



Consumers and their representatives, distribution network operators (DNOs), independent distribution network operators (IDNOs), potential project collaborators, owners and operators of distributed energy systems, generators, electricity suppliers and any other interested parties.

Promoting choice and value for all gas and electricity customers

Direct Dial: 020 7901 7209
Email: rachel.fletcher@ofgem.gov.uk

Date: 24 February 2010

Dear Colleague,

Low Carbon Networks (LCN) Fund:

Notice under Charge Restriction Condition (CRC) 13 of the Electricity Distribution Licence with respect to the LCN Fund Governance Document;

and

Consultation in relation to other aspects of the LCN Fund

This letter constitutes formal notice under CRC 13 of the Electricity Distribution Licence of Ofgem's intent to issue the LCN Fund Governance Document for purposes connected with the regulation, governance and administration of the Low Carbon Networks (LCN) Fund. A draft of the document is appended to this letter. Representations or objections to this Notice should be made to Ofgem on or before Wednesday 24 March 2010. Representations or objections that are received and not withdrawn will be considered by Ofgem prior to the document coming into effect on 1 April 2010¹.

The Governance Document at this time only covers the arrangements relating to the First Tier of the Fund – £80m funding available directly to DNOs over the DPCR5 period (April 2010 to March 2015) for relatively small scale projects that meet the criteria set out in the document. Later this year we will update the document to cover the arrangements for the Second Tier of the Fund. This Tier comprises £320m to fund large flagship projects over the period and will be awarded to DNOs through an annual competition. This letter also seeks views on the arrangements for the Second Tier and invites interested parties to attend a workshop on the Second Tier and wider aspects of the LCN Fund.

In the Final Proposals of the electricity distribution price control review (DPCR5), we proposed the LCN Fund to encourage the Distribution Network Operators (DNOs) to use the DPCR5 period (1 April 2010 to 31 March 2015) to try out new technology, operating and commercial arrangements. The objective of these trials and demonstration projects is to help all DNOs understand how they can provide security of supply at value for money as Great Britain (GB) moves to a low carbon economy, and what role they could play in facilitating the low carbon and energy saving initiatives that are underway to tackle climate change.

¹ The document will come into effect on 1 April 2010 subject to CRC 13, which will come into effect following a direction given by the Authority to all Distribution Services Providers ("DSPs"). The direction will be given once it has been confirmed that the LCN Fund has been granted State Aid clearance by the European Commission.

The LCN Fund consists of two tiers of funding as noted above. There is an annual competition for Second Tier funding and the DNOs will compete against each other for an allocation of the funds. The annual process will start with DNOs putting forward outline project proposals for Ofgem to assess whether they meet the eligibility criteria. This will be followed by the annual call for, and submission of, full proposals. A Discretionary Funding Mechanism enables Ofgem to reward up to £100m over the five year period for successful delivery and to projects that bring particular value in helping the DNOs understand what investment, commercial arrangements and operating strategies they should be putting in place to provide security of supply at value for money for future network users, while doing all they can to tackle climate change.

Responding to this Notice

The attached document represents the draft first version of the LCN Governance Fund Document, and sets out the requirements a DNO must comply with to be eligible under the First Tier Funding Mechanism. Those reviewing the attached draft document should note that the First Tier involves relatively small amounts of money and the intention is to set criteria so that Ofgem need to have relatively little direct involvement in approving First Tier projects. We have set relatively tight criteria for the First Tier so that DNOs can self certify compliance in most circumstances and to minimise the need for Ofgem involvement.

In contrast, the annual competition process for the Second Tier will involve detailed scrutiny of projects by an Expert Panel ahead of Ofgem deciding to award and release funding for projects. Our current thinking is that it may be appropriate for us to set more flexible criteria for Second Tier eligibility than we propose for the First Tier. We are keen in particular, to ensure that the arrangements do not prevent DNOs from testing highly innovative technology, operating or commercial arrangements.

Representations or objections to this Notice should be made to anna.rossington@ofgem.gov.uk on or before Wednesday 24 March 2010.

Way forward, consultation and workshop

The LCN Fund Governance Document covers all aspects of the governance of the LCN Fund, including regulation, governance and administration. To give interested parties early notice of the governance arrangements and to allow work to commence as quickly as possible on First Tier activities we have developed the arrangements for the First Tier ahead of other aspects of the LCN Fund. We will develop and publish further versions of the Governance Document to cover the remaining mechanisms in the LCN Fund as follows:

- in early June 2010 we will include the arrangements for the Second Tier Initial Screening Process; and
- in July 2010 we will include the arrangements for the Second Tier and Discretionary Funding Mechanisms.

We will provide formal notice ahead of publishing each of these revised versions of the Governance Document. These publication dates are designed to fit with this year's timetable for the LCN Fund process which is as follows:

- the deadline for submission of summary Second Tier proposals for initial screening is late June 2010;
- the deadline for submission of full Second Tier proposals is early September 2010; and
- winning projects will be announced in November 2010.

We are beginning to develop the governance arrangements for the Second Tier Funding Mechanism and for the Discretionary Reward Mechanism. We will continue to work closely

with DNO representatives in this process, but we are also keen to hear the thoughts and comments of others (especially potential project partners) on the arrangements for Second Tier Funding. In particular, we are interested to get views on:

1. The criteria we might use in screening projects for inclusion in the annual competition for Second Tier funding;
2. The evaluation criteria we might use in assessing which project proposals receive Second Tier Funding;
3. The arrangements we should put in place regarding the treatment of Intellectual Property Rights (IPRs);
4. The criteria we might use to allocate the Discretionary Reward.

We welcome **written responses** from interested parties regarding the governance arrangements that should apply for the Second Tier, and in particular relating to the questions above. Responses should be sent to anna.rossington@ofgem.gov.uk **on or before Monday 12 April 2010**.

We are planning to organise a **half day workshop** in late March to discuss the governance of the Second Tier and wider aspects of the LCN Fund. Attendance will be limited, if you would like to register your interest in attending then please email anna.rossington@ofgem.gov.uk by **5pm on Friday 5 March 2010**.

If you have any queries on the contents of this letter, please contact Anna Rossington, on anna.rossington@ofgem.gov.uk, direct dial: 020 7901 7401.

Yours faithfully,



Rachel Fletcher
Partner, Distribution