

Interested parties

Direct Dial: 020 7901 7000

Date: 7 April 2021

RIIO-2 Strategic Innovation Fund - informal licence consultation

In our RIIO-2 Final Determinations¹, we set out our decision to introduce the Strategic Innovation Fund (SIF) for the Electricity System Operator, Electricity Transmission, Gas Transmission and Gas Distribution sectors.

The SIF is intended to support network innovation that contributes to the achievement of Net Zero, while delivering real net benefits to network companies and consumers; and to promote the increased alignment of Net Zero-related innovation so that activities appropriately funded by energy consumers are coordinated with activities funded by Government.

To meet the above-mentioned objectives, we will set the strategic direction on SIF funding using Innovation Challenges, invite funding applications from network companies and the Electricity System Operator to address these Innovation Challenges and seek to coordinate with other public funding bodies where appropriate.

We aim to introduce the SIF during 2021, with the ambition of setting our first Innovation Challenges in the summer; receiving bids for funding in response to those challenges in the autumn; and making funding decisions in winter. Ahead of this, we will engage with stakeholders on what those Innovation Challenges should focus on, on the process for issuing Innovation Challenges and consult on the governance arrangements for the SIF. Our current plan is to consult on the SIF Governance Document in May 2021.

¹ RIIO-2 Final Determination – Core Document, December 2020, pages 99-105:
<https://www.ofgem.gov.uk/ofgem-publications/170687>

The purpose of this consultation is to seek stakeholder views on a set of draft licence conditions that are required to implement the SIF.

The licence conditions

The draft SIF licence conditions are at Appendix 1 to this letter. The four draft licence conditions that are included within this informal consultation are as follows:

- Draft Special Condition 5.8 (for inclusion in each of the Electricity Transmission licences held by National Grid Electricity Transmission plc, Scottish Hydro Electric Transmission plc and SP Transmission Ltd)²
- Draft Special Condition 3.4 (for inclusion in the Electricity Transmission licence held by National Grid Electricity System Operator Ltd (NGESO))
- Draft Special Condition 5.5 (for inclusion in each of the Gas Transporter licences held by Cadent Gas Ltd, Northern Gas Networks Ltd, Southern Gas Networks plc, Scotland Gas Networks plc and Wales & West Utilities Ltd)
- Draft Special Condition 5.7 (for inclusion in the Gas Transporter licence held by National Grid Gas plc)

Alongside draft versions of these conditions, we have published a consolidated document containing in draft the interpretations and definitions that will apply in each condition.

The purpose of these new licence conditions is to establish the SIF. In accordance with the decision set out in Ofgem's RIIIO-2 Final Determinations, the licence conditions provide for Ofgem to direct that NGESO and NGGT recover funds via use of system charges, which will subsequently be distributed by the two system operators to other licensees in order to fund eligible SIF projects. The draft conditions also establish a mechanism through which funds can be returned by licensees to NGESO and NGGT under certain conditions (where directed by Ofgem). As part of our forthcoming statutory consultation on the RIIIO-2 Price Control Financial Models (PCFM) and Price Control Financial Handbooks (PCFH) later this month, we will consult on the introduction of the SIFF_t term into the PCFM and PCFH for National Grid Gas Transmission, to facilitate the recovery of SIF funding via this year's annual iteration process.³

In addition, these new licence conditions will provide for the introduction of the SIF Governance Document. This document will set out in detail (among other matters) how the

² The condition shall take the reference Special Condition 5.7 in the licence of Scottish Hydro Electric Transmission plc but is otherwise identical.

³ Changes to the PCFMs and PCFHs of other licensees are not required in order to implement the SIF.

SIF will be governed, the eligibility criteria for and the process through which proposed projects will be assessed and approved.

Responding to this consultation and next steps

Stakeholders are invited to provide views on the draft licence conditions in Appendix 1 by no later than 5pm on 5 May 2021. Responses should be sent to the RIIO-2 mailbox (RIIO2@ofgem.gov.uk)

Subject to feedback received via this consultation, the table below provides an indicative view of the next steps towards the finalisation of the SIF licence conditions.

Milestones on the SIF license	Date
Deadline for responses to this informal consultation	5 May 2021
Publication of statutory consultation	Mid-May 2021
Deadline for responses to statutory consultation (28-day consultation)	Mid-June 2021
Ofgem decision to modify licence (thereafter 56-day standstill)	End June 2021
Licence comes into effect	End August 2021

In the Electricity Distribution (ED) sector, we have confirmed that the SIF will be introduced in the RIIO-ED2 price control.⁴ We intend to consult on the introduction of the SIF licence conditions in this sector nearer to the commencement of RIIO-ED2 on 1 April 2023 as part of the wider RIIO-ED2 licence development process. ED stakeholders are nevertheless invited to respond to this current consultation.

Yours faithfully,

Steve McMahon

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⁴ RIIO-ED2 Sector Specific Methodology Decision: <https://www.ofgem.gov.uk/publications-and-updates/riio-ed2-sector-specific-methodology-decision>