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Dear Dora,

Further consultation on design features of the Network Innovation Competition (NIC)

I am writing to you on behalf of Northern Powergrid Holdings Company and its wholly owned electricity distribution licensees Northern Powergrid (Northeast) Limited and Northern Powergrid (Yorkshire) plc. This letter provides our response to Ofgem's recent consultation on design features of the Network Innovation Competition (NIC).

To summarise, we support the eligibility of non-RIIO licensees to take part in the NIC and believe that their participation could enhance the volume and quality of project proposals. We recognise that the non-RIIO licensees have different licencing regimes and that some accommodation with respect to both the NIC governance or network licences may be needed in order to better facilitate their full participation. We particularly believe that the discretionary rewards mechanism, applied to its full potential, can incentivise non-RIIO companies to be fully involved whilst also eliciting highly innovative project ideas and high quality project execution from RIIO licensees. This will be to the ultimate advantage of the networks' customers.

Responses to all the questions raised in the consultation with respect to the participation of non-RIIO licensees are provided below.

i. Appetite for Entry?

As a RIIO licensee, it is difficult to directly judge the degree of appetite for participation in the NIC from non-RIIO licensees. We therefore consider that this is a question for them to answer.

ii. Potential benefits

We agree with Ofgem's view that the inclusion of all network licensees in the NIC would potentially increase the range and quality of potential projects. The non-RIIO licensees may have different set of commercial and technological imperatives which will influence their assessment of what constitutes projects that potentially provide the customer and industry with value-for-money outcomes. These will potentially provide a different perspective to that held by the RIIO licensees and as such will increase the innovative range of proposals.

The much smaller size of the majority of the non-RIIO licensees may also mean that important areas for innovative deployments are proposed, that could otherwise be overlooked in the context of larger organisations, but are nonetheless important for the future.

iii. Meeting the evaluation criteria

We believe that the evaluation criteria for the NIC, based on the Low Carbon Networks (LCN) fund criteria, have been well developed, resulting from long and careful consideration from a large number of participants. The evaluation criteria of the LCN fund provide a clear framework

without being excessively prescriptive and, as such, all participants in the NIC should be required to adhere to them.

Where potential projects by non-RIIO licensees are felt to be insufficiently applicable to the national network we believe that they should not be eligible for funding under the NIC. Under such circumstance we do not believe that customers' money should be used to fund narrow projects which would potentially provide only commercial advantage for the proposer rather than general technical advantage for the broader GB network.

iv. Potential barriers

The key barrier to participation of non-RIIO licensees is likely to come from their size. Smaller organizations are more likely to be constrained with respect to innovation resources required to delivery NIC bids and projects. Consequently they are likely to prioritise such limited resource into innovative areas where competitive advantage can be gained. NIC projects, where outcomes need to be shared across the industry, may therefore represent an opportunity cost to non-RIIO licensees that presents a considerable barrier to participation in the competition.

There may be potential to mitigate this by providing the opportunity for organizations to earn a premium return as the result of the outcome of projects (akin to the second tier award in the LCN fund). We consider that the opportunity to earn a return on investment in innovation projects incentivises companies to bring forward good ideas and deliver funded projects effectively. A discretionary reward or similar mechanism should be extended to all participants in the NIC including RIIO licensees.

v. Funding bid submission costs

The experience of the RIIO licensees taking part in the LCN fund second tier completion has been that the costs of preparing a high quality bid, in line with the requirements of the fund governance and evaluation criteria, is expensive both in terms of time and money.

The ability to offset these costs against the first tier allowance has been vitally important in allowing the breadth and quality of competitive bids to the LCN fund to date. The intention to allow companies to continue to offset such costs against the Network Innovation Allowance (NIA) is noted and welcomed.

We believe that the non-RIIO licensees also need to be able to recover reasonable costs if they are to participate in the NIC, therefore enhancing the volume and quality of project proposals. We suggest that, as now for RIIO licensees, such recovery is dependent upon an expectation of high quality bids being submitted.

This can simply be the requirement to reach a particular level of scoring in the bid assessment process and under these circumstances bids of sufficient quality should allow cost recovery whether the project is successfully funded in the competition or not.

vi. Halting Projects

The ability of Ofgem to recover underspent, misspent or no longer required monies is a key aspect of the LCN fund and is similarly required for the NIC. All participants in the NIC need to be in a position where such a sanction can be applied and we welcome Ofgem's intention to amend the licences of non-RIIO companies wishing to participate in the NIC to allow this.

With respect to RIIO licensees the consultation puts the following question;

Do you agree with a sliding cap of between 5 and 10 per cent of the NIA to fund bid submission costs for RIIO network licensees?

We agree that a sliding cap for the proportion of NIA that can be used for funding NIC bid submission makes an appreciable contribution to ensuring that an equivalent proportion of

allowable revenue is available for spending by each DNO.

We do however note that main factor in determining the ability to effectively compete in the NIC is likely to be the value of allowable revenue (AR). Larger DNO groups, having a larger AR, may therefore be in a better position to fund more sophisticated, expensive bids that are not feasible for smaller companies thus gaining an advantage, not necessarily related to the inherent value of the bid, and detrimental to the stated aims of the competition. This possibility needs to be monitored during the life of the NIC.

I hope you find these comments useful. If you have any questions arising from this response please do not hesitate to make contact.

Yours sincerely

Chris Goodhand