

Anna Rossington
Ofgem
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Your ref

Our Ref

Date 16 July 2010

Contact / Extension

Jeremy Blackford
0151 609 2346

Dear Anna

Low Carbon Networks (LCN) Fund – notice under Condition CRC 13 of the Electricity Distribution Licence

I am writing on behalf of SP Distribution and SP Manweb in response to draft version 3 of the LCN Fund Governance Document issued on 18 June 2010.

We acknowledge the significant amount of work involved in developing the current version of the Governance document. We think that it will need to be reviewed over time in the light of experience and we will participate constructively in any such review.

Our comments by subject area are set out below.

“Direct Impact” on system operation (section 1, paragraph 2.13, section 2, paragraph 2.13)

It is not entirely clear what this term means. We assume that this includes impacts on flows on the distributor's network, but these won't necessarily affect its operation. It could be clarified that such impacts are included.

Allowable Set-up expenditure (section 1, paragraph 3.5)

We assume that this is not subject to DNO minimum funding of 10%, but this could be clarified in the text.

“Revenue allowed for in the DPCR5 settlement” (section 1, table 2.1, paragraph 3.8, paragraph 3.20)

Base allowed revenue for DPCR5 is not allocated to specific areas. Also, we do not recognise the reference to revenue allowed for specific project “i” in the term “DPCR5it” in paragraph 3.8. We did not submit specific costs in this category for DPCR5.

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Second Tier Funding Mechanism (section 2, paragraph 1.9)

The statement that Ofgem will “... *annualise any multi-year costs and allow them to be expensed in the first year of the Project*” is not entirely clear. We assume that this means that multi-year costs will be discounted to present values at a discount rate of [x%] to derive costs to be expensed in the first year of the Project. However, this and the discount rate to be used should be made clear.

Direct Benefits (section 2, paragraph 3.13)

We find this paragraph a little hard to follow. A suggested clearer version is set out below.

- 3.13. *The DNO may use Direct Benefits to contribute to the DNO Compulsory Contribution ~~up to the value of the DNO Compulsory Contribution~~. If Direct Benefits do not exceed the value of the DNO Compulsory Contribution, then the Initial Net Funding Required less the **value of the** DNO Compulsory Contribution is the Second Tier Funding Request Amount. If Direct Benefits exceed the value of the DNO Compulsory Contribution, then the Initial Net Funding Required less Direct Benefits **gives the** ~~must be deducted from the Initial Net Amount Required to identify the~~ Second Tier Funding Request **Amount**.*

Response deadline for queries during Evaluation Process (Section 2, paragraph 3.33, 3.36, 3.37)

We are concerned about the preset mandatory timescale of two working days for responding to an information request (“request for clarification”) regarding a Full Submission. Two days is also the preset limit for written responses to questions from the Expert Panel or the Authority. Depending on the complexity of the request, it may take significantly longer than two days to prepare a response and obtain internal approval as required. We do not think that it is appropriate to set such a timescale in the Governance Document. In other cases where Ofgem seeks information it will provide a requested timescale depending on the nature and detail of information required, and this should apply here also.

Disallowed Expenditure (Section 2)

We note that the section on Disallowed Expenditure (Section 2, paragraphs 3.93 and 3.94) does not require Ofgem to give reasons for its view that funds received by a DNO fall into that category, and the basis for disallowing the relevant portion of these. It would be helpful if this was made explicit.

Funding Directions (Section 4)

It is not clear at what point following the initial funding decision the Funding Direction is issued. Paragraph 1.3 of section 4 says that “sufficient time will be allowed” for each DNO to reflect the impact on its allowed revenue from 1 April. However, the timetable is clearly very tight, given that in paragraph 3.61 of section 2, it is stated that the decision on project funding will be issued by November 30 in each year, to be followed by a period to allow for draft and then final Project Directions. Following the Funding Direction, the DNO must then finalise its pricing proposals to take account of the Direction, and obtain formal internal approval, before publishing indicative charges to users by 31 December. The sums involved may be very significant for individual DNOs in both absolute terms and in proportion to allowed revenue.

We therefore think that for future years, Funding Directions should be issued earlier in the year (by the middle of November) in order to allow companies sufficient time to take account of these in their pricing. The timetable for ISPs, full submissions, etc. should be amended accordingly.

I hope that this is helpful, but please contact me if there are any queries.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'J Blackford', with a stylized, cursive script.

Jeremy Blackford
Regulation and Commercial
SP Energy Networks