



All Electricity Distributors

*Promoting choice and value for
all gas and electricity customers*

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Date: 2 March 2011

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.

This letter constitutes formal notice under CRC 13 of the Electricity Distribution Licence of the Authority's intent to issue version 4 of the LCN Fund Governance Document ('the Governance Document') for purposes connected with the regulation, governance and administration of the LCN Fund (the 'Notice'). A draft of the Governance Document is appended to this letter. **Representations or objections to this Notice should be made to Ofgem¹ on or before Wednesday 30 March 2011. Representations or objections that are received and not withdrawn will be considered by Ofgem prior to the document coming into effect on 1 April 2011.**

On 22 July 2010 we published version 3 of the LCN Fund Governance Document which represented the complete version². We have now completed a high level review of the operation of the LCN Fund, following the completion of the first year process. A separate letter has been published today setting out the findings from that review. On the basis of our findings we have made a limited number of amendments to the Governance Document – which are summarised below. These amendments are designed to improve the process for future submissions. We intend to undertake a comprehensive review following the conclusion of the second year process.

Carbon and Financial Benefits (First Tier, Initial Screening and Full Submission evaluation criteria)

We have amended the way in which we ask for the carbon and financial benefits of projects to be presented. We have asked that financial benefits are presented separately from the carbon benefits. In their presentation of carbon benefits, we are requiring DNOs to identify the specific aspect or aspect(s) of the Low Carbon Transition Plan³, as published by the Department of Energy and Climate Change (DECC), which the project can facilitate if successful. We are requiring DNOs to outline the contribution the method their project is trialling can make in this facilitation compared to business as usual. We are also requiring DNOs to outline why their project enables the aspect(s) of the Low Carbon Transition Plan to be facilitated more quickly than business as usual. In addition, we are requiring DNOs to set out a qualitative account of the replicability of their project across GB distributions

¹ Ofgem is the offices of the Gas and Electricity Markets Authority. The terms Authority and Ofgem are used interchangeably in this letter.

² The governance document was developed in stages; version 1 covered First Tier arrangements, version 2 added the initial screening arrangements and version 3 the full submission arrangements.

³ The UK Low Carbon Transition Plan: National Strategy for Climate & Energy July 2009.
http://www.decc.gov.uk/en/content/cms/publications/lc_trans_plan/lc_trans_plan.aspx

systems. We have removed the requirement for DNOs to quantify the value of carbon savings that their project can deliver if successful, although DNOs are still permitted to provide this analysis if they wish.

In the presentation of financial benefits, we will require DNOs to identify the cost of the method the project is trialling compared to the base case. The base case is the lowest cost method of delivering the solution which has already been proven on the GB distribution system.

Definitions of Project terms and parties (Definitions and used throughout)

We have amended the definitions of 'Method' and 'Solution' and added two new terms: 'Trial' and 'Problem'. This is to improve clarity and to enable the DNOs to better describe their projects. We have also ensured that the terms are used consistently throughout the Governance Document.

We have amended the definitions for the parties involved in a project. This is to distinguish between a 'Project Partner' who provides a financial commitment or resources to a project and a 'Project Supporter' who simply endorses a project.

Detailed guidance on customer engagement and data protection (First Tier, Initial Screening and Full Submission)

We have introduced some detailed requirements on customer engagement which DNOs must follow for First Tier projects, the initial screening process (ISP) and at Full Submission. We have added new requirements outlining what a customer engagement plan should detail for First Tier projects. Further, at ISP we are requiring DNOs to provide a summary of how their project will impact customers. At Full Submission we are requiring a detailed account of how project implementation will impact customers. We are also requiring that where a project is selected for funding, DNOs must provide Ofgem with a plan of how they, or their partners, will engage and communicate with customers. Where the project involves collecting personal data we are also requiring a detailed plan of how this will be managed.

ISP decision process (p35)

We have removed the requirement on us to provide a decision letter for each project which has passed the ISP. We will still provide a decision letter for those projects which have failed the ISP within 20 working days of the deadline for submitting initial screening proposals.

Greater scope for DNO collaboration following the ISP (p37)

We have made a number of small changes to increase the opportunities for DNOs to collaborate following the submission of ISP proposals. These include publishing the DNOs' screening submissions in full and setting out the process by which DNOs can collaborate following ISP.

Derogations and exemptions (p39)

We are requiring DNOs to justify why any derogations, exemptions or changes to regulatory arrangements are required to implement their project are necessary and justified. We are also asking DNOs to identify how customers would be impacted by them. We are requiring DNOs to identify where the roll out of the Method will require similar derogations, exemptions or changes regulatory arrangements.

For projects which introduce new distribution charging arrangements⁴ we are requiring DNOs to identify how the trial charging arrangements will better achieve their relevant objectives set out in Standard Condition 13 of the electricity distribution licence⁵. We are also requiring that DNOs set out how customers will be recruited to the trial and if they can be financially worse off through adopting the new charging arrangements.

Include cost of IIS penalties in funding request (p41)

We consulted on providing protection to LCN Fund projects that would need to interrupt customer supply from IIS penalties⁶. We have today published our decision that, if DNOs wish to seek protection, DNOs should include the amount they expect to incur in penalties under the IIS scheme as part of the application process. We have reflected this in the Governance Document.

More formalised Full Submission question and answer (Q&A) process (p45)

We have introduced a requirement for DNOs to resubmit their full submission following questions and clarifications during the evaluation process. We propose that this version will be the one published and will provide a more complete picture of the submission for interested parties. This is to ensure that the published information on the project is the most up to date and reflects any changes made as part of the evaluation process.

Changes to the Second Tier Direct Impact Evaluation Criterion (p48-49)

We have amended the title of this criterion to refer to the level of impact, as opposed to Direct Impact, that the project has on the Distribution System. This is in recognition that Direct Impact⁷ is a defined term which a project either meets or does not. At Full Submission, projects are assessed against the degree to which they achieve a criterion. Therefore we have amended the title, and focussed the criterion wording to remove some of the existing overlaps with other criteria. We consider that this amendment removes the possibility of any confusion between the application of this criterion at Full Submission and the application of the Direct Impact criterion for First Tier projects and ISP.

Representations or objections to this Notice should be made to mark.askew@ofgem.gov.uk on or before Wednesday 30 March 2011. Responses will be published on Ofgem's website unless marked as confidential.

Yours faithfully,



**Rachel Fletcher
Partner, Distribution
For and on behalf of the Gas and Electricity Markets Authority**

⁴ These are the tariffs which DNOs charge suppliers for transporting electricity across their network. It can also cover the costs charged for connecting to the network.

⁵ The Relevant Objectives in relation to the Charging Methodology are: (a) that compliance with the methodology facilitates the discharge by the licensee of the obligations imposed on it under the Act and by this licence; (b) that compliance with the methodology facilitates competition in the generation and supply of electricity, and does not restrict, distort, or prevent competition in the transmission or distribution of electricity; (c) that compliance with the methodology results in charges which reflect, as far as is reasonably practicable (taking account of implementation costs), the costs incurred by the licensee in its Distribution Business; and (d) that, so far as is consistent with sub-paragraphs (a), (b), and (c), the methodology, as far as is reasonably practicable, properly takes account of developments in the licensee's Distribution Business.

⁶ <http://www.ofgem.gov.uk/Networks/ElecDist/lcnf/Documents1/IIS%20consultation%20letter.pdf>

⁷ Direct Impact is defined as "Where the deployment of the Method will cause a directly related measurable change in the operation of the Distribution System in a controllable way".