

Email to:

[RIIO3@ofgem.gov.uk](mailto:RIIO3@ofgem.gov.uk)

12 March 2024

Dear Ofgem,

### **Response to the RIIO-3 Sector Specific Methodology Consultation**

Scottish Renewables is the voice of Scotland's renewable energy industry. The sectors we represent deliver investment, jobs and social benefits and reduce the carbon emissions which cause climate change. Our 360-plus members work across all renewable energy technologies, in Scotland, the UK, Europe and around the world. In representing them, we aim to lead and inform the debate on how the growth of renewable energy can help sustainably heat and power Scotland's homes and businesses.

Scottish Renewables welcomes the opportunity to respond to Ofgem's consultation on its RIIO-3 Sector Specific Methodology. We recently engaged in providing input to the overarching Future Systems and Networks Regulation (FSNR) consultation and are strongly aligned with Ofgem's ambition to change regulation to adapt to the fast-changing global context.

In line with Ofgem's newly proposed Sustainable Growth duty, the price controls for the upcoming period of 2026 onwards need to adequately reflect the turbulence of global markets to safeguard investments fuelling the green economy. Developing a methodology that has the flexibility to react to present and future impositions has become a more relevant approach than historic econometric benchmarking, as seen in RIIO-T2.

The focus is sharpening on the urgency of grid reinforcement to meet net-zero targets and facilitate the efficient delivery of domestic, clean renewable energy to end consumers. As the foundational point for the sector, grid readiness determines whether the potential for green economic growth can be seized. In line with the national approach for strategic, whole energy reform, RIIO-3 must closely consider the aims of the Transmission Acceleration Action Plan (TAAP) and the Connections Action Plan (CAP) to ensure harmonised regulatory reform that does not delay the urgent delivery of emission reductions.

Scotland is poised to deliver the renewable energy demands set out by the UK government, however, this hinges on an electricity system that is sufficiently capable of transporting energy from strategic areas of supply to final demand. As Scottish renewables are leveraged to meet UK energy targets, Ofgem must in turn recognise the ambition of the Scottish Government's

own net-zero targets for all greenhouse gas emissions by 2045, five years ahead of the UK, and appropriately reflect this in its regulatory decisions.

While we are in general agreement with Ofgem's proposals, we would like to draw attention to several areas of the methodology that we believe would require additional work.

### **Certainty in a time of volatility**

To afford the levels of confidence in business plans and timelines that industry and investors require, greater certainty and thus greater detail need to be provided within the methodology. While price controls have previously exercised a more cautious approach, the current macroeconomic environment demands greater security for Transmission Operators (TOs) to ensure transmission is not only financeable but investable. Since RIIO-T2, costs have changed considerably, and supply chains are becoming increasingly strained to meet the urgent demand from climate targets being pursued worldwide. Thus, Ofgem will need to maintain that the cost of capital is globally competitive to secure sufficient investment for grid projects at the scale required to deliver on climate targets.

While the industry is supportive of Output Delivery Incentives (ODIs) and other incentivisation, mechanisms need to be employed to account for the uncertainties arising from the unstable political, regulatory, and financial global landscape. To avoid unfair penalties resulting from external factors outside of TO control, flexibility mechanisms should be introduced to lessen the risk to investors on cost and timing uncertainty. Flexibility in price to factor in high-cost volatility and ongoing planning reforms could absorb some of the inflated risk placed on investors. Likewise, mechanisms that ensure sufficient investment is available for network resilience are increasingly important in accounting for extreme weather events incurred by climate change, often felt more intensely by Scotland.

Recent announcements have shown that investing in transmission infrastructure can help to revitalise Scotland's economy. SSEN Transmission plans<sup>1</sup> to spend £10 billion on upgrading the electricity grid in northern Scotland, which is expected to create over 9,000 high-value green jobs. The Scottish government has also announced<sup>2</sup> a £24.5 million grant to secure investment from Sumitomo Electric Industries for a new cable factory in Nigg that will serve the offshore wind sector, highlighting the synergy between economic growth and net-zero.

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<sup>1</sup> <https://www.sse.com/news-and-views/2023/06/ssen-transmission-s-10bn-networks-investment-to-support-over-20-000-jobs-throughout-uk/>

<sup>2</sup> <https://www.gov.scot/news/growing-scotlands-green-economy/>

The plant will create around 330 jobs and bring £350 million in inward investment to Scotland. This project has in turn provided opportunities for Scottish suppliers with THREE60<sup>3</sup> Energy securing a multi-million-pound contract to design and deliver cable storage carousels for the Sumitomo facility. Providing pipeline certainty to transmission operators and the grid and networks supply chain will ensure the nation can maximise the economic benefits arising from these vital infrastructure projects.

Electricity infrastructure enables thousands more jobs in new and existing renewable energy projects, from wind farm technicians to civil contractors and hotel staff.

### **Project regime building on ASTI**

Industry is asking for the regulatory framework to provide funding earlier than ever before based on transmission needs being pre-determined in the context of strategic planning for target delivery. The Accelerating Strategic Transmission Investment (ASTI) programme has proven successful in accelerating development and providing TOs with certainty and funding at an early stage. Ofgem should build on insight gained from this initiative to develop RIIO-3 methodologies that maintain a safe balance between protecting consumers and enabling investment.

Scottish Renewables welcomes the introduction of the Major Projects Regime (MPR) that builds on the principles of ASTI in supporting TOs to deliver grid development at pace. We commend Ofgem's proven agility in response to the urgency of targets and propose this continues with the introduction of automatic confirmation of pre-and early construction funding. This would both ensure developers can secure contracts within the constrained global supply chain network and are afforded more security in a time of unbalanced risk and return. In addition, the cumulative impact of ASTI/MPR projects will have a financial knock-on effect on estate, business support and information and operation technology costs that need to be recovered during the T3 period.

The pipeline of transmission infrastructure to be delivered in Scotland is extensive and presents the country with the opportunity to grow the local supply chain. To allow existing and new suppliers to increase their capacity and capabilities providing a clear view of the work to be delivered is crucial. Attracting inward investment and providing clarity for suppliers looking to expand their capabilities will allow them to prepare for the future whilst boosting green jobs and skills.

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<sup>3</sup> <https://scottishbusinessnews.net/three60-energy-pens-multi-million-pound-deal-with-japanese-company/>

Under Ofgem's new legal remit of ensuring net-zero, grid development needs to be prioritised ahead of forecasted demand to ensure a timely transition that protects existing and future consumers and meets government targets. A 'least regrets' approach to decision-making on network approvals would allow network companies to make affordable investments at the pace required with minimum risk while providing maximum benefit.

### **Support for Regional Investments**

While larger, strategic projects form the critical backbone of transmission infrastructure, neglect of regional investment would be detrimental to the eventual delivery of such strategic investment capacity downstream.

As it is currently outlined in the document, a robust regional regime is lacking and we believe Ofgem needs to consider regional planning more carefully, both at a similar scale and complementary to its major strategic project investments. Within regional planning, there is the absence of the financial mechanisms seen by larger projects, e.g., Pre-Construction Funding (PCF), which could hold back regional and Medium Sized Investment Projects' (MSIP) delivery dates that strategic projects ultimately rely on for connection delivery. It is imperative that strategic and regional planning are coupled together and financed to the same degree to ensure timely consumer connection and for this reason, we believe regional investments should fall under the MPR.

Within this remit, we believe that Ofgem should establish a set of common processes including for pre-and early construction funding, de-risking delivery and allowing early supply chain engagement to be adopted at regional and major project level. In so doing, Ofgem would engender greater harmony between national and regional investment in terms of delivery timescales, direction of travel and appropriate incentivisation.

Developing a coordinated regulatory framework that considers all scales of the transmission network, is well-evidenced and aligned is vital to ensuring a smooth and timely transition. Avoiding a fragmented 'piecemeal' approach will lead to better outcomes for consumers and return a faster pace of connection delivery.

### **Incentivisation**

Incentivisation needs to centre more closely around efficiency and the timely delivery of projects to meet net-zero and generate energy security, which, as aforementioned, must include strategic, regional investment. More generally, all incentivisation needs to be scaled up significantly to propel efforts to meet the ambitious 2030 target that falls within the RIIO-T3 period. The scale should appropriately reflect the change in investment required in the current

context to minimise the risk of windfall gains and losses. We are proposing that Ofgem should look to re-weight the incentive package to reflect these suggestions.

### **Innovation**

The promotion of innovation within energy network company monopolies through funding and support mechanisms provided in the innovation package is welcome. The Network Innovation Allowance (NIA) in RIIO-2 provided TOs with upfront funding for projects that targeted consumer vulnerability and/or long-term benefits for consumers. We would like to see similar measures that encourage innovation and reduce consumer costs to fight rising fuel poverty.

Despite previous innovation incentivisation, a bottleneck issue has emerged concerning the tangible delivery of innovative solutions, preventing benefits from being reaped, for example in the digitisation of infrastructure. Proposed shared data infrastructure and new deployment routes are available but need greater incentivisation for final follow through. Therefore, we are arguing that while the digital and innovation framework should include development, its priority should be on pushing pathways for delivery at scale to improve efficiency across the entire system.

### **Community benefit**

The role of communities in enabling the energy transition is almost nowhere more pertinent than within grid reform. By hosting national infrastructure, communities recognise the importance of enhanced transmission for a net-zero future but can also reap benefits both at a local and national scale. As Scottish communities will likely be impacted heavily by grid reform, the RIIO-3 framework should incorporate benefits to communities more explicitly and embed this as a priority into the price control structure to reflect its importance. The opportunity to pass through the costs of community benefit payments into the Transmission Demand Residual (TDR) should be robust to whomever constructs/owns the related network assets.

The scale of transmission works around the UK, and of their accompanying community benefits, is set to reach heights that will need to be recoverable for TOs through price control. To ensure projects are financeable, TOs will need to factor in the cost of individual and community-based compensation and the associated governance within their business plan submissions and projects.

As such, consideration, and subsequent calculation of community benefits at the individual and community level for strategic network plans need to receive much closer attention.

Scottish Renewables cautions Ofgem over the possible impacts of the implementation of a discount-based compensation and urges it to consider the eventual methodology for eligibility as well as monitoring the impacts of ungoverned financial injections. At the scale currently under discussion, the community benefits scheme needs far greater coordination and reflection to maximise benefits and ensure efficient spending.

Considering a wider perspective, innovative regulatory reform seen in the previous price control, including mechanisms such as ASTI, has been fuelled by government-led, nationally backed net-zero targets. To maintain the momentum that is driving the urgent pace of development and motivating swift policy reform, the need for clearer interim targets between 2035 and 2050 is crucial. Not only is policy reform expedited by the rigidity of targets, likewise incentivisation for both developers and investors relies on the certainty of deadlines to acquire competitive contracts with large supply chain providers.

Moving forward with the series of price controls leading up to 2050 targets, more frequent, periodic targets need to be set to drive consistent project delivery, for example, aligned with the CCC's carbon budgets. It is necessary to incorporate 'sticks' at regular intervals to garner government and public support and push for a 'follow-the-target' over a historic 'follow-the-market' outlook.

By making the right decisions now we can ensure that RIIO-3 facilitates the journey to meet net-zero while delivering long-term value for money and a green economic recovery.

Scottish Renewables would be keen to engage further with this agenda and would be happy to discuss our response in more detail.

Yours sincerely,

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