



All Electricity Distributors

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

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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 5 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 sent, preferably by email, to sam.williams@ofgem.gov.uk on or before Monday 16 April 2012. We will consider representations or objections that are received and not withdrawn prior to the document coming into effect on 19 April 2012.

On 1 April 2011 we published version 4 of the LCN Fund Governance Document¹. We have now completed a high level review of the operation of the LCN Fund, following the completion of the second year process. We launched this review on 11 December 2011 with a consultation that set out a number of potential areas for refinement but did not consider any fundamental changes to the fund². We considered that the LCN Fund had worked well to date and had successfully incentivised DNOs to undertake a range of innovative projects.

We are pleased to note that respondents to the consultation supported our views and emphasised the role of the LCN Fund has played in stimulating innovation. Consequently, on 22 February we published a decision that we intended to make a number of refinements to the LCN Fund rather than undertake wholesale reform³. This document sets out the reasons for the changes set out in this Notice. To implement these refinements we have made a limited number of amendments to the Governance Document, which are summarised below. These amendments are designed to allow the LCN Fund to provide better value for money to current and future consumers.

Cost benefit analysis (pages 15-16, 42-43 and 57-59)

We have amended how we evaluate the way in which projects deliver carbon benefits. DNOs must provide an estimate of how much capacity the methods trialled in their projects will release, and how much more quickly this will be released than with conventional methods. We will also require DNOs to provide an estimate of how the methods trialled reduce the cost of creating capacity compared to conventional methods. We are

¹ [Low Carbon Networks Fund Governance Document v.4](#)

² [Low Carbon Networks \(LCN\) Fund: Two year review](#)

³ [Decision on the Low Carbon Networks Fund Two Year Review](#)

maintaining the requirement for DNOs to provide a qualitative description of how the project facilitates the move to a low carbon economy. These requirements take account of two separate evaluation criteria – (a) accelerates the development of a low carbon energy sector and (b) has the potential to deliver net benefits to existing and/or future customers. We have therefore merged these two considerations into a single Full Submission evaluation criterion, Initial Screening Process (ISP) criterion and First Tier project specific requirement for Full Submission, ISP and First Tier projects respectively.

Full Submission Evaluation Criteria (pages 59 - 62)

We have amended the title of criterion (b) to "provides value for money to distribution customers". This is because we are requiring DNOs to set out how the processes they have put in place and other steps they have taken ensure that the Second Tier Funding Request represents best value for money to Distribution Customers. As a result

We have amended criterion (d) involvement of other partners and external funding. We are requiring DNOs to specify the systems and processes they have in place to identify project partners. We are also requiring DNOs to set out how they have ensured that project partners involved in selecting other project partners have followed similar steps.

We have amended criterion (e) relevance and timing. We are requiring DNOs to outline how the Methods being trialled will affect business plan submissions, regardless of the increase in renewable energy and low carbon technologies.

We have amended criterion (f) demonstration of a robust methodology and the project is ready to implement. We are requiring DNOs to set out how the project would still deliver learning in the event that the take up of low carbon technologies and renewable energy in the trial area is lower than anticipated.

Process (pages 55-57)

We have amended the Full Submission evaluation process. We are providing DNOs with the opportunity to resubmit their project in light of questions raised by the Expert Panel or points raised in the report prepared by Ofgem's consultants. DNOs will not be able to change the underlying problem, method or solution of the project. We have also included additional detail on the process for issuing Project Directions for each project.

Intellectual Property Rights (IPR) (pages 67, 70, 77 and 85-86)

We have amended a number of sections of the Governance Document to include a mechanism to return revenue earned through IPR generated by projects to customers. We have included:

- a requirement for DNOs to report details of royalties revenue earned through projects;
- a mechanism to allow DNOs to recover the costs of maintaining IPR;
- a mechanism to disallow expenditure on the maintenance of IPR if we consider it to have been misreported or not recovered in accordance with the Governance Document and Project Direction;
- a term in the funding direction to return royalties to customers and transfer royalties between DNOs; and
- the process Ofgem will follow to calculate the amounts relating to royalties to be returned to customers and transferred between DNOs.

Other (pages 25-26, 52 and 65-67)

We have amended the requirements on customer engagement which DNOs must follow for First Tier projects, ISP and at Full Submission. We are keen to ensure that domestic and small or medium enterprise customers are not adversely affected by LCN Fund projects.

Therefore we have removed the requirement for DNOs to set out their plans for engagement with all customers. Instead we are requiring DNOs to set out their plans for engagement with domestic and small and medium enterprise customers.

We have amended the definition of Direct Benefits. DNOs will not be able to use incentive payments generated as a result of their project during the implementation of their project to cover all or part of the DNO Compulsory Contribution.

We have amended the reporting process for Second Tier projects. We will now publish all project progress reports on our website. DNOs will be able to provide a separate confidential annex, which will not be published.

Representations or objections to this Notice should be made to sam.williams@ofgem.gov.uk on or before Monday 16 April 2011. Responses will be published on Ofgem's website unless marked as confidential.

Yours faithfully,

Andrew Burgess
Associate Partner, Transmission and Distribution Policy
For and on behalf of the Gas and Electricity Markets Authority