools and increase its computational power, so it can model more scenarios and sensitivities. It also needs to be able to use external data in more variety and volume and to ingest it into its modelling systems, which will enable it to meet its open data platform obligations and ambitions.
- 3.3 For its optioneering, SHET considered:
- Do nothing
 - Deliver the project now – preferred.
 - Deliver the project later
- 3.4 We agreed with SHET that the project should be undertaken and should be undertaken during RIIO-2 as it will further SHET's digital agenda and deliver significant value for consumers.
- 3.5 We agreed that the majority of proposed spend is efficient. However, we disagreed with one element of the project, which is changes to the Regulatory Reporting Pack (RRP). We consider this element is unnecessary as this is a business-as-usual activity and therefore funded through baseline allowances. To adjust for this, we proposed to reduce the requested allowances by 1/6 of the requested amount (to account for a reduction of 1 out of the 6 sub-projects) by £0.75m.

SHET's response to our Draft Determination

- 3.6 SHET disagreed with our proposed reductions of £0.75m. It highlighted that Ofgem had previously informed SHET that the RRP process would be overhauled

and digitised, creating a more structured way to submit regulatory data. SHET believes that investments to improve its regulatory reporting is a “no-regret investment” which will improve the efficiency and effectiveness of its processing by reducing manual processing and therefore setting it up for the next price control period.

Our Final Determination

- 3.7 Having reflected upon SHET’s response, we continue to consider that allocating allowances to prepare for potential RRP changes is not economically efficient. There are currently no major changes to the RRP process, and we would expect changes to be handled as a business-as-usual expenditure within existing baseline allowances. As SHET has not provided any additional information on the specific costs of the RRP sub-project in its response, we will maintain the position in our Draft Determination, which is a 1/6 (£0.75m) reduction for the System and Network Planning project.
- 3.8 **Table 1** below details SHET’s requested funding and our final allowances awarded for this project.

Table 1: Final Determination on Project 2

SHET proposal	Our Draft Determination	Our changes following consultation	Our Final Determination
£4.47m	£3.73m	£0	£3.73m

- 3.9 To ensure good value for money is achieved, we will allocate a Price Control Deliverable (PCD) to this project. This will require SHET to evidence successful delivery of the System and Network Planning project, and to achieve this we would expect to see evidence of its delivery of the five sub-projects. The project will need to be completed on or before 31 March 2026 (the end of the RIIO-T2 price control period). We have set this PCD out in the formal PCD format as part of the direction in Appendix 1.

4. Project 3: Final Determination

Section summary

This section summarises Project 3 (RIIO-T3 Strategy and Planning): our Draft Determination, SHET's response to it and our Final Determination.

Summary of our Draft Determination

- 4.1 In its submission, SHET requested £1.25m to run a RIIO-T3 IT Strategy and Planning project.
- 4.2 This project would include:
- Development of a new strategy framework for IT
 - Development and approval of an evergreen IS strategy, and corresponding sub-strategies
 - Delivery of an IT operating model design
 - Establishment of a roadmap of change needed to achieve the desired future state
 - Development, assurance, and submission of a business plan appendix for the next price control period covering Non-operational IT & Telecoms and Operational IT
 - Development, benchmarking, assurance, and submission of project definition and justifications, in line with the yet to be released sector specific methodology and guidance for the next price control period
 - Ongoing support to Ofgem in the evaluation of its submission through the Supplementary Question process
- 4.3 Our Draft Determination concluded that we consider planning for future price control periods as a business-as-usual activity and is funded through baseline Total Expenditure (Totex) allowances. Our Draft Determination was therefore to reject the full amount requested (£1.25m).

SHET's response to our Draft Determination

- 4.4 SHET disagreed with our Draft Determination to reject this project. It replied that whilst it accepted the requirement to prepare for the next price control has been anticipated since the outset of RIIO-2 the growth in its business represents a "paradigm shift" for SHET. To illustrate its point, it highlighted that the

investments under the Accelerated Strategic Transmission Investment (ASTI) framework is equivalent to twelve London Olympic stadiums.

Our Final Determination

- 4.5 We appreciate that the work SHET is undertaking has grown since the RIIO-2 price control period began. However, the type of work that SHET is looking to undertake with this project – creating an IT strategy, developing the future business plan, supporting Ofgem in the Supplementary Question process – was always going to be needed in any scenario and are activities that we would expect all network companies are likely to undertake throughout RIIO-2.
- 4.6 Therefore, we continue to conclude that this is business-as-usual activity and is funded through baseline Total Expenditure (totex) allowances. Our Final Determination remains to reject the full amount requested (£1.25m).

5. Project 4: Final Determination

Section summary

This section summarises Project 4 (Small IT Changes): our Draft Determination, SHET's response to it and our Final Determination.

Summary of our Draft Determination

- 5.1 In its submission, SHET explained that there is an increasing expectation from its customers and stakeholders that it will be able to adapt and provide digital solutions as part of its day-to-day activities. In line with this, SHET predicts that the number of requests, both internally and externally, for small IT changes will increase over the coming years. Example requests include:
- Small hardware purchases
 - Software upgrades
 - Small software purchases
 - Small platform changes
 - Small workflow or user interface changes
- 5.2 To handle the increase in requests for small IT changes, SHET proposed an ex-ante 'use it or lose it' (UIOLI) funding pot, with an allowance of £1,072,482 to support this investment.
- 5.3 Our Draft Determination concluded that the type of investments requested by SHET represent business-as-usual activity and is therefore funded through baseline Total Expenditure (totex) allowances. Our Draft Determination was therefore to reject the full amount requested (£1.07m).

SHET's response to our Draft Determination

- 5.4 SHET disagreed with our Draft Determination to reject the project. As with Project 3, SHET explained that its business has seen substantial growth since the start of RIIO-2 due to the ASTI framework. Additionally, SHET explained that Covid-19 has driven the move to large-scale hybrid working which has necessitated changes such as office refits and the provision of IT equipment for home working. SHET continues to consider that a UIOLI pot would be the right method for handling small changes required due to these two key changes (ASTI and Covid-19).

Our Final Determination

- 5.5 Like Project 3, we appreciate that the work SHET is undertaking has grown since the RIIO-2 price control period began. However, the type of work that SHET is looking to undertake with this project – software/hardware upgrades, small platform changes and user interface changes – was always going to be needed in any scenario and are activities that we would expect all network companies are likely to undertake throughout RIIO-2. SHET’s policies on post-covid working arrangements, such as office refits and working from home, are its own policies that it is funded to deliver as efficiently as possible through baseline allowances.
- 5.6 Therefore, we continue to conclude that this is business-as-usual activity and is funded through baseline Total Expenditure (totex) allowances. Our Final Determination remains to reject the full amount requested (£1.25m).

6. Project 5: Final Determination

Section summary

This section summarises Project 5 (Project TReNDS): our Draft Determination, SHET's response to it and our Final Determination. This project relates to Critical National Infrastructure, some parts have been redacted.

Summary of our Draft Determination

- 6.1 [REDACTED]
- 6.2 [REDACTED]
- 6.3 [REDACTED]
- 6.4 We concluded that the project is likely to deliver significant value and a rapid return on investment. However, given the significant commercial viability of this project, there did not appear to be a strong case for additional consumer funding as the Totex Incentive Mechanism (TIM) provides a route for rewarding licensees for savings delivered through innovations such as this project. Therefore, our Draft Determination was to reject the full allowance requested (£2.18m).

SHET's response to our Draft Determination

- 6.5 SHET disagreed with our Draft Determination position and explained that we should approve the project, for two key reasons:
- The financial savings from implementing the project within RIIO-2 will not be realised until the next price control period so there is no financial incentive to deliver this project now.

- That SHET believes the work it intends to do is “considerably more impactful than that undertaken to date by other network operators” who would also benefit if the project was successful.

Our Final Determination

- 6.6 SHET has provided additional evidence in its consultation response demonstrating that any savings from the project would not be realised within RIIO-2. Additionally, if SHET is willing to share the learnings from this project and ensure other network companies can achieve savings then this could multiply the benefits for consumers.
- 6.7 Based on the additional information provided by SHET in its consultation response, and our reconsiderations, we have concluded that funding this project is likely to drive future savings for consumers for the next price control period. So, we are changing our Draft Determination position and approving this project in full. **Table 2** below details SHET’s requested funding, changes following our consultation, and final allowances.

Table 2: Final Determination on Project 5

SHET proposal	Our Draft Determination	Our changes following consultation	Our Final Determination
£2.18m	£0m	+£2.18m	£2.18m

- 6.8 However, to ensure that the benefits set out by SHET are realised we will impose a Price Control Deliverable that means the project must be delivered in full and SHET must demonstrate that the learnings have been shared with other relevant network companies. The PCD must be delivered by the end of the RIIO-T2 period, and it is set out in the formal PCD format in Appendix 1.
- 6.9 Given the information provided by SHET, we expect that SHET will reflect the expected savings from this project into its unit costs in its Business Plan for the next price control period. If we do not see the expected savings in SHET’s Business Plan, then we will factor this into any allowances that we set for the next price control period.

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Appendix 1 – Direction

Direction under Special Condition 3.7.6 of the electricity transmission licence held by Scottish Hydro Electric Transmission plc (the Licensee) to add allowances for Non-Operational IT Capex

A1.1 Scottish Hydro Electric Transmission plc is the holder of a licence granted or treated as granted under section 6(1)(b) of the Electricity Act 1989.

A1.2 Special Condition 3.7 provides a re-opener mechanism by which the Licensee may seek additional funding during the RIIO-2 price control period for activities capable of improving the efficiency or performance of its Non-operational IT Capex. The Licensee applied to the Authority under Special Condition 3.7.6 in January 2023.

A1.3 The Gas and Electricity Markets Authority ('the Authority') gave notice on 22 May 2023 in accordance with Special Condition 3.7.12 of our issuance of a direction under Special Condition 3.7.6 to amend Appendix 1 (Total Non-operational IT Capex Re-opener allowance) of Special Condition 3.7. The notice, published on the Authorities website, included the text of the proposed direction to issue, the reasons for the proposed direction and provided for representations to be made on or before 24 June 2023.

A1.4 The Authority received one non-confidential representation and has placed it on [ofgem.gov.uk](https://www.ofgem.gov.uk). Having considered this representation, the Authority has decided to proceed with making this direction. This document constitutes notice of the Authority's reasons for the direction.

A1.5 This direction will implement the Authority's decision on the Licensee's application to the Authority to add additional Non-Operational IT Capex allowances into its RIIO-2 price control framework. Further details on the reasons for and effect of this direction can be found in the main body of this document.

A1.6 Pursuant to Special Condition 3.7.6, the Authority hereby directs the changes to Appendix 1 Special Condition 3.7 as set out in this direction.

A1.7 This direction will replace Table 1 (the existing table within Special Condition 3.7 Appendix 1) with Table 2 below. The formatting has been improved to reduce ambiguity and align with tables used elsewhere in the licence.

Table 1

Total Non-operational IT Capex Re-opener allowance (£m)

	2022	2023	2024	2025	2026	Total
Re-opener Allowance	0	0	0	0	0	0

Table 2

Total Non-operational IT Capex Re-opener allowance (NOITOT) (£m)

	<u>2021/22</u>	<u>2022/23</u>	<u>2023/24</u>	<u>2024/25</u>	<u>2025/26</u>	<u>All years</u>
<u>Re-opener Allowance</u>	<u>0</u>	<u>0</u>	<u>2.383</u>	<u>2.283</u>	<u>1.243</u>	<u>5.909</u>

A1.8 This direction will also update Table 3 to include the new Price Control Deliverables.

Table 3

Non Operational IT Capex Price Control Deliverable (£m)

		Regulatory Year						
<u>NOITRE Project</u>	<u>Output</u>	<u>Delivery date</u>	<u>2021/22</u>	<u>2022/23</u>	<u>2023/24</u>	<u>2024/25</u>	<u>2025/26</u>	<u>Total</u>
<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>
<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>
<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>
<u>System and Network Planning Project</u>	<u>Completion of System and Network Planning project</u>	<u>before 31-March-26</u>	<u>0</u>	<u>0</u>	<u>1.243</u>	<u>1.243</u>	<u>1.243</u>	<u>3.729</u>
<u>TReNDS Project</u>	<u>Completion of Project TReNDS and demonstration that the learnings have been shared with other relevant</u>	<u>before 31-March-26</u>	<u>0</u>	<u>0</u>	<u>1.14</u>	<u>1.04</u>	<u>0</u>	<u>2.18</u>

network
companies

A1.9 This direction will take effect immediately.

Yours sincerely,

Jourdan Edwards

Interim Deputy Director Onshore Price Control Operations

For and on behalf of the Authority