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customer groups and other  
interested parties.

Direct Dial: 020 7901 1851  
Email: [dora.guzeleva@ofgem.gov.uk](mailto:dora.guzeleva@ofgem.gov.uk)

Date: 7 January 2015

## **Consultation on the assessment of benefits from the roll-out of proven innovations through the Innovation Roll-out Mechanism**

The Authority<sup>1</sup> is currently considering how to assess the applications we expect to receive next year under the Innovation Roll-out Mechanism (IRM). Licensees will need to demonstrate that the roll-out of a proven innovation will deliver financial as well as low carbon and/or other environmental benefits for it to be eligible for funding.

In response to this letter we would like transmission and distribution licensees and other interested parties, to consider how licensees should quantify, with a high degree of certainty, the benefits of rolling out a proven innovation under the IRM.

### **The Innovation Roll-out Mechanism**

The IRM is intended to facilitate the roll-out of proven innovations, which will provide long-term value for money to customers, in advance of the next price control period. To qualify roll-outs must deliver carbon and/or environmental benefits. Application will not be accepted where the licensees can roll-out a proven innovation using their existing allowance. We will not approve requests for funding under the IRM where we consider a licensee has already received funding through the price control or where there is an alternative mechanism in the price control that could provide funding for the required investment.

### *Benefits*

The first application window for licensees to make applications to use the IRM opens on 1 May 2015 and closes on 31 May 2015. We will make a decision by 30 September 2015 on whether any applications for funding should be approved. The IRM Licence Condition<sup>2,3,4,5</sup> contains the high level evaluation criteria we will use to assess whether a proposed roll-out should be funded. If implemented proposed roll-outs should deliver carbon benefits and/or other environmental benefits and provide long-term value for money for network customers.

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<sup>1</sup> The terms "the Authority", "we", "us" and "our" are used interchangeably in this letter. The Authority is the Gas and Electricity Markets Authority. Ofgem is the Office of the Authority.

<sup>2</sup> Special Condition 5D of the National Grid Gas Transmission's Gas Transporter Licence.

<sup>3</sup> Special Condition 3D of the Gas Distribution Networks Operators Gas Transporter Licence.

<sup>4</sup> Special Condition 4J of National Grid Electricity Transmission's Electricity Transmission Licence.

<sup>5</sup> Special Condition 6E of Scottish Hydro Electric Transmission and Scottish Power Transmission Limited's Licences.

We may approve applications for funding if we are convinced by the evidence provided in the licensee's application that the roll-out will deliver significant benefits and value for money to network customers.

### *Demonstrating benefits*

To be eligible for funding licensees must be able to demonstrate significant carbon and/or other environmental benefits. We consider that the relevant gas and electricity network licensees should develop a robust methodology to demonstrate these benefits. We will only provide funding for a proposal if a robust methodology (together with appropriate evidence) is used to demonstrate benefits.

We are aware that there is already a framework in place as part of the Network Innovation Competition for assessing some of these benefits, eg carbon benefits. However, for the IRM there should be a higher degree of certainty around the low carbon and/or other environmental and financial benefits of the proposed roll-out.

We invite licensees and other interested parties to propose methodologies that licensees making an application for funding should use when calculating and demonstrating carbon and/or environmental benefits. We also invite licensees and other interested parties to propose how licensees can demonstrate a roll-out will deliver long term value for money to customers.

**Question 1: What methodology should licensees, on the basis of robust evidence, use to demonstrate significant carbon and other environmental benefits of each proposed roll-out? Provide as much detail as practicable.**

**Question 2: How should licensees demonstrate that projects will deliver long term value for money to consumers? Please provide details to support your answer.**

### *Funding the roll-out*

The roll-out of a proven innovation through the IRM should deliver additional and significant benefits for customers. It should not lead to licensees making additional profit or be used to fund activities that are already business as usual or have been funded through the price control. The IRM licence condition makes it clear that proposed roll-outs should not:

- enable the licensee to receive commercial benefits from the roll-out within the remainder of the price control period (for instance, where the roll-out of a proven innovation will lead to benefits from any incentive payments greater than its implementation costs within the price control period); and
- be used to fund any of the business as usual activities of the licensee.

As part of our evaluation we will consider whether a proposed roll-out of an innovation could be implemented through licensees' existing allowances. We will also consider whether there are other mechanisms that could be used to fund the roll-out of the proposed innovation. Where we consider licensees could successfully roll-out a proven innovation without the IRM we will not provide additional funding. Licensees will be required to provide evidence that IRM funding is necessary to fund the roll-out. Where strong supporting evidence is not provided then IRM funding will not be made available.

We will also consider whether a proposed roll-out is seeking funding for something which is already considered business as usual. Where we consider something is business as usual we will not make IRM funding available.

**Question 3: How should licensees demonstrate IRM funding is necessary to fund a roll-out? Please provide details to support your answer.**

**Question 4: How should licensees demonstrate that the proven innovation is not already considered business as usual?**

We would like to develop a consistent framework for measuring the benefits of a project in the assessment of its eligibility for funding under the IRM mechanism.

Responses to this consultation will feed into the development of guidance for licensees to use when developing their submissions for funding under the IRM.

We welcome responses to the questions in this letter by **4 March 2015**. Responses should be sent, preferably by email, to [networks.innovation@ofgem.gov.uk](mailto:networks.innovation@ofgem.gov.uk) or in writing to:

Neil Copeland  
Ofgem - Glasgow  
107 West Regent Street,  
3<sup>rd</sup> Floor,  
Cornerstone,  
Glasgow  
G2 2BA

Unless marked confidential, all responses will be published by placing them on our website. We intend to publish a decision in January next year.

Should you wish to discuss the issues raised in this document, please contact Neil Copeland at [neil.copeland@ofgem.gov.uk](mailto:neil.copeland@ofgem.gov.uk) or on 020 7901 7193.

Yours faithfully,



Dora Guzeleva,  
**Head of Networks Policy: Local Grids**