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Dear Akshay,

SSEN Distribution response to Ofgem's RIIO-3 Draft Determinations for the Electricity Transmission, Gas Distribution and Gas Transmission sectors

1. SSEN Distribution welcomes the opportunity to respond to Ofgem's RIIO-3 Draft Determinations for the electricity transmission, gas distribution and gas transmission sectors. A separate process is being run for the next price control for electricity distribution (ED3), and it is important that decisions made for other sectors do not automatically set a precedent for the electricity distribution sector, which has its own set of challenges and opportunities.
2. However, the requirement for significant levels of network investment at pace to support economic growth and deliver net long-term decarbonisation goals is a common theme in the electricity sector. In that context, ED3 presents a distinctive opportunity to generate significant value for the UK by accelerating investment to efficiently build the future network and deliver the capacity required to meet stakeholder needs. By getting ED3 right we can:
 - Facilitate and accelerate development and sustainable economic growth.
 - Maximise value capture across the economy through skilled job creation, supply chain development, and innovation.
 - Accelerate electrification, benefiting customers through lower energy costs and unit rates.
 - Contribute to future-proofing the overall energy system, enhancing national resilience to climate change and external geopolitical threats.
3. We are the first DNO to have set out our emerging thinking for ED3¹, with our key message being that we see ED3 as a staging post on the way to 2050, a critical five-year period in our 25-year plan to ready networks for growth and net zero. In short, we are advocating that the Government and the regulator both mindfully approach ED3 with the goals of optimising the long-term contribution ED3 can give to UK growth and maximising long-term UK-value capture.
4. The objectives for ED3 are very different from the ED2 aim of minimising network costs and "decarbonising at least cost". The suite of mechanisms and incentives in ED3 therefore will need to look different to RIIO-ED1 and RIIO-ED2. This thinking is supported by the findings in the National Infrastructure Commission's report², which highlights that a step change in the approach to electricity distribution networks is needed including investing proactively in the network through greater strategic planning and a simplified price control framework. It also

¹ [Empowering Communities, Enabling Growth – Emerging Thinking for ED3](#)

² Electricity Distribution networks: Creating capacity for the future (NIC)

stated that the current rate of investment in electricity distribution networks needs to double by 2050 to meet demand.

5. Learnings must also be taken from the Independent Water Commission's review (IWC Review) of the water sector³ to ensure that Ofgem does not overly focus on minimising networks costs in the short term but instead incentivises network companies to plan and deliver ambitious network development that will meet the needs of consumers out to 2050. Ofgem should also reconsider its approach to ongoing efficiency in light of the IWC Review, as detailed further in the cost assessment section below.
6. We have focussed our response on areas we consider to be highest priority in line with our ED3 thinking in advance of Ofgem's Sector Specific Methodology Consultation (SSMC) later this year.

Business Plan Incentive

7. We note from discussions at working groups that Ofgem is proposing to base the ED3 Business Plan Incentive (BPI) on the RIIO-3 BPI with modifications to ensure it supports the objectives of the ED3 price control. In our view, the key evolution should be for the ED3 BPI to explicitly incentivise high-quality long-term investment planning. This will be fundamental to the success of RIIO-3 and ED3 and therefore should be appropriately within the BPI.
8. For Stage A, we are supportive of the principle of clear minimum requirements and Ofgem could incorporate aspects of the long-term integrated plan into this stage. However, we emphasise that that minimum requirements must be clearly articulated and provided early to DNOs, with a proportionate approach to penalty. We also welcome Ofgem's request for DNOs to submit early proposals for ambitious and progressive new commitments and / or delivery mechanisms that benefit consumers ahead of SSMC. Further thinking is required on how these could be used to set new minimum requirements for all DNOs in practice.
9. For Stage B, Ofgem needs to be clear on what it is seeking to incentivise in the BPI in relation to cost efficiency. It must avoid overlapping rewards and penalties for cost efficiency performance, and the approach to assessing cost efficiency should take into account the longer-term network investment approach, pace of change and appropriate level of efficiency challenge. There are significant interactions with the cost assessment framework, which we comment on later in this letter.
10. On the quality stage of the BPI, Ofgem should incentivise high-quality long-term investment planning that drives the ED3 plan where it delivers clear benefits for consumers over the long-term. It should consider Ofgem's strategic priorities such as economic growth and resilience as well as the ambition embedded within the long-term integrated plans.
11. The results from the application of the RIIO-3 BPI show that the rewards and penalties under the comparative element of Stage B significantly outweigh those in any other element of the BPI. In an environment with significant growth, Ofgem should reconsider the balance of rewards and penalties across the different elements of the BPI to ensure that suitable importance is placed on quality and ambition of long-term plans, and that the cost efficiency component is proportionate to the scale of the challenge and the changing environment.
12. Finally, it is important that learnings from the RIIO-3 BPI process are taken on board for ED3. Ofgem should consider whether the wide-ranging outcomes from the BPI (ranging from £24.2m reward for NGN to -£17.5m for SGN) are a truly reflective measure of differences in the quality and ambition of companies' business plans.

³ [Independent Water Commission: review of the water sector](#)

Incentive Package

13. Incentives play two key roles in the price control: most obviously they drive performance on the chosen outputs, however they also play a critical role in making network investment attractive as it competes for capital across other asset classes.
14. We note the proposed introduction of new incentives to drive performance in areas that will be critical in RIIO-3, as we ramp up activity to support wider decarbonisation and societal goals. For ED3, we support the consideration of new incentives on which should be consulted on through the SSMC. Some of the incentives proposed in the RIIO-3 DDs could be relevant in the context of ED3, for example incentives on delivery, or on innovation delivery roll-out, and should be considered as part of SSMC. However, careful consideration will be required to ensure that mechanisms drive the right behaviours, deliver genuine consumer benefit and do not increase risk by penalising DNOs for factors outside their control.
15. This applies to reviewing and evolving the any existing incentives, to ensure they remain fit-for-purpose in an ED3 context.

Early ED3 Funding

16. The upfront mechanisms of the Accelerated Strategic Transmission Investment (ASTI) and the Advanced Procurement Mechanism (APM) are both useful tools that Ofgem has introduced to enable TOs to deliver the pace of investment required to meet demand and generation needs. want to work with Ofgem to ensure that DNOs similarly have the appropriate tools in place to enable advanced funding ahead of ED3 to deliver schemes that are critical to ensure we are on track to meet Net Zero and Clean Power 2030.
17. Mechanisms such as ASTI and APM have allowed TOs to give clear signals to the wider industry about the supporting needs that they will require throughout RIIO-3 and beyond. However, they could also have unintended consequences at the distribution level, including increased costs and difficulty sourcing materials in ED3. This is because we rely on many of the same supply chains as TOs, particularly in our SEPD licence area, where we have a programme of major capital delivery at the Extra High Voltage (EHV) / 132kV level, similar to Transmission projects.
18. Lead times are increasing, in particular for certain assets such as transformers and GIS equipment. Supply chain appetite to risk has also changed considerably in recent years and we are competing internationally with other network operators who have greater certainty to secure capacity.
19. In addition, we face distribution-specific issues at the HV and LV levels, with a smaller market altogether, and a risk of suppliers pivoting to transmission or renewables. Compounding these challenges is the fact we face an acute workforce and skills shortage. DNOs need an estimated 2,200 people each year from 2024 to 2030 to deliver future plans – including people with craft skills like jointers who can take years to train. There is a risk of increasing workforce cannibalism within the energy sector, and between Distribution and Transmission, which could become a serious blocker for DNO delivery.
20. As part of our Load Related Expenditure Uncertainty Mechanism (LRE UM) re-opener strategic needs case submission to Ofgem in January 2025, we highlighted these challenges, as well as the approach we are proposing to take to mitigate risk. This will be captured as part of our funding ask in the LRE UM re-opener in October 2025, and we will be looking to Ofgem to consider those points as part of their assessment. This is in line with steers we have received from Ofgem in various bilaterals, and Ofgem's recent letter⁴ to DNOs directing additional windows under SpC 3.2 Part K: Load Related Expenditure (LRE) Re-opener, in which Ofgem stated:

⁴ Letter from Ofgem to Regulation Managers of Electricity Distribution Licensees, Load Related Expenditure Re-opener windows, 12 August 2025.

“ED3 will be developed to support long-term planning, enable strategic investment, and ensure the sector is equipped to meet future demand.”

21. We need to be able to make investment decisions now so that delivery within ED2 is possible, and we are set up to commence ED3 without pause or delay. These investment decisions include detailed engineering designs; procuring land and planning permission; and procuring contractors and long-lead equipment.

Uncertainty Mechanisms

22. We agree with Ofgem’s overall intent to include as much as possible in upfront baseline allowances and to reduce over-reliance on uncertainty mechanisms (UMs). However, there will naturally be cases of genuinely uncertain costs and this rationalisation must not come at the expense of having the right mechanisms to deal with these circumstances. It may be sensible to consider having a smaller number of UMs but with each having a slightly broader remit. We would also highlight that we would expect there to be a need for some new uncertainty mechanisms in ED3, such as for resilience.
23. There is no mention of amendments to the re-opener application process itself for RIIO-3, although there is reference to work over the summer to ensure that the pipeline of applications can be managed efficiently. In the rapid growth environment in ED3 it is critical that the re-opener process is streamlined, avoiding any unnecessary regulatory burden that risks creating delays to progressing with projects. Lessons should be learned from the re-opener application process in ED2, where final decisions have come 10-11 months after the application window, impacting on our ability to progress with projects.

Innovation

24. SSEN Distribution have a strong track record in participating fully in the NIA and SIF funding streams and welcome their retention for the RIIO-3 price controls. These funding mechanisms / allowances provide significant value in helping to drive change in the energy industry and deliver clear benefits for consumers. This is especially important in light of recent policy changes such as Clean Power 2030 and the increasing urgency of the need to decarbonise society. Furthermore, innovation funding in the energy sector helps to develop specialist skills in innovation companies in Great Britain, and helps to promote GB as a country at the leading edge of technological development, strengthening the value of GB plc.
25. On the NIA, setting allowances based on the assessment of the RIIO-3 Business Plan submission is sensible and should be retained as an option for consideration within the ED3 price control framework. We recognise the points made about the transparency of reporting on innovation projects. We support working with Ofgem to ensure the quality of reporting is improved, giving clear details of the work undertaken as well as the outputs and benefits to consumers.
26. The introduction of an advisory service for innovators is a positive step and we agree with the approach that Ofgem has taken for the funding of this service. As founder members of the Energy Innovation Centre (EIC) we recognise the value in bringing innovators into the energy industry to introduce new skills and perspectives to help us deliver greater benefits for consumers. For this to derive the greatest benefit, the advisory service needs to be clearly positioned within the overall innovation ecosystem to avoid confusion over different parties’ roles and responsibilities.
27. Regarding SIF funding, based on the current rate of spend, it seems sensible to keep the level of funding broadly equivalent to RIIO-2, which would mean adjusting for inflation to allow us to deliver a similar volume of work within the budget. From our perspective, the SIF mechanism has been successful, with around 250 projects funded and a good number of projects in the Beta phase. However, given the current innovation pipeline across the energy industry is about to deliver a significant number of deployment-ready solutions, the innovation deployment pot of £50m is too low and could be spent on a very small number of deployments. Particularly for

electricity distribution, it would be extremely valuable to have certainty that there will be an innovation deployment pot in ED3 as we develop our current portfolio and plan implementation in the next price control.

Cost assessment and efficiency

28. Though Ofgem has noted that many of the cuts to company business plans are due to lack of justification, our view is that the headline message of cutting allowances for network companies during a crucial period is detrimental. We would welcome clear feedback and methodology from Ofgem to ensure that DNOs are able to sufficiently justify strategically important work during ED3 business plan submission.
29. We welcome Ofgem publishing clear EJP guidance at the outset of the RIIO-3 process and would encourage that this process is followed for ED3 and incorporates learnings from this RIIO-3 process to avoid the same level of disallowances at DD stage. Ofgem needs to take a proportionate approach to EJPs, to minimise unnecessary regulatory burden and reflect the introduction of tRESP which should expedite needs case assessments.
30. We welcome recognition that several regional and company specific factors will continue from RIIO-2 to RIIO-3, however we note that when normalising across GDNs, Ofgem has rejected all regional and company specific factors proposed by the networks that reflect the evolving nature of resourcing challenges within the UK. Our view, which echoes similar findings from the IWC Review⁵, is that it is imperative for company specific factors to be accounted for sufficiently to provide an adequate level of allowances for network companies to deliver. It is not clear that the RIIO-3 DDs have achieved this outcome.
31. Whilst we agree that, in normal times in steady state, there is an element of inherent ongoing efficiency that DNOs should naturally achieve over time, we are not in steady state. To meet electrification decarbonisation goals, electricity network companies need to transform their businesses and drive step-changes in capacity. Expecting significant ongoing efficiency during such a big transition is obviously illogical. We are disappointed to see that Ofgem have taken a broad-brush approach, reducing the range of ongoing efficiency suggested by their consultants in order to justify 1% as a mid-point position at the risk of driving under investment. It will be imperative for RIIO-3 and ED3 that unachievable cost targets do not come before delivery at pace.
32. The above ongoing efficiency target paired with the proposed continued focus from Ofgem on achieving the 85% percentile efficiency frontier risks embedding lower performing networks into an inescapable cycle of lower allowances and poorer performance, exactly the trap Ofwat fell into. This risks a perverse incentive to deliver less critical capital investment, which is a clear parallel to the challenges outlined in the IWC report⁶.

Real price effects

33. We welcome Ofgem's acknowledgement that the approach to addressing real price effects needs to evolve. However, we note that there is no evidence provided to support the revised indices or weightings proposed. The lack of clear impact assessment to articulate how closely the suggested approach correlates to cost movements experienced by the networks makes it difficult to comment in more detail.
34. On the surface it is hard to justify why the movement in timber, aluminium and copper costs would each be weighted equally to those of plastic pipes in a sector with a substantial replacement programme based on installation of plastic pipes, for example.
35. It is therefore difficult to comment on whether the appropriate approach to RPEs has been identified. It is important that these issues are addressed for the calibration of any RPE mechanism in ED3.

⁶ [Independent Water Commission: review of the water sector](#)

36. Any imbalance in the assessment of RPEs has a consequence to overall assessment of efficiencies. If this is mis-calibrated, costs that should appropriately be considered as outside of networks' control would be incorporated into the cost assessment process and affect understanding of the efficient notional network.

Finance

37. ED3 must be both financeable and investable. As already outlined, we are entering a critical phase where Distribution networks must scale rapidly to support both economic growth and decarbonisation. Our ED3 strategy emphasises the need for stable returns to attract capital in an increasingly competitive global environment. We therefore welcome Ofgem's recognition that the financial framework must evolve to reflect macroeconomic volatility, rising capital costs, and the need for long-term certainty.
38. Since the RIIO-2 decisions, index-linked gilt yields and the Bank of England base rate have risen sharply, marking the end of the cheap money era— yet the uplift in allowed returns has been inadequate in reflecting this shift. We urge Ofgem to ensure that the cost of capital is set at a level that enables Network Operators (across the electricity sector) to deliver efficiently and confidently, while maintaining affordability for consumers. The current macroeconomic environment is characterised by heightened volatility, inflationary pressures, and increased geopolitical risk. These factors materially affect the cost and availability of capital and must be better reflected in the financial parameters underpinning RIIO-T3 and by consequence ED3. SSEN Distribution supports the use of robust market evidence in setting the allowed return on equity and debt, but cautions against relying too heavily on historic averages that may no longer be representative. A forward-looking approach is needed—one that recognises the delivery risks associated with scaling up investment, and the need to maintain investor confidence in the face of rising costs and supply chain constraints. We are concerned by the lack of recognition that extensive, evidence backed risk analysis submitted by TOs has received by Ofgem.
39. SSEN Distribution supports Ofgem's acknowledgement of the vital role financeability plays in enabling the UK's energy transition. However, we believe Ofgem's decision to align capitalisation rates with the natural rate weakens financeability compared to the previous approach of setting them marginally below the natural rate. The earlier methodology provided a prudent buffer that supported cash flow stability and investor confidence—both critical to attracting long-term capital. By removing this buffer, the revised approach increases exposure to short-term volatility and reduces the financial resilience of Network Operators at a time when sustained investment is essential.
40. As outlined in our response to Ofgem's ED3 framework consultation SSEN Distribution urges Ofgem to reassess its regulatory depreciation approach for ED3 and beyond, highlighting that the extension of asset lives from 20 to 45 years — intended to promote intergenerational fairness—has instead created disparities and financeability challenges. The dual depreciation profiles have led to a temporary under-recovery of costs, reducing depreciation income and customer bills in the short term but increasing long-term costs due to higher RAV and return elements. Analysis forecasts a critical low point in depreciation income by 2036, with full recovery only by the late 2060s, undermining investor confidence and sector attractiveness during a pivotal phase of the net zero transition. SSEN Distribution also questions the alignment of the 45-year policy with actual asset lifespans, particularly for offshore infrastructure, and calls for a balanced approach that considers technical asset lives, cashflow needs, and a fair distribution of costs across generations.
41. Finally, we encourage Ofgem to consider mechanisms that enhance investability. SSEN's ED3 priorities—resilience, agility, and community empowerment—depend on the ability to make strategic investments ahead of need. This requires a regulatory framework that not only ensures financeability in theory, but actively supports it in practice.

Bill impact

42. We recognise the importance of balancing necessary investment in the electricity distribution network with affordability for consumers. We support Ofgem's strategic rationale that investing now will mitigate higher future

costs, accelerate the transition to net zero, and enhance energy security. SSEN Distribution is committed to delivering value for money and ensuring that the benefits of a modern, resilient network are equitably shared across current and future consumers.

Yours sincerely,

Clothilde Cantegreil

Head of Strategy and ED3 – SSEN Distribution