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Distribution Policy
Ofgem
9 Millbank
London
SW1P 3GE

Your ref

Our Ref

Date

17 October 2011

Contact / Extension

Martin Hill
0141 614 1962

Dear Neil,

Decision and further consultation on the design of the Network Innovation Competition – Ref 113/11

Thank you for the opportunity to comment on Ofgem's decision and consultation document above. This response is written on behalf of SP Energy Networks, which acts as the holding company for licensed network businesses of SP Transmission, SP Distribution and SP Manweb.

I can confirm that this response is not confidential and can be published on the Ofgem website. In the supporting annex we have set out our responses where relevant to your specific questions however our main points for consideration are:

- We support the introduction of the Network Innovation Competition (NIC) and welcome the fact that the design of the NIC will be based upon the principles of the Low Carbon Networks Fund (LCNF) which has been very successful to date
- A key requirement of the Expert Panel is that it should include representation from persons who have had previous experience of working within a network organisation. The existing membership criteria is quite restrictive in our view and limits the number of true "expert" participants
- The focus of the award of NIC funding should be to develop learning around technology/techniques that will assist in the development of the GB electricity and gas network. Projects should be assessed against the potential learning benefits, and otherwise worthwhile projects should not be rejected on the basis that there is no partner from the small to medium enterprise sector

Should you have any questions regarding any aspect of our response, please do not hesitate to contact me by return.

Yours sincerely,

Martin Hill

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Annex

Question 1

Do you agree with our proposed two stage evaluation process and evaluation criteria?

In principle we believe that a two-stage evaluation process is appropriate, However each company is unlikely to submit a bid to the competition which does not meet the defined prequalification criteria set by Ofgem, a view which is reinforced based upon the fact that no projects that have failed the ISP stage to date. Therefore we would wish that meaningful criteria be defined to determine whether projects are eligible to go forward to the Full Submission stage.

The existing criteria for membership of the Expert Panel is overly restrictive, in our view, in that one of the main criteria is that potential candidates must highlight any conflict of interest with any member of the existing network community. Given that we seek an “expert” panel to oversee the competition and consider the merits of each project, it is perverse that a previous working knowledge within a network organisation may preclude a person from being part of the panel.

We do not foresee any conflict of interest developing as each project will be subject to review by a panel of experts from different fields and any participant could rule themselves out of the process if they considered that their relationship with a competing network operator was likely to cause a significant conflict of interest.

Going forward we would consider it appropriate to develop a pool of expert panel members which could be called upon to make an assessment of projects submitted for consideration for funding however one of the overriding criteria should be that at least one member of the panel must have a working knowledge of the activity of a network operator. By encouraging the use of panel members with a working knowledge of a network operator, this will increase the practical working knowledge and expertise of future panels.

With respect to the additional criteria that the expert panel judge each project against, we have a concern over the proposal to include an extra weighting for projects which involve partnerships between network operators and small and medium enterprises. The overriding objective of the NIC process should be to drive future benefits and learning for all GB network operators and suppliers of equipment to those organisations. Furthermore, all network operators acknowledge a commitment to disseminate learning from each of their projects to all stakeholders.

Therefore to possibly restrict funding for a proposed project which on merit may provide a greater learning for all GB stakeholders over another project on the basis of who was partnering the network operator will drive no major benefits and risk the opportunity for real learning to be missed as a consequence of misguided criteria.

To date we can provide evidence of network companies collaborating with a range of organisations which vary in scale from the SME, Academic and Charity sectors, through their Tier 1 and IFI projects and we do not believe that there is any barrier to preclude smaller organisations from participating in existing and future trials. The overriding focus should not be biased towards the partner organisation but what the partner can bring to the table in the sense of learning and how this may benefit GB PLC.

We also have a concern over the criteria to demonstrate a robust methodology and readiness for implementation. By the very nature of the NIC process, network operators may seek to bring forward a project which was in the early stages of development i.e. the project may require Research and Development or equivalent to the IFI stage, we would therefore seek further clarification on how such projects could compete in the proposed NIC framework for funding. We are also not clear on the propose criterion of relevance to current (as opposed to future) network requirements,

We also do not believe there is yet sufficient clarity in the classification of projects as between the different funding mechanisms proposed for RIIO T1 (NIA, NIC, and Innovation roll-out funding).

Question 2

Do you agree with our proposals for facilitating non-network company participation in the NIC?

We agree with Ofgem's assessment that non-network companies have a role to play in bringing new and innovative ideas forward that can assist network companies. However we would stress that through deployment of the existing IFI and LCNF mechanisms, network operators can adequately demonstrate a high degree of participation and partnerships with non-network companies and therefore do not see any barriers for those companies to become involved with a particular project where it can be demonstrated that their involvement adds value to the process and results in learning for wider industry participants.

We welcome the fact that Ofgem recognise that during the first year of the LCNF that there is evidence to support that network companies are already collaborating effectively with third parties and that there is no evidence to suggest that network companies are rejecting good ideas which originate from non-network companies. We expect this to only grow during the development of the NIC.

Question 3

Do you agree that the transmission companies should raise the funding for the NIC, and that it should be borne by customers according to their network usage?

We believe that the funding of successful projects following the NIC should be borne by energy customers and can see the merit of this being collected based upon network usage as all customers will benefit proportionately from the learning of each project.

Having considered the pros and cons for how the funding revenue will be collected, we believe that the better option is for the GBSO to be responsible for the collection and distribution of those funds as it is responsible for charging all transmission users. Transmission licensees raise their allowed revenue through a charge on the GBSO which in turn it passes on to users through use of system charges. This would mean implementing a licence condition upon the GBSO to allow them to raise the required funding through their use of system charges and be the sole point of contact for the distribution of funds. Also based upon their existing charging methodology, charges borne by customers would naturally be proportionate to their network usage.

Question 4

Should network companies be funded to cover some or all of the preparation costs for submissions to the NIC? If so, is the Network Innovation Allowance (NIA) the best way to achieve this?

We believe that network companies should be funded to cover efficient costs incurred in the preparation of submissions to the NIC. Adoption of a similar mechanism to that in existence for LCNF Tier 1 projects would be appropriate whereby the network operator can use up to 20% of their LCNF allowance to fund development costs. As already discussed in our response to this consultation, the overriding objective should be to explore the possibility for learning and therefore we should not put in place a mechanism which leads to companies reducing their willingness to enter the competition for fear of risking development cost for potentially no reward.

Question 5

Do you agree with our approach to learning and intellectual property (IP) generated by the NIC? If not, please indicate how these arrangements could be improved.

We agree with the existing approach taken by Ofgem in respect of the treatment of IP for LCNF/IFI projects and agree that this should be extended for the operation of the NIC. For our part we are keen to share the IP benefits without necessarily owning the IP and can see the benefit to customers of the current approach.

Question 6

Do you agree with our proposals to offer a successful delivery reward and protection against cost overruns?

Yes. We agree with the proposals to offer a successful delivery reward and protection against cost overruns however would suggest that this element of the competition requires further dialogue with industry stakeholders to ensure that the governance is fit for purpose and does not unduly reward/disadvantage companies that enter the competition. Until this review takes place with Ofgem we would have reservations regarding a company being unable to seek reward if there were legitimate reasons why a project has required additional funding.

Question 7

Do you agree with our proposal not to have an ex-post delivery reward or specific reward for commercial innovation?

Yes. We believe than any commercial innovation will for the vast majority of projects be established on the back of technical advances/innovation therefore we do not foresee any requirement for a separate delivery reward for commercial innovation. There may be occasions when due to the nature of some projects, commercial arrangements begin to push the boundaries of existing commercial rules that surround the industry, however we believe that any commercial reward would be naturally realised as the project progressed.

Additional comment

As most projects in the Electricity Transmission sector that take place in Scotland will require co-operation of the GBSO, there may be a need for a modification to the STC to provide for dispute resolution in the event that progress on an approved project by one of the Scottish Transmission Owners encounters difficulties due to the actions of the GBSO.