

Dora Guzeleva,  
Head of Networks Policy: Local Grids  
Ofgem  
9 Millbank  
London  
SW1P 3GE

28 June 2012

Dear Dora,

**Consultation on funding the cost of preparing submissions for the Network Innovation Competition (NIC) and the Governance of the Network Innovation Allowance (NIA)**

Thank you for the opportunity to comment on these proposals.

We welcome Ofgem's decision to allow funding of bid costs and believe the suggested approach of capping the cost at 5% and funding via the NIA is reasonable at the outset of the NIC. We believe there should be a review of the cap based on experience of NIC scheme participants and the quality of bids received. The associated licence drafting should allow flexibility for the cap to be adjusted during RIIO-GD1 following the outcome of this review.

We do feel that there are elements of these proposals that are inhibiting to the overall development of innovation. The specific areas that give us most concern are:

- The need to obtain formal from Ofgem for any project without a positive NPV irrespective of the scale of the project.
- The need to register all projects with Ofgem in advance.
- Continuation of the 15% restriction on internal costs.

Ofgem proposals for all projects to conform to a default IPR position and a requirement to apply for approval for alternative IPR or commercial arrangements may also create significant barriers to small scale innovation. NGN believes that under NIC this default position is appropriate and any alternative can be made as part of the submission. However, under NIA we believe this would create an unnecessary administrative burden on Ofgem, ourselves and significantly on SME partners, who may be dissuaded from bringing innovations to the gas sector for this reason.

Our detailed responses to each of the detailed questions in the consultation are set out in the attached appendix. Please do not hesitate to contact Alec Breen or myself if you wish to discuss any aspect of our response.

Yours sincerely

A handwritten signature in black ink, appearing to read 'S. Parker', written in a cursive style.

**Stephen Parker**  
**Regulation Director**

## APPENDIX

**Question 1: Do you agree with a fixed annual allowance for bid costs for all licensees and an annual cap per bidding group of £175k or 5% of annual NIC funding request, whichever amount is the smaller? If not please provide evidence to justify an alternative level of cap.**

The proposed limits seem reasonable. However, we do not have the same level of knowledge as those companies involved in the Low Carbon Network Funding process. We therefore consider a review of the cap based on experience of NIC scheme participants and the quality of bids received should be carried out during the early years of the NIC. The associated licence drafting should allow flexibility for the cap to be adjusted during RII0-GD1 following the outcome of this review.

Providing a quality bid for any successful project application does take a significant amount of resources and NGN always strives to submit high quality submissions. Should the expert panel require a detailed project plan, with detailed stagegate costs, start date, project manager name and delivery dates then the bid cost could rise significantly, based on the experiences of the DNO's.

**Question 2: We welcome views from stakeholders on whether the funding for bid preparation costs should be funded from the existing funding set aside for funding the NIC, or alternatively, should it be raised in addition to the annual NIA allowance?**

NGN supports the approach of funding for NIC bid costs through the NIA allowance. Given the relative scale of the bid costs to the overall NIC allowance, we believe the funding for bid costs should be from the existing funding set aside for NIC, rather than asking customers for additional monies.

NIA has a clear governance process known to NGN, and it has proven a successful tool to develop project scopes and dependencies. By including the bid submission costs within our NIA annual report visibility will be available to all stakeholders, whether we were successful or not.

In our view it would be a high risk approach to submit a bid if there was no mechanism to recover at least some of the bid costs and this may deter some potential bidders. If a large number of bids were received in any one particular year, this would reduce the level of funding available for the successful bids and may make it difficult to smooth out the issue of funding to the businesses.

**Question 3: Do you agree with the proposed high level eligibility criteria? If you do not agree then please explain why.**

We agree with your proposed high level eligibility criteria.

**Question 4: Do you agree with our proposed approach to funding projects with non-financial benefits? If you do not agree then please explain why.**

The proposed approach of seeking Ofgem approval to include projects in the NIA aimed at non-financial benefits (e.g. safety & environmental performance) does raise some concerns. Within NGN, safety and environment are high priorities for our business and much of our IFI work to date has related to these two areas.

Innovation projects, especially those at the lower Technology Readiness Level (TRL) or those that purely provide knowledge that inform us of which direction to focus innovation, often have negative or no positive NPV. If the networks were required to seek approval for

innovation projects that do not have a positive NPV NGN believes this could result in a significant number of projects requiring approval.

We believe all projects we enter into will have an ultimate positive value to customers, but this value will only be realised on implementation and that level of value can only truly be established during the latter parts of the TRL, trial & demonstration.

The IFI good practice guide, used by the GDN's, has an excellent projects' scoring mechanism that uses a balanced scorecard approach and provides a project score that can be used as a measure of potential value early on in the project's development. We believe this should be utilised to assess the value of the project.

If Ofgem proceeds with this the proposal then the process for approving such projects needs to be clearly set out and be straightforward so this does not prove resource intensive for both Ofgem and the participants. Nor introduce significant delays to delivering projects. We would also suggest that for smaller projects (below £50k) simple notification rather than formal approval is required.

**Question 5: Do you agree with our proposal that licensees should self certify projects against the eligibility criteria? If you do not agree then please explain why.**

Yes we agree licensees should self certify against the eligibility criteria. We have a good understanding and maturity around the eligibility of projects from the existing IFI scheme. With projects reported annually and the ability to audit those reports, eligibility issues can be picked up relatively quickly.

**Question 6: Do you agree with our proposal that licensees should register projects with Ofgem before they begin? If you do not agree then please explain why.**

Whilst we do not have the experience from the tier 1 LCNF it does seem an unnecessary step and we struggle to understand what benefit such registration brings. Therefore we do not agree with this proposal.

Publically reporting projects on an annual basis will provide visibility to all stakeholders throughout the project lifespan.

NGN suggest an amendment to the IFI G85/Good Practice Guide to provide a report on the proposed projects that the network intends to embark on over the forthcoming 12 months. This will give a heads up to all stakeholders should they wish to get involved and will assist in preventing any duplication.

**Question 7: Do you agree that in the three sets of circumstances, described above, licensees should require Ofgem's permission before registering the project? If you do not agree then please explain why.**

We do not agree with the proposal for seeking permission in the circumstances outlined and believe this may hinder or restrict innovation in some areas.

NIA projects are likely to be extremely wide in terms of where in the TRL stages we become involved. SME's have a vested interest in IPR and without this will often retract from the process at a very early stage. NGN proposes that each project identifies how IPR is to be dealt with as part of its project proposal plan and this should clearly state how the customer will benefit from the IPR arrangements where these are not default arrangements.

NGN recognises the concerns of Ofgem and customer regarding payments for innovation between licensees. As a business we believe we can obtain value for customers in sharing knowledge and developing joint innovation projects, without the requirement to obtain permission, removing tiers of administration from the process. NGN would not have any objection to registering, after the initial scoping process, projects with Ofgem and would welcome visibility of others.

Should Ofgem proceed with the proposed approach as stated earlier the process for approving such projects needs to be clearly set out and be straightforward so this does not prove resource intensive for both Ofgem and the participants. Nor introduce significant delays to delivering projects. We would also suggest that for smaller projects (below £50k) simple notification rather than formal approval is required.

**Question 8: Do you agree with our proposal to include an annual cap on internal expenditure? If you do not agree then please explain why.**

No. NGN have now gained significant maturity around IFI and have exceeded its 15% cap over the past two years (10/11 & 11/12). We also foresee that this level is only likely to increase over the next 8 years as more projects come to higher TRL stages.

Internal involvement is critical at the early stages of project development in order that the project strictly meets our requirements. We have now learnt that it also needs constant involvement to ensure the project remains on track, is delivering what was expected and that project drift does not occur.

Significant resources are also required when testing, demonstration and deployment are required. This is where most change programmes fail, as without user buy in and involvement at an early stage, acceptance proves difficult.

**Question 9: What proportion of a licensee's NIA do you consider would be an efficient level of internal expenditure? Please include evidence and justification of your view.**

We agree that the majority of the innovation projects should be undertaken by third parties with significant knowledge of the new area. NGN has no intention of developing in house skills to undertake research or development activities.

However, over the whole lifecycle of a project to a point where a product, service or process is ready for full implementation, we believe a cap of 50% overall internal spend should be applied. If we then find that this cap is being exceeded then it can be considered that licensees are drifting into becoming developers.

**Question 10: What elements of the current IFI annual report work best; and what would you improve to make these reports more effective as knowledge dissemination tools?**

Since developing with ENA the IFI Good Practice Guide, this provides consistent visibility of projects being undertaken by the GDNs. We undertook a great deal of work to produce a document that has proved overall successful in sharing information.

The report is very mechanistic and focuses purely on compliance, spend, risk, collaboration and progress. Sharing knowledge will require a different approach to Project Status Reporting:

- **Purpose of Project**
- **Project Overview**
  - Objectives
  - Aims
  - Timescales
  - Stages
  - Major
- **Current Status Summary**
- **Achieve Successes / Forecast Accomplishment**
- **Internal & External Successes**
- **Risk Review and Summary**
- **Project Metrics**

We should continue the good work undertaken by the R&D Sub Group and develop a sharing template based on best practice with other industrial sectors.

**Question 11: Do you agree with our proposal for sharing the NIA annual reports? In addition, what other means are there of disseminating this learning to all interested parties?**

Yes. In addition, we plan to use the ENA website, our business website which contains an a specific innovation portal containing all our innovation reports.

**Question 12: Would an annual NIA conference be a useful tool for disseminating the knowledge gained from NIA projects? Why?**

Publishing reports is a good method of sharing information within the industry on what projects licensees have been undertaking. From our limited knowledge of the LCN Conference NGN see this as a method of showcasing to stakeholders what the industry has been undertaking on innovation. It is a good mechanism for learning about new ideas in the innovation field from others and is also a good opportunity for those with vested interests in innovation to share best practice. NGN would welcome involvement in this type of sharing.

However, we do not see this as a primary mechanism to share knowledge on specific projects as this is done by practitioners talking and engaging with peers on the ground and "around the van". We believe a "Push / Pull" incentive is required to encourage companies to develop innovative knowledge sharing methods and incentivise licensees to pull ideas from others.

Whilst we recognise that this may have the potential for the fast follower, NGN believes this should be more than offset by the incentivisation on the "push" side of the equation. This would result in those developing the product having the incentive to share and recovering some of the 10% risk element.

**Question 13: Do you agree with our proposals requiring licensees to share the learning from NIA projects? If you do not agree then please explain why.**

Yes we agree that sharing should play a significant role in NIA. However, as mentioned above sharing information and data does not necessarily result in successful deployment.

**Question 14: Do you agree with our proposed approach on IPR?**

NIA is designed for smaller scale and larger numbers of projects which vary significantly in scope. These types of projects also come to us at various stages of technology readiness, addressing a wide degree of industry issues.

With this level of complexity the default IPR approach would, in our opinion, therefore be very restrictive on all collaborative parties if applied on every occasion.

Whilst we recognise that consumers derive significant value from any developed IPR, the vast majority of this value is derived when innovations are implemented. Default IPR for NIA could dissuade SME's from collaborating with the utility sector and therefore consumers missing out on opportunities. In addition, larger know how driven companies may also be reluctant to transfer ownership of developed IPR in the way envisaged by the default arrangements.

NGN will always ensure value is driven out of every innovation in order to benefit customers and we believe that allowing a degree of flexibility on IPR for NIA projects would benefit all stakeholders. We recommend that the IPR arrangements are one change that can be added to the NIA Annual Report to ensure open visibility of how networks are managing these requirements.

**Question 15: Should a carve out for commercial products be included with the default IPR arrangements?**

Again, NGN wishes to work with as many stakeholders as possible but the default IPR position may actually increase the cost to consumers. Having to share the developed product with others on a free and unfettered basis has the potential to drive up the cost of the innovation trial and the cost of the final product to all users.

By allowing negotiation on IPR and open reporting, consumers would be protected against any organisation charging premiums for using new products which have used NIA stimulus to create a commercial item or service. We believe that licensees should demonstrate at least a significant return on investment from any IPR.

**Question 16: Should the carve out be limited to projects focusing on lower technical readiness levels?**

NGN believes that under NIA IPR arrangements should be as flexible as possible and that companies should publish these arrangements to ensure all UK customers benefit and do not pay twice.

**Question 17: If a carve out is provided, should other requirements be placed on the licensee to ensure best value for consumers?**

Our view is that companies should report IPR arrangements annually, but that flexibility of IPR arrangements must be retained.