

Neil Copeland
Ofgem- Glasgow
107 West Regent Street
3rd Floor
Cornerstone
GLASGOW
G2 2BA

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By email only to: networks.innovation@ofgem.gov.uk

Dear Neil

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

Thank you for the opportunity to respond to the above consultation. This letter should be treated as a consolidated response on behalf of UK Power Networks' three distribution licence holding companies: Eastern Power Networks plc, London Power Networks plc, and South Eastern Power Networks plc. Our response is not confidential and can be published via the Ofgem website.

Please find in the appendix to this letter our feedback on the Innovation Roll-out Mechanism (IRM). We look forward to a further consultation from Ofgem post implementation for these sectors so any learning can be built in before the roll-out to the electricity distribution sector.

I hope that you will find our comments helpful. If any part of our response requires further explanation or clarification, please do not hesitate to contact me.

Yours sincerely



Keith Hutton
Head of Regulation, UK Power Networks

Copy Martin Wilcox, Head of Regulation, UK Power Networks
Paul Measday, Regulatory Returns & Compliance Manager, UK Power Networks

Appendix

Question 1: What methodology should licensees, on the basis of robust evidence, use to demonstrate significant and other environmental benefits of each proposed roll-out?

We believe that licensees should use the best practice available at the time and in use by government departments when forming impact assessments to support legislation and/or public policy – we give more concrete examples below.

Secondly, we believe surveys carried out in a similar fashion to previous willingness-to-pay surveys are an example of robust evidence, and elaborate on this below.

Ensuring the scope of discussions is not restricted

It is important that the scope of the Innovation Roll-out Mechanism, whether for the electricity transmission, gas transmission and gas distribution licensees, or the electricity distribution licensee, should not be limited by the most commonly phrased examples (such as electricity transmission towers with a new design which has less visual impact but possibly at an increased cost). As an example, visual amenity in urban settings is equally important as in rural settings but in urban settings, the value is in being able to keep infrastructure hidden. Several local authorities are mandating public realm policy which implicitly places a value on either maintaining utility infrastructure hidden from view or going further and removing existing infrastructure from view¹. Another example is the value that might be generated for the wider GB by DNOs continuing to manage their current and future telecommunications requirements within their existing spectrum allocation. Once again, radio spectrum is not a traded commodity but one with significant value.

We see the role of the Innovation Roll-out Mechanism as the means to address any exogenous benefits which do not have an openly-traded value (in the way that carbon emissions do) or for which an equivalent financial value has not been defined (which it has in the case of safety).

As such, we can imagine that any of the following are examples of exogenous benefits which may need to be quantified in support of an IRM application:

- gross value-added (GVA) enabled by infrastructure investments;
- avoided costs of system balancing, or avoided capacity mechanism payments;
- DG or renewable generation brought forward (if not sufficiently quantified through carbon);
- avoided business disruption/avoided streetworks;
- reduced noise;
- reduced cost of gas-handling (such as SF6) and oil treatment;
- efficient use of the radio frequency spectrum.

In each case, there is government best practice² in the form of the impact assessments³ which were required to support, for example the Traffic Management Act and its introduction in 2004; to support local planning policy; and to support, for example, the Digital Switchover of terrestrial

¹ One example is available at:

http://transact.westminster.gov.uk/docstores/publications_store/Westminster_Way_Public_Realm_Strategy_Adopted_September_2011.pdf

² <https://www.gov.uk/government/collections/impact-assessments-guidance-for-government-departments>

³ <http://www.legislation.gov.uk/ukia?stage=Final>

television signals. We would seek to draw on these examples of best practice. Furthermore we would expect the Airports Commission⁴ to provide further best practice in quantifying gross-value added alongside environmental benefits or impacts.

Stakeholder surveys with stakeholders other than the end customer are valid

There has been an established precedent of using qualitative survey data in the form of willingness-to-pay surveys as robust evidence within price control discussions. We believe that the same approach could be useful in assessing Innovation Roll-out Mechanism applications. In such cases there are likely to be occasions on which the appropriate survey respondents would be government bodies and local authorities rather than network customers themselves and this must be borne in mind.

To provide a practical example, it might be appropriate for a local authority to respond to a consultation on the financial value which they would place on an innovative method to avoid street-works. In this case they would be replying on behalf of particular groups of residents and businesses in their region who might be affected and judging the financial benefit that the innovation would bring. The actual costs of either continuing with business-as-usual without the innovation, or the costs and benefits of rolling out the innovation under the IRM, would ultimately be borne by all customers through Distribution Use of System charges, but the local authority may be better placed to judge its value. Similarly, local authorities may be best placed to judge the financial benefits to an overall region from public realm and planning policy, even though this places a financial burden on customers, developers and utilities such as UK Power Networks in meeting these requirements.

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

We are comfortable with the Cost-Benefit Analysis (CBA) approach which Ofgem mandated for the RIIO-ED1 price control and believe that Ofgem should use this same format in the first instance. In line with our response to question 1, we agree that the burden rests with the licensee applying under the IRM to justify any additional benefit streams or conversion factors above and beyond those currently catered for in the Ofgem CBA approach, for example to account for losses, safety, greenhouse gas emissions and oil leakage.

Question 3: How should licensees demonstrate IRM funding is necessary to fund a roll-out?

We believe that the materiality threshold has already resolved this issue. The materiality threshold means that the DNOs will be bringing forward applications of material size, and therefore are expecting scrutiny.

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

We believe that there may be a role for independent engineering audit to support IRM applications and specifically to address the question of the current state-of-the-art in Great Britain, or as phrased in the licence, what is regarded as having already been subsumed into “Ordinary Business Arrangements”. DNOs are likely to arrange for independent audits where they deem this necessary to demonstrate novelty.

⁴ <https://www.gov.uk/government/organisations/airports-commission>

It may also be useful for Ofgem if an independent organisation were to review the state-of-the-art overseas various different technologies. Ofgem's approach probably should and can be lighter-touch in technology areas in which the GB is evidently leading other countries, and the only remaining distinction is between each DNO's progress through trials of the new technology.