



Regulation & Commercial

By e-mail
Sam Cope
Ofgem
9 Millbank
London SW1P 3GE

Your ref

Our Ref

Date 28th June 2012

Contact / Extension

Martin Hill
0141 614 1768

Dear Sam

Consultation on funding the cost of preparing submissions for the Network Innovation Competition and the Governance of the Network Innovation Allowance

I am writing to you on behalf of SP Energy Networks in response to the consultation paper issued on 29 May 2012. Our detailed comments are set out in the attachment. We welcome the opportunity to comment on the issues raised.

Please contact me on the above number if there are any queries.

Yours sincerely

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Future Networks Manager
SP Energy Networks

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Attachment – Detailed response by SP Energy Networks

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.

SP Energy Networks response: It is our view that the proposed cap of £175k for bid preparation is too low given our experience of the costs associated with preparing previous LCNF Tier 2 projects. The level of funding that is required is directly linked to the level of preparedness that is required whenever the bid is submitted. Our experiences from the LCNF are that the Expert Panel expects a project proposal which is fully planned out and in a position to be delivered almost immediately. To provide this level of preparedness, a higher cap will be necessary. We have provided an indicative breakdown of the resources required with the preparation of our Tier 2 project for 2011 below.

- 1.5 Full time equivalent staff to prepare the project proposal
- Additional contracted resource to provide expertise in particular areas
- Input from the wider business to ensure buy-in of concept and project is ready to deliver
- Contributions from project partners on an in-kind basis – approximately 1 Full time equivalent across all partners

These costs amounted to approximately £270k, excluding in-kind resourcing from project partners to assist with the development of the proposal.

We would also seek clarification on the cap on a per bidding group basis as it is unclear if this implies a cap per DNO group or per project.

We believe a cap of c.£250k would be more appropriate and would be workable. Including a percentage cap may drive the reverse incentive of a licensee increasing the cost of the project to ensure they receive the appropriate level of funding for their preparation costs, albeit likely that the project would be challenged in terms of value for money by the Expert Panel if this were perceived to be the case.

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 be raised in addition to the annual NIC allowance:

SP Energy Networks response: We believe that separate funding should not be provided in addition to the NIC allowance as this is a further cost which will need to be borne by the customer. As highlighted in our previous response we think a fair method to fund this would be that the non-RIIO licensee may include the bid preparation costs as part of their bid, so that should they be successful they will then be reimbursed for costs incurred. This has the incentive of ensuring value for money as it is a component which will be evaluated by the Expert Panel when they evaluate the project and will provide a strong incentive for the bid proposer to ensure a well justified project proposal. This approach would also limit the risk of projects being developed and expensed from the overall funding available, which are not successful.

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

SP Energy Networks Response: We are in agreement with the high level eligibility criteria that are proposed. However we believe that some of the existing industry wide initiatives such as STP (Strategic Technology Platform) and ScottishPower's network business' sponsorship of academic activity may not fully align with these criteria. In particular, some of the benefits of a research programme may not be fully understood given the nature of the research from the outset. These programmes have however provided immense value to the industry as a whole and we would not like to see any of them being placed at risk under the NIA arrangements. As suggested, an appropriate treatment may be through seeking permission from Ofgem

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

SP Energy Networks response: We agree in principle, however a range of activity does happen at a very small scale related to projects which could fall into this category. We would propose that a financial threshold is placed on projects which need to take this route of c. £200k, below which licensees may use their own discretion but with the understanding that Ofgem may ask for further information should the licensee be seen to be using this mechanism excessively. This is also the case with projects at a low TRL where a small piece of work is required in order to prove the benefits case before a larger investment is made in developing/demonstrating the concept. It is our view that this is in the interest of the customer for us to continue to do this so that the administrative process does not become overly burdensome for the licensee or Ofgem.

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

SP Energy Networks response: Yes, we agree that licensees should self certify as this has been successful under both IFI and LCNF.

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.

SP Energy Networks response: We can understand the principles behind registering projects before they commence but are concerned that this may become onerous. An alternative may be to register projects which are above a financial level (e.g. £200k as suggested in our response to Q4). This process would help to ensure that larger commitments of funds under the NIA are highly visible.

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.

SP Energy Networks response: Yes, we agree that these three circumstances would be appropriate for a licensee to seek permission from Ofgem. We would request that a time is included in the permission to be granted to ensure that it does not create an undue delay in starting the project.

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, and;

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.

SP Energy Networks response (Question 8 and 9): It is our view that a cap of 50% would be reasonable. A lower cap may lead to the wrong behaviours such as the outsourcing of innovation activity which is not of benefit to the licensee and nor would it achieve the overall objectives of the DNO being able to fully adopt the learning. It also needs to be recognised that some projects have a high internal resource requirement to ensure that all internal staff are fully bought in to the project which is where the overall benefits are realised as it moves from a demonstration to a business as usual solution. The development of more commercially based projects is also likely to require a greater intensity of internal resource to develop the appropriate arrangements which has an area that has not been examined in great detail previously.

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?

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?

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

SP Energy Networks response (Questions 10, 11 and 12): Rather than imposing a set criteria around the annual report, we would favour a high level requirement from Ofgem which would require the licensees to revisit the G85 Innovation good practice guide. Rather than prescribing a formal annual report, a high level obligation which required licensees to report on an annual basis would be appropriate with an outcome of the G85 review detailing the most appropriate approach. This obligation would also include identifying the most appropriate means of disseminating learning. We should be cognisant of future developments of industry databases which are currently being developed and new means of disseminating information, rather than being prescriptive regarding the need for an annual conference or use of the ENA portal. Significant work is already being undertaken by the ENA and as part of the SGF WS5 to develop a new project database which covers all of the existing LCNF projects and will have capability to capture future NIA/NIC projects as well as other notable activity from other areas of industry which may be of benefit.

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.

SP Energy Networks response: We fully support this idea as some learning cannot be covered in a conference or report and the most appropriate method is through a bilateral discussion. This approach further supports the need for a higher cap on internal resource spend and the licensees budget for project preparation as this activity would be undertaken by internal resources and may not be attributable to a single NIA project.

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

SP Energy Networks response: We agree in principle with the adoption of default IPR arrangements similar to those for the LCNF. However, it is important that there is flexibility to depart from these arrangements in certain cases with Ofgem's approval.

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

SP Energy networks response: We agree that this is a sensible provision.

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

SP Energy Networks response: We believe a carve out for lower TRL level projects would be appropriate so that separate arrangements do not need to be approved by Ofgem for each project in this category. We recognize that without a carve out there may be a risk that partners are less willing to collaborate on lower TRL projects as the outcome is less certain and the IPR restrictions are more prescriptive. This flexible arrangement has worked for IFI projects to date where appropriate IPR arrangements have been negotiated successfully.

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

SP Energy Networks response: It should be recognised that lower TRL projects will have a greater uncertainty which makes IPR arrangements more difficult to provide a prescriptive IPR arrangement. A high level requirement on licensees to ensure value for money for customers through IPR may be an appropriate approach whereby it is for the licensee to agree the most appropriate solution. This would give the licensee the flexibility to consider various options such as reductions in the future unit cost, royalties based revenue or other solutions as these are likely to depend on the nature of the IPR.