

Dear Sir/Madam,

I would like to provide input on some specific areas of the RIIO-2 Sector Specific Methodology consultation, specifically around the area of Innovation and the NIA mechanism, questions CSQ44 and CSQ48.

**CSQ44. Do you agree with our proposals to encourage more innovation as BAU?**

An innovation as BAU approach will tend to focus minds on purely short term impact activities. The regulation of the industry sets a clear framework in which a company can maximise its return to shareholders. If the incentives in place do not include long term innovation, inevitably, businesses will squeeze long term innovation activities as they do not directly contribute to the financial return on a short term basis.

Research and Innovation are inherently risky and measuring in terms of business plan payback only could ignore the valuable leadings that come from ideas that do not reach BAU. Projects that would be regarded individually as failures in terms of delivering business impact may in fact deliver valuable learning on what doesn't work, that saves money and wasted effort across the industry.

Already it could be argued that DNO's are looking primarily at innovations that can be adopted as BAU and deliver a return on investment within the same price control period. While an important consideration, taking exclusively this approach will result in failure to build up a backlog of earlier stage technologies and solutions into the innovation funnel that can feed future years short term impact innovation projects.

There is a risk that all companies move towards a "fast follower" model, paying only lip service to longer term innovation or earlier stage innovation that can drive some of the major changes required for the energy system revolution. In this scenario innovation leadership would be lost and despite short term progress, the funnel of suitable early stage innovation could fall off a cliff edge in the foreseeable future. While early stage research would continue in universities and other research organisations, the bridge between the lower TRL and higher TRL activities would be impaired.

For these reasons I believe it is important to retain an NIA mechanism in the innovation framework.

**CSQ48. Do you think there is a continued need for the NIA within RIIO-2? In consultation responses, we would welcome information about what projects NIA may be used to fund, why these could not be funded through totex allowances and what the benefits of these projects would be.**

I believe there is a continued need for NIA in RIIO-2. The Innovation allowance enables a whole portfolio approach to be taken by a company, by supporting end to end innovation and the enabling activities required for successful long term innovation. Building on the input I provided for question CSQ44, the NIA provides the incentive to enable early/mid stage research that may not be funded in a BAU totex allowance arrangement and may be too small or too risky to survive in a competition only environment.

Requiring a competition for spend of any innovation funds would increase barriers for Universities and SME's to propose and engage in innovation projects. The time and effort required to be spent pre-approval would increase and likelihood of approval for early stage ideas would decrease, all

stifling innovation and engagement with these 3rd parties. NIA avoids this administrative overhead in setting up a project and reduces uncertainty that can kill an early stage project idea.

The NIA supports the establishment of baseline innovation supporting capability both inside DNO organisations and external supporting bodies like the EIC, University engagements and the PNDC. Transactional innovation funding would inevitably reduce the supporting activities and inhibit the longer term capability for innovation. It would require supporting bodies to spend more effort on “bidding” versus “doing”. It is unlikely that supporting bodies like the EIC or PNDC would exist to support innovation without the NIA framework or similar.

Best regards,

Alan Dunn  
*Chief Operating Officer*