



Promoting choice and value
for all gas and electricity customers

April I WG meeting

Agenda

1) Update on Actions from March meeting

2) NIA

- Review the LCN Fund IPR arrangements
- Knowledge transfer (reporting requirements)
- Eligible expenditure
- Internal cost cap

Lunch

3) NIC

- Bid costs
- Policy discussion on evaluation criteria
- Comments on drafting of IPR and Collaboration

4) Any other business

Coffee	10:45-11:00
Lunch	12:00-12:30
Close	14:00

ITEM 1: Actions Update

Actions update

- Update ToR and circulate – COMPLETED
- Circulate LCN Fund document - COMPLETED
- Consider alternative means of funding the NIC
 - We have received limited suggestions from IWG members – we are assessing these.
 - Continued dialogue with DECC colleagues
- Consider contingencies if a NIC cannot be held in 2013
 - Several **suggestions** received from IWG members, these included:
 - Billing local customers for NIC projects
 - Equity for customers, benchmarking impact.
 - Additional allowance for GDNs
 - Regulatory control – scope of spending?
 - Consistency

- Consider how environmental benefits of NIC projects could be assessed
 - Further discussion today
- Case studies of cross sector projects
 - Received
- Confirm scope of NIC
 - Considered internally – limited to projects with Carbon/Environ bens.
- IFI IPR arrangements
 - Meetings with several IWG members
 - Information provided by EIC
 - Further discussion today under first NIA agenda item
- IFI – what works well and where is there room for improvement
 - Regulatory reporting could be better focused (to discuss today)
 - Internal cap a concern for some (to discuss today)

ITEM 2: NIA

Policy Implementation Principles – what are we looking for NIA to achieve?

- Projects that are funded through the NIA should:
 1. Deliver relevant innovative solutions.
 2. Generate knowledge that can be shared amongst licensees.
 3. Deliver value for money to present and future consumers.

Governance Document Structure and Mapping to our Principles for implementing the NIA

<u>Chapter</u>	<u>Contents</u>	<u>Principle</u>	<u>IWG</u>
<u>1. Introduction</u>			
<u>2. NIA Projects</u>	Eligible NIA Projects	1, 2 & 3	22 March
	Registration requirements	2 & 3	22 March
<u>3. Allowable NIA Expenditure</u>	Allowable set up expenditure.	3	Today
	Eligible Project expenditure	3	
<u>4. Reporting for NIA projects & Project Audits</u>	Requirements for Network Innovation Annual Report & Project Audit	1, 2 & 3	Today
<u>6. Knowledge Transfer/ Intellectual Property</u>	Knowledge Transfer	2	Today
	Intellectual Property	2, 3	Today

ITEM 2a: Intellectual Property

Intellectual Property

Context

- We had some initial ad-hoc discussions on IPR and knowledge sharing at the March Working Group. The group identified this as a key area for further work.
- We have since spoken to the EIC and licensees to gain further insights.

Aims for today

- We'll focus top down on what we want to achieve through the NIA – then focus on the role IPR and knowledge sharing arrangements have in achieving our goals.
- We sent you the IPR arrangements for the NIC, which is based on the LCN Fund – we will start by discussing the principles of these arrangements. We hope this provides some context for our discussion on NIA.

LCN Fund

Objective – customers take a share of the risk on innovative projects that help all DNOs understand how they can provide security of supply at value for money in the move to a low carbon economy

Funding – by all customers (Tier 2), by individual DNO's customers (Tier 1)

Why did we introduce IPR arrangements?

- To ensure that parties are unable to restrict effective knowledge dissemination
- Recognise that there could be income from royalties

Principles

- Protect background intellectual property
- Introduced concept of "Relevant IPR" to ensure effective dissemination
- Carve out for commercial products to maintain incentive on collaboration
- Mechanism to return DNO's royalty revenue to customers

NIA

Objective – customers take a share of the risk on innovative projects that may provide improved future outputs or lower future costs

Funding – by individual network's customers

Why are we concerned about IPR arrangements?

- IPR may generate significant financial gain for collaborators:
 - Are consumers due a share in profits?
 - Is there a risk that customers would be paying twice? (ie will the collaborator offer a 'fair' price, given potential strength?)
- Need to ensure effective knowledge dissemination between parties

Discussion

1. How do we ensure customers benefit from innovations that they have funded, or partially funded?
2. Should customers share in profits?
3. Should other companies and their customers get the benefit from any arrangements (discounts etc) negotiated with collaborators through NIA projects?
4. Should knowledge be disseminated from projects which are funded through the NIA?

Looking at the LCN Fund arrangements in this context, do they achieve what is required?

- We note potential issues around lower TRL levels and the definition of “commercial products”
- Other disincentives to innovate or collaborate?

ITEM 2b: Knowledge transfer

Knowledge Transfer - medium

We want to ensure that Relevant Foreground IPR and other learning from NIA projects is shared as effectively as possible

Current

LCN Fund Tier 1 requires close down reports and annual conference
IFI requires an annual report
NIA licence drafting requires an NIA annual report and allows for further requirements

Proposals

LCN Fund review supportive of annual conference – applicable for NIA?
Propose requiring an annual NIA update report – including further detail for project close down. Feedback suggests content review

Questions

What benefits do the IFI annual reports provide, and what could change to provide more effective knowledge dissemination?

NIA larger than Tier 1 - would benefits of an annual conference outweigh costs given the broader range of topics and companies?

Other measures?

ITEM 2c: Project expenditure

Eligible Project Expenditure: issue

NIA is aimed at funding smaller scale innovative projects

- We've put the LCN Fund Tier 2 and NIC in place for large, flagship projects. Due to the scale of consumer funding involved in the projects, there is a significant level of scrutiny through the competitive process, Expert Panel and detailed reporting requirements
- We put the LCN Fund Tier 1 and NIA in place as companies may also need to undertake smaller innovative projects. Because it is smaller scale projects, Ofgem has less involvement
- NIA will provide significant level of total funding – some companies may be able to undertake projects on a similar scale to the NIC using NIA allowance

Eligible Project Expenditure: options

Existing approaches

- Under LCN Fund Tier 1 there is no maximum value of individual projects but projects are limited to three years
- Under IFI there is no cap on length or value of projects

Discussion

What benefits/costs are there in providing a limit to individual project expenditure?

Options

- Could cap annual expenditure/total project expenditure?
- More stringent registration or reporting requirements for larger projects?

But: we recognise that some projects may provide benefits but aren't suitable for NIC.

ITEM 2d: Internal costs

Internal Expenditure

- There is no Internal Expenditure cap in LCN Fund T1
 - However a maximum of 15% of IFI Expenditure can be spent on the internal resources of the licensee - unless the Authority consents otherwise. We think that this:
 - Incentivises collaboration with outside organisations; and
 - Incentivises efficient expenditure by licensees.
-
- Under IFI licensee can seek approval to exceed the internal spend limit. This has only happened in a limited number of cases.
 - But, some have raised the cap as a concern, so want to understand the issue from others' perspective:
 - We want to know what the benefits of removing the cap would be?
 - What evidence is there? For instance, is the ratio of internal external spend for LCN Fund T1 Projects?

ITEM 3: NIC

NIC

- Bid costs
- Detailed evaluation criteria – benefits and scope of innovation
- Governance drafting

ITEM 3a: Bid Preparation Costs

Bid preparation costs

- Consulted in Sept and March on funding bid preparation costs
 - Sept: Should we fund bid costs, is using proportion of NIA appropriate?
 - January: Outlined sliding cap mechanism and cap levels of between 5-10%
- Mixed views from stakeholders – taken some more time to consider options
 - Importance of level playing field
 - Additional complexity of non-RIIO network licensees involvement
- Stakeholder proposal to introduce a fixed cap for all
 - Consider there is clear merit in this approach

Bid preparation costs

- Cap on funding bid costs
 - Range of funding provided for DNOs to prepare Second Tier submissions through First Tier:
 - £260k-£810k (through First Tier Allowable Setup Expenditure)
 - Includes bid prep cost and set-up expenditure
 - Some feedback that this was unfair on single licensees
- Don't think it's reasonable for NIC bid costs to exceed 5% total funding available (~175k per bidding group)

Updated Proposal

- Proposal
 - to cap recovery of bid costs equivalent to 175k of NIA or 5% total funding requested (whichever is smaller)
 - Same bid prep allowance available for non-RIIO network licensees
- Ensuring efficient expenditure
 - Place condition that bid costs only recoverable where licensee passes the ISP
 - Ofgem ability to audit costs and processes to ensure efficient expenditure – reserve right to claw back if not
 - Will review arrangements once competition has started to assess effectiveness

Set-up expenses?

- Funding for bid costs up to cap (just discussed)
 - Internal spend cap on NIA (discussed this morning) – use on a per project basis for set-up of individual projects
- Are there additional costs beyond these?
 - One off expenses not covered by bid costs or internal spend

ITEM 3b: Detailed evaluation criteria - benefits

Background –Evaluation criteria

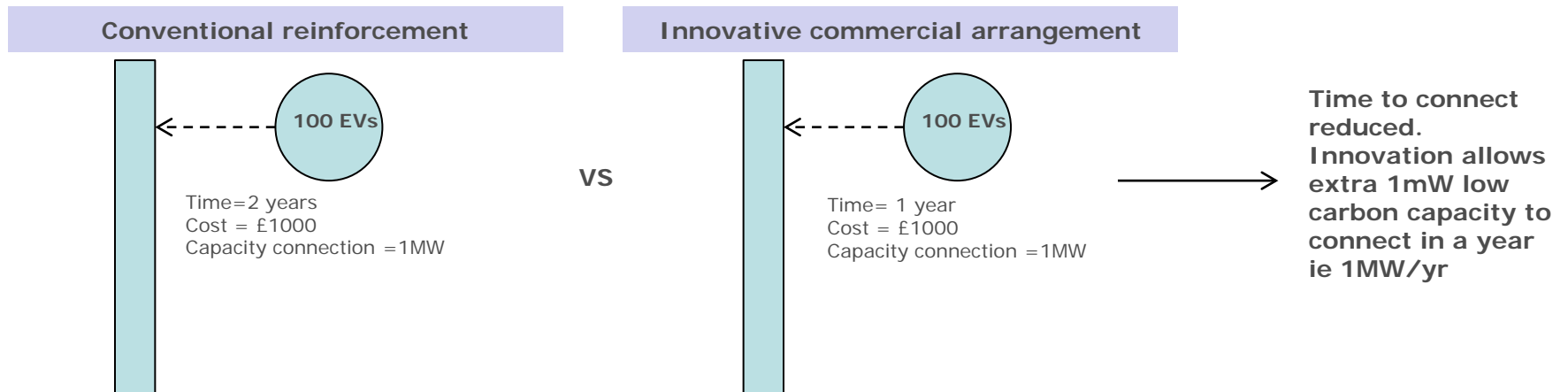
- High level evaluation criteria – set out in March decision
- Our approach to date – follow the LCN Fund unless reason to diverge
- In the case of evaluation of projects there are two potential reasons to diverge from LCN approach, both related to scope of projects
 - Wider “type” of benefits allowed (ie low carbon and environmental)
 - Wider scope of innovation activities allowed (ie not just trialling and demonstration)
- Discussed project benefits at last IWG at a high level

Project benefits

- LCN Fund assess project benefits in a number of ways
 - a) DNOs must qualitatively explain how the proposed project solution makes a contribution to the UK Government's current strategy for reducing GHG emissions
 - b) DNOs must provide an estimate of the network capacity released if the project is successful and how much more quickly it would be released than through the most efficient method currently in use (ie conventional reinforcement)
 - c) DNOs must calculate the potential financial benefits the proposed solution can bring by comparing the most efficient method currently in use against the costs of replicating the project solution if successful

Capacity calculation

- Most LCNF projects will involve facilitating the connection of low carbon technologies onto the network using innovative technological, commercial or operational arrangements as an alternative method to conventional reinforcement
- Capacity of the network can be defined in a number of ways. Here we define it as the capacity of the technologies/generation that connects to a network
- If successful the innovation will release network capacity for low carbon connections either more cheaply or quicker than conventional reinforcement
- This should also be applicable for gas and electricity NIC projects which aim to utilise innovative technological, commercial or operational arrangements as an alternative method to conventional reinforcement for connecting low carbon technologies



Assessing NIC project benefits

- Licensees will need to demonstrate a project delivers:
Carbon and/or environmental benefits and
Net financial benefits
- We propose to ask licensees to demonstrate projects benefits in the following manner:

Carbon

- qualitatively explain how the proposed project solution can make a contribution to the UK Government's current strategy for reducing GHG emissions; and
- estimate how much network capacity will be released if the project is successful and how much quicker;

and/or

Environmental

- qualitatively explain how the proposed project solution provides net environmental benefits to consumers;
- **and**

Financial

- calculate the potential financial benefits the proposed solution can bring by comparing the cost of the current method used against the costs of replicating the project solution if successful

Wider scope of innovation allowed

- Project proposals should be: *"innovative, have an unproven business case and the risk warrants a limited trial, research or development or demonstration project to demonstrate it's effectiveness. Need to demonstrate how current incentives are not sufficient to justify the project"*
- LCNF is focussed primarily on trialling and demonstration projects
 - This means the innovative solutions are typically more developed (ie higher TRL)
- Were considering what information we should ask licensees to provide in order to sufficiently demonstrate this criterion. For instance:
 - Demonstrate why the project is innovative and not viable under BAU ie, the reasons why you would not perform the innovation in its normal course of business or have not attempted to use the solution before including reference to the specific technical, operational, commercial or regulatory risks associated with the project
 - Specify at what point in the "innovation cycle" the project sits and justify this position
 - Demonstrate why the trial, research or development or demonstration project is untested at the scale and circumstance in which the licensees wishes to investigate it
 - Outline why the project is not suitable for NIA funding
 - Outline what new learning will result from the project

What information is required to allow licensees to effectively demonstrate how they meet this criteria?

ITEM 3c: Governance drafting

Governance drafting plan

- As we draft each section of the Governance document we will circulate it to IWG members in advance
- At the moment we have one template for both Gas and Electricity – ease of use when discussing sections, eventually will be separated
- The drafting represents policy decisions we have made following our recent consultations on the NIC
- We will use the text from the LCNF Governance document as a starting point and made changes to make it relevant for the NIC
 - (NB: we circulated the LCNF Governance document to members after the last IWG)
- We are looking for high-level comments on whether you think the drafting represents the policy decisions we have already made
 - Opportunity to provide more detailed comments via email after the meeting

Indicative timetable for drafting

Chapter of document		Date for discussion
Strawman circulated to group for discussion		March IWG
Section A		
Introduction		June IWG
Collaboration		April IWG
Annual competitive process	ISP process	June IWG
	Full Submission Process	June IWG
Section B		
Project Implementation		July IWG
Funding direction		July IWG
IPR		April IWG
Royalties		June IWG

Indicative plan for drafting sections of the document over the coming 3 months

Guide to drafting

- We have populated the collaboration and IPR sections of the document
- We have also began populating the definitions page to aid clarity
- We intend to use the following terms throughout the document:
 - Problem: means the issue that needs to be resolved in order to facilitate the low carbon future or facilitate net environmental benefits to [electricity or gas] network customers,
 - Method: means the proposed way of solving the Problem,
 - Trial: means a limited, controlled and monitored test to demonstrate if the Method works,
 - Project: means the Trial or group of Trials being proposed or undertaken, and
 - Solution: means the outcome if the Problem is solved.

Collaboration

- Collaboration is a key feature of the NIC
 - Licensees should look to collaborate with a range of parties and leverage external funding where possible
 - Stated we will require licensees to set out processes for collaboration at ISP – (this falls within the ISP section of the document)
- March decision document
 - To facilitate collaboration, we expect licensees to maintain and update a collaboration website , where non-network companies can find out information about the NIC, suggest potential projects and contact licensees
- Governance drafting
 - Sets out expectations that licensees will collaborate and facilitate collaboration where possible
 - Sets out expectation that licensees will develop a collaboration website and notes that it may be appropriate to develop current LCNF website to include the NIC as well

We welcome high level comments on the drafting – do you consider the drafting reflects the policy intent?

Intellectual Property Rights

- Knowledge transfer is a key aim of the NICs – benefits from projects maximised if other licensees can utilise learning
 - Want to ensure all licensees have access to IPR material to the dissemination of learning in a given project
- March decision document
 - We will implement the same default IPR arrangements that exist for the LCN Fund
- Default IPR arrangements
 - Relevant Foreground IPR created and material to learning dissemination must be shared royalty free by licensee to other licensees
 - All project participants retain rights to their own background IPR
 - All participants may own all foreground IP it creates independently of the project

We welcome high level comments on the drafting - do you consider the drafting reflects the policy intent?

The background is a composite image. On the left, there are rows of solar panels under a bright sun. On the right, a hand is shown holding a white paper airplane. In the bottom left, a blue gas burner is visible. The overall theme is energy and consumer choice.

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