

nationalgridESO

**ESO RIIO-2 Business Plan  
Board assurance statement**

9 December 2019

## ESO Board Assurance Statement

### Introduction

The ESO Board recognises its collective responsibility to oversee the ESO as it evolves and engages in the transformation of the energy market.

We understand the ESO's duty to meet the current and future needs of the energy industry and its wider stakeholders, and its role in the achievement of net zero emissions by 2050, along with the continued provision of a reliable energy supply at an efficient cost to consumers.

We want to ensure that the ESO continues to deliver an excellent service to its customers and stakeholders, building a trusted relationship with industry, and earning a fair rate of return that incentivises strong performance on behalf of consumers.

As the company's Board of Directors, we take collective responsibility for assuring the quality (including accuracy and efficiency), ambition, and financeability of the ESO RIIO-2 business plan. We note that the internal ESO RIIO-2 Decision Board has provided additional assurance over the stakeholder engagement and strategic direction that underpin the plan.

### 1. Plan accuracy: data assurance and governance

The ESO Board has reviewed the business plan and the controls and governance that the ESO has in place. We are satisfied that the business plan has been through governance and stakeholder scrutiny to ensure it is of high quality.

The assurance report sets out how the data models, supporting annexes, and data tables have been scrutinised to ensure their integrity and ability to produce a repeatable, reliable output. The data has undergone three levels of review to ensure that the opportunity for error is minimal. Each data owner has reviewed and signed off the elements that they are responsible for, and a supporting risk assessment has captured and mitigated further opportunities for error.

The development of the ESO's business plan has undergone a rigorous governance process. The proposals that were initially developed from within the business align to the ESO's mission and 2030 vision. They have been tested through internal governance processes, the ESO RIIO-2 Stakeholder group and numerous meetings with industry stakeholders. The ESO has adapted and improved its proposals using this feedback.

In this context, the Board provides the following assurance statement:

**The Board has challenged and satisfied itself that the overall strategy for data assurance and governance has delivered a business plan of high quality and accuracy.**

### 2. Plan efficiency: robust and efficient expenditure forecasts

The ESO Board has reviewed the expenditure forecasts created for the ESO RIIO-2 business plan, and the supporting justification, and is satisfied that the cost profile is efficient.

All new and transformational activities (both opex and capex) have been subject to a cost-benefit analysis which has calculated a net consumer benefit of £2 billion. External, cross-sector benchmarking has been used to assess the ongoing and proposed transformational IT costs which are within the comparator range. Shared business support costs have been benchmarked and found to be efficient. The business plan has also embedded £7 million of efficiency savings into direct opex costs, and will apply a 1 per cent efficiency stretch target to these costs in RIIO-2.

Innovation is woven throughout the business plan proposals. The business plan has highlighted where, in RIIO-1, innovation has contributed to the proposed activities and costs, and where it is expected to play a role in RIIO-2. The benefits of these innovation activities will be tracked to highlight reductions in consumer costs, environmental impact and enhanced quality of service.

In this context, the Board provides the following assurance statement:

**The Board has challenged and satisfied itself that the expenditure forecasts included in the company's Business Plan are robust and efficient.**

### 3. Plan ambition: stakeholder-endorsed, ambitious proposals that will deliver significant benefits to consumers

The ESO Board believes the RIIO-2 business plan to be ambitious. This ambition includes the commitment made to facilitate net zero emissions by 2050 through market and system reforms, and the proposed investments to control room systems to be able to operate a zero carbon system by 2025.

The business plan has identified major benefits for consumers and the energy industry. The proposals to promote zero carbon operability could deliver £466 million consumer benefit. Transforming network planning to increase competition could deliver £663 million benefits. Overall, a net present value of £2 billion benefits will be delivered, reducing consumer bills by around £3.

During the creation of the RIIO-2 proposals, stakeholders were engaged through multiple channels. A detailed account of the feedback received, and how it has been acted on, is in the Stakeholder Report that accompanies the business plan. We are satisfied that the plan reflects the ambition that stakeholders have for the ESO, and that stakeholders' feedback has been used to shape and improve the business plan proposals and ensure that the plan is aligned with the needs of consumers and the industry.

In this context, the Board provides the following assurance statement:

**The Board has challenged and satisfied itself that the company's Business Plan is ambitious.**

### 4. Plan financeability: a business plan that is financeable for both the notional and actual company using the proposed financial framework for the ESO

The ESO Board has reviewed and challenged the analysis of the financial arrangements that underpin the business plan. We recognise that in order to be financeable and able to be ambitious, proactive, and agile in driving the £2 billion consumer benefits set out in this plan, the ESO needs to be able to maintain an investment grade credit rating, operate on a standalone basis, and cover the costs of its own financing. It must also provide a fair return to investors for the services it delivers and the risks it takes on behalf of industry and consumers.

In this context, the Board provides the following assurance statement:

**For the purpose of this statement, we define financeable and financeability as applying to the baseline totex forecasts for the five-year RIIO-2 period in our 9 December business plan submission only, and meaning:**

- **Generating sufficient cash to maintain a Baa1 credit rating on average over the RIIO-2 price control period based on the March 2017 Moody's Grid Regulated Electricity and Gas Utilities Rating Methodology and recent Moody's rating of the company; and**
- **Complying with the requirement in the Company's licence to use all reasonable endeavours to maintain an investment grade issuer credit rating based on the actual capital structure of the Company.**

**In giving this statement, the Board does not provide assurance that the investor offering represents an adequate equity investor proposition, or that financeability (as defined above) of the Company can continue to be achieved beyond the RIIO-2 price control period using the working assumptions set out by Ofgem. In providing this assurance statement the Board is not agreeing to the financial framework and the working assumptions proposed by Ofgem, and this statement should not be construed as doing so. The Board further notes that being financeable (as defined above) is not sufficient to enable the culture of ambition, innovation and proactivity that stakeholders want.**

**On this basis, the Board provides assurance that, in its opinion, the licensee is debt financeable on both a notional and actual capital structure basis based on Ofgem's financial framework and its working assumptions. This statement is based on the prevailing market conditions at November 2019 and internal modelling of credit metrics, which has not been tested with rating agencies.**

**An adequate equity proposition to enable an ambitious, proactive, agile and efficient business requires the provision of additional remuneration, not only to compensate the risks not currently remunerated, but also to provide a level of margin comparable to similar services provided in relevant sectors. While this is allowed within the Ofgem framework, its current working assumption is zero.**

**The ESO is an asset-light business with high operational gearing and an ambitious business plan. There is a significant risk that the current financial framework encourages risk-averse behaviours rather than the ambitious objectives and innovation desired by the various stakeholders of the ESO. Without the inclusion of additional remuneration, Ofgem's working assumptions do not provide an adequate equity investor proposition, or encourage the behaviours stakeholders want from the ESO. If additional equity cannot be attracted there is likely to be a deteriorating trend in financeability, with potential consequences for delivery of the business plan objectives. Using these current working assumptions:**

- **Investors receive minimal return for two of the three key services provided by the ESO (the industry revenue management role and markets and industry role).**
- **The notional company requirement for equity injection exceeds the dividend returns provided.**
- **The actual company is loss-making before the inclusion of RIIO-1 timing balances.**

**Signed**



Fintan Slye – Chair of NGESO board



Kayte O'Neill – Strategy and Regulation  
Director



Duncan Burt – Operations Director



Paul Plummer - Independent Non Executive  
Director



Gillian Merron – Independent Non Executive  
Director



Claire Tuckman – Finance Director



Hannah Nixon - Independent Non Executive  
Director

**27 November 2019**

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