

## Innovation Working Group (IWG) Meeting January 2012

Ofgem hosted this meeting to update the IWG on the work plan for 2012 and to understand their views on some of the issues currently being consulted on.

From  
Date and time of Meeting  
Location

Neil Copeland  
19 January, 1400-1600  
Ofgem, 9 Millbank, Westminster

### 1. Present

Stewart Reid (SR)	SSE
Roger Hey (RH)	WPD
Simon Brooke (SB)	ENWL
Martin Hill (MH)	SP
Sean Kelly (SK)	Transmission Capital
Martin Atkinson (MA)	SGBI
Denise Massey (DM)	EIC
Chris Goodhand (CG)	NPG
Jenny Cooper (JCo)	NG
Sara Bell (SBe)	UKPN
Insaf Ahamed (IA)	SGN
Haren Thillainathan (HT)	NGN
Zoltan Zavody (ZZ)	Renewables UK
John Christie (JC)	DECC
Jason Eis (JE)	The Carbon Trust
Dora Guzelava (DG)	Ofgem
Sam Cope (SC)	Ofgem
Nicola Merehan (NM)	Ofgem
Neil Copeland (NC)	Ofgem

### 2. Welcome and Introduction

2.1. SC welcomed the attendees and thanked the members of the working group for their attendance. He noted the new members of the team at Ofgem and drew attention to the new email address ([networks.innovation@ofgem.gov.uk](mailto:networks.innovation@ofgem.gov.uk)) where all members of the innovation policy team can be contacted. SC then set out that the purpose of the meeting was to update stakeholders on the work plan that will be followed to implement the RIIO Innovation Stimulus and discuss the current consultation on the Network Innovation Competition.

2.2. These notes aim to capture the key points of discussion. They do not indicate or imply Ofgem's agreement to points made by attendees.

### 3. Part 1: Overview of work for 2012

3.1. SC presented a set of slides to the group<sup>1</sup>. He presented 4 areas.

#### *Work to be completed*

3.2. SC talked the group through slide five which set out the three areas of the network innovation stimulus that were to be developed through 2012. These were the Network Innovation Competition (NIC); the Network Innovation Allowance (NIA); and the innovation

<sup>1</sup> The slides referred to throughout this document are available as a subsidiary document to these minutes on the Ofgem website.

rollout mechanism (IRM). He noted that governance documents would need to be developed for both the NIC and NIA and highlighted the predecessors to these policies.

### ***Overview of timings***

3.3. SC summarised slide six which drew attention to the statutory consultation on the licences for the RIIO: T1 and GD1 price controls at the start of 2013 noting this drives when the drafting of the governance documents must be complete. SC also noted the Low Carbon Networks (LCN) Fund second year review and pointed out that the lessons learned from implementing the LCN Fund will feed into the development of the NIC and NIA.

### ***Developing the Governance***

3.4. SC set out Ofgem's proposed approach for developing the governance documents. He set out that Ofgem will seek to follow the approach adopted in the LCN Fund in drafting the governance of the NIC and NIA unless there is a particular reason for divergence. This was because of the considerable effort that both Ofgem and their stakeholders have already expended in developing those arrangements. It was noted, however, that the scope of the NIC and NIA are broader because they cover gas and electricity. In addition the NIC is focused at low carbon and environmental projects (as opposed to solely low carbon as in this case with the LCN Fund). SC noted that these issues were likely to be the drivers of any divergence away from LCN Fund arrangements.

3.5. He went on to note that the next steps in developing the governance are to determine the structure of the various governance and guidance documents before beginning the detailed drafting. SC noted that Ofgem wanted this process to be collaborative and that Ofgem intended to consult members of the working group throughout the process (meetings every 4-6 weeks). With this in mind Ofgem would be publishing a letter shortly inviting full stakeholder participation in the IWG.

3.6. SC also noted that electricity distributors will be party to the arrangements developed through this group, once the RIIO-ED1 control begins in 2015. As such he stressed the importance of stakeholders with an interest in ED1 being involved in the development process.

### **ACTION: - Ofgem to publish a letter which invite interested parties to participate in the IWG.**

SC went on to summarise slides eight and nine which set out some further detail with regard to the potential structure of the governance documents and highlighted areas where Ofgem considered divergence from the LCN Fund arrangements may be necessary. He also drew attention to the issues that are being discussed by the LCN Fund review. In particular he noted:

- Structure of Governance Documents. SC noted that there would be separate governance documents for NIA and NIC. He also noted that, as there are a number of different types of licensee involved in the NIC and NIA, it could be appropriate to include a different obligation section for each separate type of licences, with a common section providing guidance on process matters.
- Other potential areas of divergence. SC noted the areas where there could be potential divergence from the current LCN Fund governance arrangements in implementing NIC and NIA. He invited the group's comments on this.

3.7. MH noted that the treatment of intellectual property may diverge from its treatment under the LCN Fund. He pointed out that the treatment of intellectual property (IP) is different under the Innovation Funding Incentive (IFI) to its treatment under the LCN Fund.

3.8. MH also drew attention to the need for transition arrangements between price controls for IFI projects to avoid a drop off in innovation projects towards the end of the current price controls.

3.9. JCo noted that for gas distribution network operators and transmission operators they will be transitioning from the IFI to NIC/NIA not the LCN Fund and they are not necessarily aware of the nuances of the LCN Fund. JCo also pointed out the criteria for the gas IFI are not the same as for the electricity IFI and this was something to be aware of. RH concurred and noted that the LCN Fund is probably the narrowest in scope. Ofgem acknowledged that the scope of IFI is broader, in terms of project scope, and this should be considered. However, Ofgem also noted that the regulatory requirements of the LCN Fund would be considered in developing the NIA governance.

3.10. SB repeated a point made at the LCN Fund meeting earlier in the day that there might be a need to be a change to the process for the LCN Fund Second Tier and for the NIC. There is likely to be a larger number of submissions each year than the LCN Fund has had to deal with in any year to date and Ofgem should consider the resource implication of this (both for Ofgem and potential bidders).

3.11. Following this a discussion then took place around the table regarding the evaluation process and focussed on the initial screening process (ISP) in particular. SBe argued companies need a comfort level that if something makes it through the ISP there is a better than even chance that a project will receive funding. SB added that when a company submits a project to ISP they have done a lot more work than necessarily makes it into the ISP. SB pointed out the effort ENWL went to in 2011 regarding derogations before making a submission to ISP. Ofgem noted that a lot of work can go into developing a project for the ISP stage, but noted that some of this work was funded by consumers and also noted the importance of competitive pressure throughout the process.

3.12. RH pointed out that the ISP had been useful for two of WPD's LCN Fund projects. The ISP allowed Ofgem to offer feedback at an early stage regarding the potential eligibility of certain projects.

3.13. DG summarised the discussion and noted that a number of suggestions had been made including: a two stage process with a short list; removing the ISP stage; or, making the ISP stage stronger and that Ofgem would consider the comments raised and bring this issue back at the next IWG meeting for further discussion.

### ***Next Steps***

3.14. Finally, SC summarised slide ten – 'Proposed next steps'. He stated Ofgem intends to hold another meeting in February and Ofgem will circulate a list of issues to the IWG members beforehand.

**Action – Ofgem will produce and circulate a list of issues to be discussed by the IWG in late February.**

## **4. NIC consultations update**

4.1. NM set out the history of consultations on the NIC and NIA. She drew particular attention to the September 2011<sup>2</sup> and January 2012<sup>3</sup> consultation documents. NM noted Ofgem's intention to publish a decision on both consultations at the same time in early in the spring.

4.2. NM gave an overview of the issues covered in these documents. To date Ofgem have left open the opportunity for all network licensees to access the NIC. These are the

<sup>2</sup> <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=319&refer=Networks/nic>

<sup>3</sup> <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=333&refer=Networks/nic>

Riio companies, the OFTOs and the independent network operators. Ofgem have set out some possible treatments for non-Riio companies in the consultation these were summarised on slide fifteen – ‘Treatment of non-Riio Licensees’. NM asked for members views on the likely level of interest that non-Riio licensees may have in participating and for views for the treatment of independents and opened the floor for discussion.

4.3. MA responded to say he had written to members of the SGBI<sup>4</sup> regarding the NIC to make them aware of the mechanism and to encourage them to make use of it. To date he has had no response. JCo asked whether Ofgem would consider revisiting the size of the fund if more IGTs came forward. NM responded that this was unlikely to be something Ofgem would consider purely based on the number of projects.

### **Non-Riio participants**

4.4. SR asked whether Ofgem felt that IDNOs do not have a reason to innovate. DG pointed out they operate under a relative price control therefore they have an incentive to innovate and increase their profits. DM felt IDNOs would be more agile and fleet of foot and therefore more likely to be innovative.

4.5. DG asked whether there were any concerns around the table about having independent network operators being able to directly access NIC funding. SR pointed out he would be concerned if they were not in. SB and RH concurred with this view.

4.6. DM pointed out that she would have some concern if money was awarded to a non-Riio licensee if Ofgem did have mechanisms to claw back misspent funding. Ofgem responded that a non-Riio licensee would be required to have the same licence conditions as Riio network licensees to ensure funding is not misspent and that we are currently looking at how this would work in practice.

4.7. A brief discussion took place regarding whether non-Riio companies should have the cost of preparing submissions paid for by the customer. SM argued that they should. CG noted that for independent network companies there is an opportunity cost to participating in the NIC and they would need to invest scant resources in preparing their submission.

### **Setup Costs**

4.8. NM introduced a discussion regarding setup costs for Riio licensees and summarised slide sixteen – ‘Funding bid submission costs’.

4.9. MA responded that he felt it was strange that a company with a 1% NIA would not be allowed setup costs of the same proportion of their NIA as a company with a 0.5% allowance. Given that this allowance would be reflective of the quality of their innovation strategy.

4.10. SB thought that this proposal could be unfair for companies with only one licensee and could allow groups with multiple licences to pool setup costs across different licence areas. SR felt the differential is acceptable and reflective of the size of the organisations involved. He pointed out that both SSE and SP are both smaller companies than NG and they will receive a smaller NIA – he felt this was equitable.

4.11. MH and SR asked how the amount of funds available under setup costs for the NIA compared with setup costs for the LCN Fund. NM pointed out that the amount of setup

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<sup>4</sup> Formerly known as the Society of British Gas Industries.

expenditure would be roughly equivalent to that available under the LCN Fund and the reasons for this are explained in the consultation<sup>5</sup>.

## 5. AOB

5.1. ZZ asked where there were opportunities for non-network parties to participate in this process. SR responded that there are groups which feed into the price control activities of all the licensees. In addition each successful LCN Fund project that impacts upon customers has a customer engagement plan and there is an opportunity for parties to feed into this process. ZZ responded that if there was a way his organisation could be useful to those around the table then they should contact him.

5.2. NM reminded respondents that the current consultation closes on 1 February and should be sent to [networks.innovation@ofgem.gov.uk](mailto:networks.innovation@ofgem.gov.uk).

## 6. Date of next meeting

6.1. SC noted that Ofgem plan to hold a meeting in late February and will confirm dates shortly.

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<sup>5</sup> POST MEETING NOTE: DNOs can spend between approximately 0.3 and 0.5 per cent of their annual allowed revenue on First Tier projects whereas the NIA will be set between 0.5 and 1 per cent of a RIIO network licensees' annual allowed revenues (i.e. the proportion of the NIA compared to allowed revenues is double that of the LCN FUND). As such, we have ½ the cap percentage for the bid costs so that the amount that can be recovered under the NIA is proportionally the same as for the LCN FUND.