

Managing Director Report 2023

Special Licence condition 9.16

As part of the Special Condition 9.16 of SP Transmission's licence, it is required to appoint a Managing Director of Transmission (MDT) to be responsible for the conduct of the Transmission Business. SP Transmission plc (SPT) is required to arrange for the MDT to be provided with the services of persons, premises, systems, and other resources as may be reasonably required by the MDT for the efficient and effective management and operation of the transmission business in accordance with SPT's statutory duties and licence obligations.

This report has been prepared as soon as reasonably possible after the calendar year 2023, the timing of this report follows the completion of the 2023-24 financial and regulatory year end allowing all the assurance and governance to be attained.

Overview

Through the Energy landscape shifting towards sustainability, we have continued to see unprecedented levels of connection applications being made to connect generation and demand projects to our transmission network. With over 700GW of contracted capacity currently in the GB-wide transmission and distribution queues, there continues to be a pressing case for significant reforms to the existing connections process, at the earliest opportunity. We therefore continue to be fully engaged in the ESO and Ofgem-led Connections Reform work. In order to support this important reform work, SPT is working closely with Ofgem, Government, the ESO, other network operators and industry, ensuring full SPT representation on the key working groups which are considering and driving forward these necessary industry changes. These key working groups include the Connections Delivery Board, the Connections Process Advisory Group, the ENA's Strategic Connections Group and the connections reform code working groups CMP 434 and CMP 435.

We also continue to work closely with UK and devolved governments and regulators to address additional challenges that are ancillary but closely connected to this challenge, specifically planning and consenting challenges, together with supply chain availability and sustainability.

We have also reviewed our contracting and delivery strategy in light of the limitations that we see in the supply chain. In response to this, we commenced an extensive tendering exercise to create a framework for our future overhead line and substation works with an estimated value of £5.4bn. This tender was launched in January 2024 and we expect to award by the end of 2024 with the first works on the framework commencing in early 2025. This framework will provide long term commitments to the supply chain to cover T2 and T3 works, as well as ASTI and other emerging projects over the next 5+ years.

This long-term commitment is essential for the supply chain to have visibility and confidence in the pipeline of work to increase resourcing and invest in the equipment required to deliver these works. We are undertaking a competitive process to select the framework partners to ensure value for money but also endeavouring to introduce

new entrants to the market through this process, in particular from service partners who are not UK based and have skilled resources in Europe.

As our investment plans increase, we are also increasing the number of staff in SP Transmission and the associated support functions. Since the start of RIIO-T2, staff numbers have increased from 403 to 616 (53%) (excluding associated support functions). The associated business support costs have also increased by a corresponding amount resulting in an overspend against allowance but is considered to be essential to be prepared for the continued growth in T3 and beyond. As a result of the increased headcount, we are in the process of opening a new operational site with significant storage facilities for transmission equipment. This will allow greater storage capacity of operational needs as well as acting as a strategic store for equipment to support project delivery. We are also at an advanced stage of securing an additional office facility in Edinburgh which will double the office capacity available to SPT.

We are continuing to work on our cyber security transformation and in the last regulatory year, achieved attestation of Basic Profile in line with the NIS Regulation duties. We are continuing to work on the delivery and management of risk reduction and continue to achieve our plans outlined in the RIIO T2 2023 re-opener. We have a comprehensive programme of eighteen workstreams in progress and are working towards the attainment of the CAF Enhanced profile by the end of 2025, to manage cyber risks with increased security and control.

Company Strategy

As part of the RIIO-T2 framework, the company has an agreed set of outputs it will deliver, and several incentives aimed at reducing network costs for both current and future customers.

The key strategies for the company to the end of the RIIO-T2 price control period and beyond are outlined in our strategic goals.

- A sustainable, Net Zero future
 - We will take the lead to build a healthier, more accessible energy model – one which leaves the carbon economy behind. We will meet carbon targets, customers' low-carbon ambitions, and make a large, proactive contribution towards Net Zero
- Increase efficiency through constant innovation
 - We will continue to improve our performance through a continual cycle of innovation. With smarter solutions, we can do more with less – deploying new technology, processes, and ways to share data. Innovation will help us deliver uninterrupted supply, faster connections,

and meet the ambitions of consumers, network users and wider stakeholders.

- Adapt our world-class, resilient network
 - This is a critical time for networks. Demand is changing, generation is evolving, and new threats are emerging. We will adapt our world-class network to meet these challenges, including extreme weather, cyber security, and black start events – delivering ever-higher performance for consumers, network users and wider stakeholders
- Keeping network users and consumers at the heart of our decisions
 - We will listen and learn even more from our stakeholders. This will allow us to continue to raise our efforts as we work to improve lives, create jobs, and protect vulnerable consumers. In everything we do, we aim to do more

We have seen progress to date across all areas, and continue to focus on these key areas to achieve our RIIO-T2 objectives successfully.

Network Reliability

A comprehensive outage plan is maintained by the Operational Planning team within the Customer Service Directorate. This plan is reviewed regularly with the investment delivery and operational functions within SPT, and then sanctioned by the System Operator NGENSO. For the 2024 submission this plan contains detailed outage requirements for all of SPT's major projects up to December 2032 in line with the current Holistic Network Design Follow Up Exercise (HND FuE) and Transitional Centralised Strategic Network Plan (tCSNP). System access is becoming increasingly challenging as the System Operator seeks to balance the need for network outages to undertake reinforcement, modernisation and maintenance while ensuring the network remains secure and network operating costs remain acceptable as generation and demand patterns change alongside fluctuations in the global energy markets. The 2023/2024 plan was especially challenging due to energy security concerns across GB in winter and short notice change in generation outages required to secure the Scottish System in summer. Experience has shown that through comprehensive engagement with the System Operator and key stakeholders supported where necessary by escalation to NGENSO's senior management, acceptable amendments can be made to the outage plan to mitigate significant impacts on SPT's ability to undertake its business.

Resources

SPT's Resource Plan for the deliverability of the RIIO-T2 business plan was laid out in our Availability of Resources statement, which was issued in May and certificated in

July 2024. This confirmed the reasonable expectation that SPT would have sufficient resources for the subsequent 12 months.

SPT continued to grow in 2023 to deliver the £5bn investment as part of the ESO's Holistic Network Design (HND) plan, the continued growth of customer connection activities and to enable the delivery of the RIIO-T2 Business Plan. This has resulted in an increase to our headcount, bringing the overall figure for SP Transmission and associated supporting functions to 942 FTE for the regulatory reporting year 23/24. To deliver the HND projects effectively and efficiently, a new Strategic team was created to focus on the identified projects in SPT licence's area required by 2037 which will act as an enabler for Net Zero. In addition, SP Transmission increased the pool of trainees in 2023 for particular skillsets to create a sustainable pipeline of internal resources and this pipeline will further increase in future years to ensure SPT have the correct skills available to meet project timescales. As in previous years, there was access to a number of contingent workers through an established framework agreement which supplemented our staff resource to meet demand.

General risk management strategies are in place to limit the impact of supply issues including multiple suppliers in place for equipment and materials, logistics stocking strategies, SPEN forecasting demand and active contract management of supplier delivery. We are also deploying long term strategic agreements via frameworks for works to be delivered in the Transmission area. This compliments our existing long term frameworks agreements for key works covering our Distribution requirements.

As a result of current economic turbulence within contracts, where fixed pricing is not reported by the supply base, we are agreeing a combination of fixed and variable elements. The variable elements are isolated to cost components that have high volatility and are monitored via official indices such as currency, metals, and energy. This approach ensures we can access the supply base and ensures we pay prices that are fair within the market.

Finance

Adequate finance was available to SPT during the year ending 31 December 2023. In accordance with Licence Condition B7, Directors approved, on 29th July 2024, the Certificate of Availability of Resources that confirmed their reasonable expectation that SPT would have sufficient financial resources and financial facilities for the subsequent 12 months.

For the regulatory year 2023/24, revenue increased by £145m to £459m compared to the prior year of £314m. SPT's operating profit was £286m, an increase of £124m compared to prior year. Net profit was £164m, an increase of £70m compared to prior year. The main driver of the increases year on year are; higher allowed revenues due

to an increase in investment and inflation offset by higher interest costs in line with the wider macro economic environment.

SPT's net capital investment for the year was £346.4m, a 120% increase on prior year consisting of fixed asset additions and transfers from inventories of £359.3m less capital contributions received of £12.9m (2022 £15.7m). This increase in capital investment demonstrates a significant step forward in the delivery of our RIIO-T2 plan. We continue to see changes in the baseline schemes for T2, primarily due to customer connections being deferred and delays in obtaining planning consents.

Of the £359.3m expenditure in the last year, £193.6m is associated with baseline works and £165.6m for incremental projects which are funded through volume driver or re-openers.

For the baseline spend, a number of assumptions were made to inform the plan at the time of submission to Ofgem in December 2019. The energy and political landscape has changed significantly in that time including:

- A rapid growth in connection applications for energy storage, wind generation and other technology. In 2023/24, we issued a total of 352 connection offers, a 60% increase on prior year.
- Lower than forecast levels of investment in the first two years in RIIO-T2 due to the legacy impact of COVID lockdown, completion of T1 schemes which were delayed as a result and supply chain shortages.
- Restrictions on outages and system access by ESO due to generation availability, particularly over winter periods which has resulted in planned works requiring to be re-arranged.
- Periods of high inflation and material cost increases as a result of global demand for electrical products and wage increases. This has had a major impact on the supply chain and the availability of resources and equipment.

Looking Forward

T3 Business Plan

The Scottish and UK Governments have set ambitious decarbonisation targets for Net Zero by 2045 and 2050 respectively and the next decade will be crucial in preparing the grid for the increase in electricity demand resulting from decarbonisation of society and the economy. Our network will be crucial to the solutions needed to meet these targets and prevent runaway climate change. We plan collaboratively and strategically, for the future, to make sure our network plays its crucial role in the most cost-effective way.

The electricity sector is currently operating in the 'RIIO-2' delivery period which for electricity transmission network owners runs from 1 April 2021 to 31 March 2026 (RIIO-T2). The next 'RIIO-3' delivery period for electricity transmission network owners will run from 1 April 2026 to 31 March 2031 (RIIO-T3). Following publication of Ofgem's

Sector Specific Methodology Decision on 18 July 2024, our plan for RIIO-T3 will be developed throughout 2024 with input from our stakeholders and will be published in December 2024.

Our RIIO-T3 Business Plan will set out proposed investment in the transmission network and other initiatives that will be key enablers to achieving government Net Zero ambitions. It will increase the security of supplies of energy, help to protect consumers from the dangers of climate change and will help generate growth, green jobs, investment and community benefits.

Throughout the development of our RIIO-T3 Business Plan, we are engaging extensively to ensure the plan we produce fully recognises the requirements of our stakeholders and commands their support.

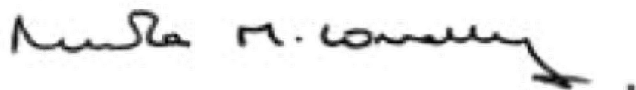
As part of the RIIO-3 Enhanced Engagement Framework, networks must have an Independent Stakeholder Group (ISG) in place to provide scrutiny in development of the RIIO-T3 Business Plan.

We have established an Independent Net Zero Advisory Council (INZAC), which will have a vital part to play in the development of our RIIO-T3 Business Plan, scrutinising both the technical plans as well as ensuring any emerging customer issues are fully considered.

Conclusion

In view of the arrangements and activities described above, and the resources made available, I am satisfied that adequate arrangements have been in place to as far as possible secure compliance with statutory and licence obligations in the year 2024.

Nicola Connelly,



CEO, SP Energy Networks