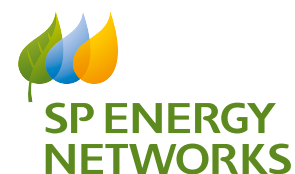


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SP Energy Networks RIIO-ED2 Board Assurance Statement

December 2021



PRINCIPAL PARTNER
**UN CLIMATE
CHANGE
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UK 2021**

IN PARTNERSHIP WITH ITALY

SP Energy Networks RIIO-ED2 Board Assurance Statement

As the SPENH board, we have taken proactive oversight in the development of the RIIO-ED2 business plan and are confident that it has been fully tested for accuracy, ambition, and efficiency. We are satisfied that it fully addresses Ofgem's business plan requirements and, further, that our proposals will deliver value for consumers that goes above and beyond these expectations.

This plan will be essential to enabling the UK's Net Zero targets, particularly those of our regional governments and communities, and we are confident that our plan forecasts fully support for legislated decarbonisation targets and trajectories. We are also satisfied in the strategic development of our business capabilities through digitalisation and enhanced workforce diversity and inclusivity. As we enter a critical time of change for the distribution sector, we fully support the ambition of the RIIO-ED2 plan to lead by example in enabling a just transition to our Net Zero future.

Objective of the Board

The Board of Directors of ScottishPower Energy Networks Holdings Limited (SPENH Board) has overall responsibility for the long-term strategy and direction of the RIIO-ED2 Business Plan. The SPENH Board comprises six Directors – two of which are independent.

Sra Elena León Muñoz	Chair	Non-Executive
Mr Frank Mitchell	CEO	Executive
Ms Alison McGregor	Member	Independent, Non-Executive
Professor Dame Lesley Anne Glover	Member	Independent, Non-Executive
Sr Jose Ignacio Sánchez-Gálán	Member	Non-Executive
Sra Monica Grau Domene	Member	Non-Executive

As the SPENH Board, we have taken a proactive oversight in the development of the RIIO-ED2 Business Plan. We have worked hard to ensure that the business plan is founded on the best interests of our consumers, stakeholders and network users – aligning with the company's future vision to ***“work with the communities we serve to enable a just transition to our Net Zero future”***.

This document sets out why we, as a board, are confident that the business plan and associated costs have been fully tested for accuracy, ambition and efficiency.

BOARD PROACTIVE OVERSIGHT

As a board, we have received regular updates on RIIO-ED2 from the outset of the project through our formal board meetings. In addition to these formal meetings, we have also held four dedicated assurance workshops with the RIIO-ED2 project team. These workshops have provided us with the opportunity to fully engage with the RIIO-ED2 project team members and challenge all aspects of the submission and development process.

They have also allowed us to understand the robust assurance framework that underpins the development process and provide us with confidence that scrutiny has been applied across all elements of the submission. We have been kept fully informed of the level of review and challenge undertaken by industry experts, leaving us with no doubt that our submission is well justified and viable.

Additionally, we have also welcomed the opportunity to speak to John Howard, the chair of our Customer Engagement Group (CEG) at both our formal board meetings and dedicated RIIO-ED2 assurance workshops. We have valued the CEG's input and challenge to the plan and we are confident, as a board, that their feedback has been fully considered and addressed by the project team.

The board also recognises the key role played by the RIIO-2 Challenge Group (CG) and have been kept informed by the RIIO-ED2 project team on the actions taken to address their feedback. However, the board notes the limitations to the depth of feedback received from the RIIO-2 CG due to their limited engagement with SPEN and the short timelines for review of extensive draft business plan content. The board also notes that CG feedback on draft business plans is largely generic across DNOs and that this has been a limiting factor in its contribution to final business plan development.

Accuracy, Efficiency and Ambition

The board is confident that the plan and associated costs have been tested for accuracy, efficiency and ambition:

Accuracy

The board recognise that our business plan must be accurate, well-justified and compliant with all regulatory requirements – this is vital to earn the trust of our consumers, network users and wider stakeholders. The robust assurance framework which underpins the RIIO-ED2 development process was approved by us, the board, and gives us confidence that every element of the business plan submission has been thoroughly reviewed by independent experts.

The assurance framework was based on a 'three lines of defence' model, with the risk scores used to drive the additional assurance activities carried out. This framework also ensures strict adherence to Ofgem's Data Assurance Guidance (DAG).

Challenge from internal or external experts

In addition to review and challenge from our independent internal experts, twelve external experts were engaged to further scrutinise multiple aspects of our submission. The areas covered by our external experts included review of our engineering justification papers to ensure they are robust, review of our Digitalisation Strategy and associated Cost Benefit Analysis, and review of our Environmental Action Plan.

The board met with one of these external assurance providers, PA Consulting, at one of the dedicated RIIO-ED2 assurance workshops and had access to all final assurance reports.

Updates on the key outputs of these assurance activities were provided by the RIIO-ED2 project team workstream leads at the dedicated assurance workshops. The board was satisfied with the breadth of coverage of these activities and that all recommendations had been addressed by the RIIO-ED2 project team.

Internal Assurance Team

The board have taken comfort from the involvement of the internal assurance team throughout the development process. The internal assurance team have used a risk-based approach to review the population of the Business Plan Data Tables – this has been an iterative process and the output of the review was presented to the board at one of the dedicated RIIO-ED2 assurance workshops. The board was satisfied with the approach and scope of the review.

Internal Audit

ScottishPower has a well-established independent Internal Audit team. Internal Audit has carried out two audits related to the RIIO-ED2 business plan assurance process. The final reports produced by Internal Audit have been noted by the ScottishPower Energy Networks Holdings Limited Audit and Compliance Committee as well as reviewed at the dedicated RIIO-ED2 assurance workshops.

Efficiency

Efficiency can be measured by the ability to avoid incurring additional expenditure in producing or delivering a desired output. These outputs are defined by the activities proposed in our Business Plan.

The board is confident that we have submitted an efficient business plan. The extensive assurance that has been used throughout the development process supports this view:

TOTEX DEVELOPMENT AND BENCHMARKING

The efficiency of our business plan Totex was tested using a benchmarking approach that was thoroughly developed in conjunction with independent economic experts NERA. The feedback received on our benchmarking approach focussed on ensuring good regulatory practice, transparency, and robustness in our modelling.

We took a structured and holistic approach to developing our Totex and benchmarking our plan. The results from our benchmarking analyses were used to continuously iterate our thinking and to challenge our Totex as it developed, ensuring our submission represents optimal value for our customers and stakeholders. The position calculated from our Cost Assessment methodology demonstrates an overall 5% efficiency in our forecast expenditure.

Totex development and benchmarking

	RIIO-ED2 Totex (£m)	Efficient view of Totex (£m)	Delta - Efficiency (£m)	Delta - Efficiency (%)
SPD	1,609	1,688	79	5%
SPM	1,661	1,735	74	4%
SPEN	3,270	3,423	153	5%

**numbers in above table do not include innovation expenditure*

The approach and methodology used for benchmarking the expenditure plans were presented to the board at the dedicated RIIO-ED2 assurance workshops; the board was satisfied with the approach used.

Bottom-up review of unit costs

A rigorous and bottom-up assessment of our approach to activity level unit costs was completed. This ensured our unit costs were thoroughly challenged for efficiency and were clear and transparent, providing opportunities to identify improvements at the lowest level.

Assurance of the methodology used to calculate the unit costs, in addition to verification of data source accuracy, was carried out by external assurance provider Arcadis.

Selection of the optimum and efficient solution

The level of activity in our plan has been substantiated by completion of over 100 Cost Benefit Analysis (CBA) papers, and over 130 Engineering Justification Papers (EJP). These papers provide a thorough appraisal of 100% of our Load related and Non-load related investments. This has enabled us to select and justify the optimum and most efficient solution.

All engineering solutions were reviewed and challenged by internal independent engineering experts, for our final submission we have progressed all of our EJPs through review and challenge by industry and regulatory experts S&C Electric who provided impartial assurance feedback.

The approach used by S&C Electric to review and challenge our EJPs was presented at one of the dedicated RIIO-ED2 assurance workshops – the board was satisfied with the approach and are confident that the justification papers that have been submitted are robust.



Refer to **Annex 7.1: Assurance for a list of all external assurance providers used, and their final assurance reports.**

Ambition

It is the board's view that we have submitted an ambitious business plan that will play a critical role in enabling the UK's ambitious climate change targets. The board has seen the level of ambition in our business plan commitments develop to meet the needs and priorities of our customers and stakeholders, informed by over 19,000 engagements, and become embedded in our plan:

Develop a network that's ready for Net Zero



We have an ambitious programme of work to develop the network of the future – we will enable our customers' Net Zero ambitions by directly facilitating 670k Electric Vehicles and 370k heat pumps in our baseline plan and the ability to flex our delivery plan if higher uptakes occur.

We will deliver a new approach to network management. Our Engineering Net Zero Platform will provide extensive network analytics to facilitate data-driven planning and operational decisions. We will increase its capability by widescale deployment of LV network monitors in RIIO-ED2, increasing coverage to 76% of customers by the end of RIIO-ED2.

We will continue to operate a safe, reliable and efficient network, reducing the rate of asset deterioration from 2.7% in RIIO-ED1 to 1.1% in RIIO-ED2, while managing greater levels of network criticality and complexity of operation.

We will improve the level of reliability our customers expect by making them 19% less likely to experience an unplanned power interruption on average, with the average duration reducing by 19%.

We have an ambitious digitally-enabled Connections Strategy which has been led by our customers' priorities. This will manage the expected increase in volumes and could result in £15m per annum of savings to connections customers by the end of RIIO-ED2 if the volumes of activity are realised.

We commit to establishing a Whole System planning function within our investment decision-making framework. This new team will be accountable for delivering a step change in Whole System solutions and outcomes. We anticipate that this initiative could result in up to £49m of net present value benefits for consumers over the RIIO-ED2 period.

Be the trusted partner for customers, communities and stakeholders



We will be a service leader in the UK, providing proactive and tailored service based on customers' preferences and needs. We will deliver excellent satisfaction for all customers to help them navigate an increasingly complex energy landscape – we will deliver customer satisfaction to 9.4 out of 10, maintaining industry leading ambition and performance.

By delivering focused support to our vulnerable and disadvantaged customers that is easy to access, we will help them save money, access the benefits of the low carbon transition, make use of technology, and receive support for wider social issues. We have an ambitious and Innovative Vulnerability Strategy that broadens our view of vulnerability and targets 276,000 customers – our highest number ever.

We are committed to helping deliver the bold ambitions of the communities we serve and will make £30m of Net Zero funding available.

We have developed our first Community Energy Strategy which, alongside our bespoke output proposals, will build on our current support for community anchor organisations who we know will be key to supporting the delivery of network innovation – particularly for those living in vulnerable circumstances - at the rate and scale required over RIIO-ED2 and beyond. We estimate that the incentivised Community Energy (CE) activities attributable to SPEN in our licence areas will produce gross customer benefits of £45.65m.

Ready our business for a digital and sustainable future



Environmental sustainability is at the heart of our plans – we will reduce our controllable business carbon footprint by 37.8% in RIIO-ED2 and achieve Net Zero of our operations by 2035.

We will promote an inclusive, diverse and community-based workforce to deliver our ambitious plans and will recruit over 1,100 staff during RIIO-ED2. We will grow our talent from the communities we serve and continue to create new, Green Jobs for young people. 90% of our workforce renewal for our craft roles and 50% of our engineering and technical roles will come from our trainee programmes.

Digitalisation and data will play a key role in improving services to our customers and stakeholders. We have an ambitious programme of digital and data initiatives that are central to the delivery of our business plan commitments – the embedding of new digital approaches, innovation and process redesign will save customers over £36m.

AFFORDABILITY

Despite delivering a 28% increase in our expenditure programmes to deliver Net Zero, our baseline plans will not see a material impact to customer bills. Our SPD customers will see a 12% reduction in RIIO-ED2, while our SPM customers will see a rise of 6% within the RIIO-ED2 period. Both SPD & SPM customer bills will then reduce into the RIIO-ED3 period.

We recognise that we provide a valued public service for our customers, therefore, it is important to us our customers benefit from any efficiencies gained from innovation in previous price controls. We have embedded £87m of efficiency into our business plans following a comprehensive review of innovation opportunities from across our sector.

We have also challenged our costs through a further stretch of £66m of embedded efficiency savings, with an additional ongoing efficiency target of 0.5% per annum, a cumulative reduction of £48m.

Board Sign-Off Statements

The board have reviewed the overall RIIO-ED2 assurance framework and are satisfied that this approach ensures that the submission is accurate, well-justified and compliant with regulatory requirements. The established risk-based assurance framework, which deploys additional assurance activities based on risk scores, ensures that all areas of the submission have been subject to rigorous challenge from independent internal and external experts. This framework also ensures strict adherence to Ofgem's Data Assurance Guidance.

The board have reviewed the approach to developing expenditure plans and are satisfied that the costs in the business plan are efficient and minimise the impact on consumer bills. The structured and iterative approach taken to the development and benchmarking of expenditure plans means that the level of efficiency embedded in the business plan has been continuously challenged throughout the development process. The benchmarking approach and assessment of unit costs has been assured by independent external specialists – giving the board confidence that SP Energy Networks' costs are considered efficient against their benchmarks.

The board is confident that we have submitted an ambitious business plan that will play a critical role in facilitating the UK's journey to Net Zero, and will maintain a safe, reliable and secure electricity supply for our customers. This is underpinned by our ambitious set of business plan commitments based on customer and stakeholder engagement, to enable us to *"work with the communities we serve to enable a just transition to our Net Zero future"*. SP Energy Networks will undertake an ambitious programme of work to meet these business plan commitments, pushing the network beyond what it was originally designed for whilst continuing to ensure the safe, reliable and efficient operation of the distribution network and wider system. The board is confident in the robustness of the investment decisions given the high level of scrutiny applied by both independent internal, and external specialists in the assessment of needs cases, expenditure and detailed technical appraisals of 100% of Load and Non-load related activity.

The business plan has been co-created with our consumers, network users and stakeholders. SP Energy Networks have engaged directly with more than 19,000 customers and stakeholders in their biggest ever engagement exercise to build the RIIO-ED2 plan, allowing us to best understand the current and future needs of our customers and stakeholders, and to make sure the services we develop deliver maximum benefit for them. We also know the plan has benefitted from the constructive challenge and feedback provided by the independent Customer Engagement Group, chaired by John Howard, and by the RIIO-2 Challenge Group, chaired by Roger Witcomb.

The business plan is deliverable. We have a strong track record of delivering on our commitments as a business. Extensive preparatory work is being carried out by SP Energy Networks ahead of RIIO-ED2 to ensure that the ambitious business plan commitments can be delivered – through digitalisation, sustainable supply chain management, and recruitment and development of local skills and talent. Business Transformation plans are also in progress to ensure SP Energy Networks is ready to deliver the commitments. This provides the board with confidence that the plan can be delivered with the timescales, budget and specifications stated – ultimately enabling our Net Zero ambitions.

Financeability Statement

As required by Ofgem's Business Plan guidance, we are submitting a business plan which incorporates Ofgem's working assumptions for the cost of capital and addresses financeability on the basis of Ofgem's key assumptions. However, we disagree with a number of aspects of Ofgem's approach to the assessment of the cost of capital for RIIO-ED2.

For the board, a robust plan is one that makes sure the expected overall credit rating for a notional average electricity distribution business will be solidly within the A to Baa (Moody's) range of credit rating.

Our financeability criteria is fully consistent with the credit quality underpinning the allowed cost of debt index, which benchmarks Utility A and Baa sterling bonds. This is consistent with our licence obligation to maintain an investment grade credit rating. We have taken into account the full range of credit rating factors, not just credit metrics. This allows for scores for the individual sub factors to be outside the wider investment grade range of A1 to Baa3 (A to BB range in S&P ratings). In our assessment we have used the last published qualitative factors for our companies which have a weighting of 50%. The remaining factors that influence the rating score are the five key credit metrics in Moody's methodology.

We have worked with NERA to develop a financeability risk model to test if the proposed financing package is robust. To do this, our model uses the Monte Carlo method to simulate the individual and aggregate credit metrics over the full range of plausible outcomes. The model does this for every individual external risk we have identified.

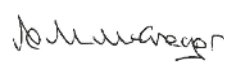
Our plan results in an investment grade credit rating which is consistent with the range that underpins Ofgem's Cost of Debt index. We have demonstrated via risk assessment that our plan, and in particular a notional gearing of 60%, should ensure our business is sufficiently and securely funded and that the normal operation of RIIO-ED2 is unlikely to lead to financial distress when coupled with adverse shocks from external risks. Additional future analysis of financeability will be required after the incentive package is agreed.



Sara Elena León Muñoz,
Chair,
Non-Executive



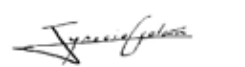
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