

Ms Olivia Powis
OFGEM
9 Millbank
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Dear Ms Powis,

Quicker and more efficient distribution connections

Thank you for opening a dialogue on this very important issue for economic growth. This response to OFGEM's open letter is submitted by the New Anglia Local Enterprise Partnership (LEP), a business-led collaboration between the private, public and education sectors across Norfolk and Suffolk. In common with other local enterprise partnerships, New Anglia LEP was established by Government in 2010 to drive growth by identifying activities to support jobs growth, securing funding, and engaging with the business community.

Our partners regularly report to us that the cost and risks of funding new electricity connections (for consumption or generation) is preventing investment coming forward, particularly on sites that are expected to deliver employment growth. New Anglia LEP's Strategic Economic Plan highlights some of the areas where the cost of reinforcing the electricity distribution network is holding back new jobs and homes, these include: Bury St Edmunds, Ipswich, Kings Lynn, Lowestoft, Norwich, Snetterton, Sudbury, Thetford and Wymondham.

Requests for forward funding of the reinforcement costs are frequently submitted to this LEP to consider. Whilst directly related to enabling economic growth, these and other requests for funding are an indication of market failure. It is the frequency of such requests and degree of cost that heightens this LEP's opinion that attention needs to be paid to the effectiveness of the regulated market, to ensure that investment is properly targeted to the areas and projects that need such assistance.

Different roles and risks: developers, consumers and the state.

On paper, Distribution Network Operators (DNOs) are already able to invest in reinforcing the network ahead of the need arising from new connections. OFGEM's 2014 policy document sets out the position clearly.¹ However, the current approach puts the onus on the DNO to justify investment either through the price control framework or on a case-by-case basis. If not justified, the customer requesting the connection must pay for the reinforcement and bear the risk of not getting a return.

¹ OFGEM (2014) *A guide to electricity distribution connections policy*, pages 12-13

The scenarios listed in the open letter raise some fundamental points about how this cost and risk could be apportioned appropriately. The different risk characteristics between developers, landowners, electricity consumers (DUoS) and the state (in its widest sense) do need to be recognised and the scenarios highlight some differences. This response provides examples from Norfolk and Suffolk where, broadly speaking, our understanding of how a potential scenario could apply. However, flexibility is a key element to promote the delivery of economic growth and OFGEM should not be constrained to focusing on the scenarios identified (**Q27**).

All the scenarios highlight the new need for local authorities, developers and DNOs to be work in partnership, whether this is through direct investment for economic growth, to deliver the homes needed in an area, or in supporting DNOs to have evidence of the timing of future new connection requests.

The potential for local authorities and developers to invest in electricity infrastructure could be further enhanced if the financial mechanisms were linked to the regulatory process and if such mechanisms were then backed-up by central government or other form of financial guarantee. The demand for such mechanisms might emerge later as developers and local authorities work more closely with DNOs, but, in considering approaches, OFGEM might consider how its regulatory systems could be better formed to accommodate such approaches.

Scenario 1: DNO funds (via DUoS) cost of anticipatory reinforcement

In this scenario, there would be clear market signals that the investment from electricity customers would be taken up within the expected time. The scenario would also be appropriate where the need for reinforcement arises from meeting existing customer needs as well as new connections. This would suggest an area-wide plan, such as local planning documents, or combined investment plans being used as a basis.

The example provided of the £100million in reinforcement works across London, a strategic reinforcement schemes such as new substations, is at odds with the statement made by UK Power Networks that Ofgem “confirmed that the current regulatory framework does not support ahead of need investment in infrastructure”.² However, such investment appears to be justified “if in time this leads to a lower overall cost of reinforcement”.³ This scenario would, therefore, depend on the following critical elements: a programme of investment, certainty of the demand, a specific period of time and a resultant lower cost (**Q1**).

The evidence needed for these critical elements to be justified is a significant barrier and this scenario works with programmes covering several sites (**Q2**). However, the evidence to justify following this scenario might emerge for some areas – particularly larger urban areas - as a result of a greater focus and joint working between DNOs, local authorities and delivery partners such as local enterprise partnerships. This might also be an appropriate route for major regeneration projects where there is clear commitment to delivery. The design of any forthcoming systems should not exclude this scenario being selected. Allowing this scenario to be followed at any time would give a powerful incentive to local authorities and developers to work together to provide DNOs with greater certainty.

² UK Power Networks (2014) *London Power Networks Business plan (2015 to 2023) Executive summary*, page 23.

³ OFGEM (2015) *Open Letter: Quicker and more efficient distribution connections*, page 5

Scenario 2: DNO funds (via DUoS) cost of anticipatory reinforcement when initial connection takes place (to be reimbursed by subsequent connection customers)

On the surface, this scenario, and the concept of OFGEM authorising investment ahead of need through the Regulatory Asset Value Buyback Model (RAV), is the preferred approach. However, as set out, this scenario still requires a high degree of certainty and evidence that early investment reduces overall reinforcement costs for OFGEM to agree (Q3). The most significant difference is the focus on one particular development area or site – being developed by the first-comer and, therefore, with a greater element of risk. This is when the RAV model fits with closer alignment with infrastructure, planning and investment regimes (Q3).

The concept of a “premium” on connections does appear to have some scope to mitigate the residual risk to customers (DUoS) of funding stranded assets. Whilst New Anglia LEP doesn’t have a view on how this should be calculated (Q6), OFGEM should not exclude other financial models that could be designed to provide the equivalent of this premium. For example, a financial model backed by central or local government could apply to priority areas such as assisted areas and enterprise zones.

This scenario would help to create a greater degree of certainty over delivery and the cost of new connections. This, and other factors, suggests that the scenario would be a very suitable approach to fund the reinforcement works for regeneration and to service brownfield sites. Such areas tend to be part of an existing urban area and, therefore, a customer base that would also require the further capacity (reducing overall reinforcement costs).

This scenario may be particularly relevant to large scale projects being backed by the Government’s Homes and Communities Agency (HCA). Indeed, there is also an argument that investment in affordable housing (whether individual sites or through programmes) committed by local authorities and housing associations provides some of the greater certainty required for this scenario. The delivery of such investment is more certain because local and national investment programmes need to be followed and because of the higher degree of financial regulation of local authorities and housing associations.

In terms of examples where this type of arrangement could have helped (Q4), there are two from Suffolk alone: the [former British Sugar](#) site to the west of Ipswich, and [Ellough Airfield](#) near Beccles. Both have very strong commitment from local authorities. However, the cost of supplying the new capacity (£6.3million -15MVA- for the sugar beet site and £8million for Ellough) is deterring investment. The British Sugar site has a local plan allocation for employment and is now owned by Ipswich Borough Council. Ellough Airfield is part of the Great Yarmouth and Lowestoft Enterprise Zone and has a Local Development Order in place, which permits development without the need for planning permission.

The concept of requiring subsequent connection customers to be only able to connect to the new infrastructure is understandable (Q5) but additional capacity may also be gained elsewhere in the local network, through greater resilience for example. Working towards an area-wide approach, using local plans and delivery programmes as tools, could provide an opportunity to look at who else might benefit and also pay.

Scenario 3: Connection customer funds cost of anticipatory reinforcement when initial connection takes place (to be reimbursed by subsequent connection customers)

This scenario, and the Development Company (DevCo) approach, has the most potential to be applied widely, particularly in higher-value areas and for energy generation schemes. The only other alternative at present is to engage an Independent Distribution Network Operator (IDNO) but often further upstream reinforcement is also necessary.

The DevCo model is only likely to be successful if the current time period for second-comer payments are extended beyond the current five-year period (this also applies to scenario 2). This is a very short time period for the development process. The types and scale of development where reinforcement work is required often takes 10-15 years to be completed (**Q14**). This is especially true of commercial and industrial development. There would also need to be greater certainty that the capacity would be available but the precise terms for the DNO to offer or withhold a connection would need to be carefully framed to avoid being anti-competitive (**Q10**).

As noted above, there are several cases where homes and jobs are not being delivered (**Q11**). Bury St Edmunds has a robust local plan to deliver over 4,000 new homes on five strategic sites by 2031. The area to the North East (around 1700 homes, new primary and secondary schools and 68 hectares of land for employment) is constrained by the lack of supply, which also impacts on the wider area.

Around Snetterton, approximately 4,000 homes and 2,000 jobs depend on a £6m investment in reinforcement works. Multiple connections would be forthcoming and the potential for greater energy efficiency and on-site electricity generation has been explored. Major expansion of Thetford is planned to include 5,000 houses and strategic employment sites. Delivery of this package of growth is reliant on a £6m cable upgrade, which is a major constraint to bringing forward permitted employment development at Thetford Enterprise Park.

A further example is the development of around 1,000 homes and 20ha of land for employment at Sudbury. In order for this development to be delivered, approximately £10m of investment is required including a new supply cable to a 132kV substation some 10km away. This new supply could provide further capacity in the longer-term but the return would not be paid to the first comer. The IDNO option is being considered for this specific site.

Clearly further work is required to work out how the DevCo approach could be facilitated by the regulated market and what level of additional premium on connection charges would ensure such models are viable. The additional premium may, for example, be more effective in higher values areas (**Q13**).

Summary

There is a clear role for local authorities and other partners to collaborate on single and multiple sites. This goes beyond the preparing local plans and could well include direct investment by local authorities. This is an opportune time to work through such arrangements as local authorities are focusing more attention on delivering developments: for an income stream (through direct investment or from financial incentives), to increase their housing stock, and to justify local planning policies on residential and industrial development (**Q29**).

Local authorities in New Anglia would welcome the consideration of how local plans, including analysis of delivery, could be used to provide more certainty to DNOs. This could help determine the degree to which the reinforcement works fit within the scenarios identified (**Q27**).

Central to the whole case for change is that the current system promotes incremental growth within a given area because assumptions are based on trends and an aversion to risk. These factors militate against larger-scale developments that might be more sustainable and supportive of higher levels of economic growth. This is particularly relevant as the economy grows more strongly following a recession.

If you have any questions on the comments and examples above, or would like to discuss how New Anglia LEP could help OFGEM further, please contact James Cutting, Planning Strategy Manager at Suffolk County Council, on 01473 264803 or e-mail james.cutting@suffolk.gov.uk.

Yours sincerely,



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