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Anna Rossington  
Low Carbon Network Fund Consultation  
Ofgem  
9 Millbank  
London  
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**Ref: Low Carbon Network Fund Consultation**

Dear Anna,

Smarter Grid Solutions (SGS) welcomes the opportunity to respond to the Ofgem consultation in relation to the governance and discretionary award elements of the Low Carbon Network Fund. SGS was enthused by the industry participation in the recent workshop that Ofgem facilitated on 30<sup>th</sup> March 2010, where a number of important topics were discussed.

SGS provides Active Network Management products and services to assist network operators to facilitate low carbon technologies and manage real-time network constraints. SGS support the intent of the Low Carbon Network Fund to stimulate innovation within the electricity industry and networks businesses and SGS stand ready to support the network operators to trial at scale new technologies that could represent significant steps forward for the UK electricity sector.

SGS expect that the competitive nature of the LCNF and corresponding access to the discretionary reward will provide strong motivation for the distribution network operators to develop new learning in technical and commercial practices. SGS believe that the competitive element is an essential driver for change, in a similar way to traditional competitive markets where the adoption of new technical and commercial innovations is commonly seen as a vital strategy to stay ahead of the competition. Stimulating competition in a regulated monopolistic market will hopefully engender the competitive mindset within the distribution network operators. However, SGS also recognise the need to share experience and learning. As such a balance must be found which avoids unnecessary duplication but also provide the opportunity to roll-out the correct technologies at scale for competitive benefit. It is in this context that SGS respond to the specific questions raised in your consultation:

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

Addressing each of these areas of consultation in turn:

***The criteria for use in screening projects for inclusion in the annual competition for Second Tier Funding***

At the recent workshop Ofgem described the following:

- The Initial Screening Process is to be a Pass/Fail process to decide if the project concept fits with the high level criteria provided
- The pre-qualification questionnaire will be short form
- Some details of the proposals will be published at the Initial Screening phase
- The expert panel will provide recommendations to Ofgem who will then make the Pass/Fail decision
- The expert panel may provide recommendations for projects to merge or change scope

Based on the information that subsequently emerged at the workshop, SGS make the following observations:

- The process for access to the Second Tier funds and hence discretionary reward should facilitate 'competition';
  - Only very high level details of projects should be published which do not reveal the important differentiating concepts proposed until successful in securing Second Tier funding or abandonment of the bid by the network operator
  - If the network operator is unsuccessful at the Second Tier review they may wish to revise the submitted bid and re-submit in a future call
- Making the pre-qualification process too simplistic may not provide sufficient information to properly assess whether a project meets Ofgem objectives
- The criteria should also include an indication of the anticipated project expenditure in order to have early sight of potential over or under subscription for project funds
- Where the expert panel performs the role of merging projects or changing the scope of projects this may reduce the impact of the competitive market being stimulated
- In some cases the merging of projects may be acceptable to allow the best parts of bids which on the whole might fail to have the ideas captured for demonstration elsewhere; however this may cause significant problems when deciding in which license area the trial should be undertaken and also how the balance of any discretionary reward would be allocated across license holders

Based on these observations, SGS recommend:

- Ofgem should try to retain wherever possible the competitive element of the Second Tier funding and avoid merging projects or altering the scope of projects
- Only very basic details, agreed with the applicant, should be published at the Initial Screening stage

***The evaluation criteria Ofgem might use in assessing which project proposals receive Second Tier funding***

At the recent workshop, Ofgem described the following:

- Rather than a pass or fail test the second evaluation phase will assess the degree to which the project proposal fits with the high level criteria provided
- Potential difficulties may arise if a scoring process is used as the only evaluation tool
- Reliance will be placed on the advice of the expert panel rather than specific criteria
- The expert panel will provide recommendations to Ofgem but the final decision on whether to fund projects will rest with Ofgem
- Projects will not only be assessed on direct network benefits but also on wider societal benefits and learning

Based on the information that subsequently emerged at the workshop, SGS make the following observations:

- Without a clear methodology for assessing projects the process for allocating Second Tier funding may lack transparency
- It remains unclear how projects may be compared against each other to assess relative merits
- Most bids will have engaged with potential partners such as local authority and other government initiatives and the failure of any bid could have a negative publicity effect if not ultimately funded

Based on these observations, SGS recommend:

- A clear methodology and assessment process should be implemented; this should be published either widely or on a bi-lateral basis with the application to demonstrate how projects have been assessed objectively against one another
- The initial screening process should be relatively stringent to ensure that projects progressing to Second Tier Evaluation have a reasonable chance of winning funding to avoid negative publicity from engaged partners if a full bid is unsuccessful

***The arrangements that Ofgem should put in place regarding the treatment of Intellectual Property Rights (IPRs)***

At the recent workshop, Ofgem described the following:

- Intellectual Property Rights will most likely not represent a problem but Ofgem requires to demonstrate that they are adequately protecting the rights of the consumer, considering the use of taxpayer funds
- The approach to Intellectual Property Rights already in use through the Innovation Funding Incentive funding has not raised any issues to date
- No change is proposed to the treatment of Intellectual Property Rights for the Innovation Funding Incentive
- Each bid made to the second stage assessment should clearly state how the distribution network operator will handle Intellectual Property Rights within the project

Based on the information that subsequently emerged at the workshop, SGS make the following observations:

- The Second Tier funding will trial proven technologies at the higher range of the Technology Readiness Level framework and therefore the technologies are already likely to have all substantial Intellectual Property protected by the relevant vendors
- The approach to Intellectual Property Rights for the Innovation Funding Incentive is practical and recognises that distribution network operators are not in a position to protect and exploit intellectual property
- Intellectual Property Rights may be generated in combining systems from multiple vendors, integrating with existing systems and practices within the network operator and new commercial contracts and legal agreements
- Intellectual Property Rights may be generated from other as yet unknown areas and Ofgem should consider how the consumer should be most appropriately protected from the slight risk that such Intellectual Property Rights may have value outwith the trial being funded
- Standard commercial agreements commonly cover both foreground and background Intellectual Property Rights

Based on these observations, SGS recommend:

- The same approach to Intellectual Property Rights as is currently adopted for the Innovation Funding Incentive should be adopted for the Second Tier
- The Second Tier assessment should consider the Technology Readiness Levels of the technologies to be trialled to reduce the risk of highly valuable Intellectual Property Rights being generated
- Standard commercial agreements such as Collaboration Agreements should be in place between project partners which define foreground and background intellectual property and how each class of rights will be used during and after the project and should be submitted with the full bid as part of the second stage evaluation process

***The criteria that Ofgem might use to allocate the discretionary award***

At the recent workshop, Ofgem described the following:

- It is unclear whether the Discretionary Reward should be allocated in a few large payments or a larger number of smaller payments
- It is unclear what the balance of risk versus reward should be and how this can be assessed
- It is unclear whether projects which ‘fail’, even if they deliver some learning, should be rewarded
- For access to the discretionary reward, projects should meet the success criteria defined in the project bid and be linked to the extent of learning evident from the project outputs
- It is unclear whether the discretionary reward should be applied to Second Tier projects only or whether First Tier projects should also be eligible

Based on the information that subsequently emerged at the workshop, SGS make the following observations:

- Using ‘learning’ as the most important metric for allocating discretionary funding will be difficult to achieve objectively and to substantiate with evidence
- The discretionary reward is a key driver for the competitive element of the funding and provides the opportunity for network operators to gain competitive advantage through participating proactively with the low carbon network fund
- It is unclear what is actually meant by a project which has ‘failed’; this may relate to network performance, failure to deliver the success criteria in the original bid or failure to deliver on time and within budget
- Rewarding a project which ‘fails’ due to reduced network performance, for example resulting in a reduction in the quality or reliability of supply in an area of trial, may be publicly and politically difficult to defend, even if learning is generated
- The earliest projects are likely to be the most risky and hence should attract more reward; projects following behind will be de-risked to some extent by the learning already disseminated from the earliest projects and may result in a reduced allocation of discretionary reward
- It is not clear whether the discretionary award will be allocated each year within the DPCR5 period or as lump sums at the end;
- First Tier funding is not competitive and therefore may not drive the same level of innovation or change as Second Tier projects; First Tier projects will not merit a pro-rata allocation of discretionary reward

Based on these observations, SGS recommend:

- Project ‘success’ should be measured based on the delivery of the project targets (carbon, financial, network, wider UK electricity system, business change and industry learning) as set out in the bid
- The emphasis for the discretionary reward should be on Second Tier projects
- Projects which commence earliest, and provide learning for later projects to benefit from, should be rewarded greatest
- Ofgem should clarify when the discretionary reward will be allocated and split across the DPCR5 years and potentially beyond

- Projects that demonstrate the most ambitious concepts and targets should be rewarded most, if successful, as they represent the most risk

In summary we believe that the competitive nature of the Low Carbon Network Fund should stimulate innovation and change. An important aspect of this is the discretionary reward as this provides the business case for network operators to participate with a view to gaining competitive and financial advantage.

We feel that although the bid applications are for trial projects the Initial Screening and Second Tier Assessment stages should ensure a clear link to the future business plan of the network operator, including how the project links to the next distribution price control review. Without this there is a risk that projects will be run as projects outside of normal business processes simply to access specific funding and potentially the discretionary reward, rather than being an integral part of the business in the future.

SGS believe that engaging with network operators, stakeholders and vendors through the workshop process has helped bring out some of the issues that will be relevant to the operation of the LCNF. SGS look forward to receiving further guidance from Ofgem on these issues in due course.

Best regards,



Alan Gooding  
**Managing Director**