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Dear Neil,

Reviewing the benefits of the Low Carbon Networks Fund and the governance of the Network Innovation Competition and the Network Innovation Allowance

SSEPD welcomes Ofgem's review on the benefits of the Low Carbon Networks Fund (LCNF) and the governance of the Network Innovation Competition (NIC) and the Network Innovation Allowance (NIA). It is important to review the governance arrangements of the innovation funding mechanisms to ensure they remain fit for purpose and encourage licensees to innovate.

Generally speaking, we believe that the innovation funding mechanisms are working well, and we have a number of recommendations which can improve the way these funding mechanisms are governed. We have provided specific comments on individual questions in Appendix I and outlined our recommendations within our responses to these questions.

We hope that this information is helpful. If you have any questions on the information provided, or would like to discuss this further then please do not hesitate to contact me.

Yours sincerely

Sam Torrance

Networks Regulation

Appendix I – Consultation question responses

Question 1: Should we change the NIC and NIA criteria? If so how and why?

SSEPD believe the NIC and NIA governance arrangements are functioning well and the existing criteria is fit for purpose. Over the last year we have seen a significant improvement in the knowledge transfer of NIA projects and an increase in the number of collaborative innovation projects. However, there is still potential to improve the level of knowledge transfer across the energy industry as a whole, in particular greater knowledge transfer between the DNOs and GDNs could be beneficial to improving innovation projects across the industry. We have outlined a couple of areas which we would encourage Ofgem to consider as part of this review:

NIA - Data Protection Strategy (DPS) and Customer Engagement Plans (CEP)

From our experience so far, one area which we believe could be improved is regarding the approval of Data Protection Strategy and Customer Engagement Plans for NIA projects. Currently the NIA governance document stipulates that the licensee must submit to the Authority, *at least two months prior* to initiating any form of engagement with a Relevant Customer OR collecting or using the data. The governance document then also stipulates that the licensee (or project partner) cannot initiate either of these actions without the plan being approved by the Authority. This uncertainty creates an unnecessary risk on the ability to deliver the project and this could potentially lead to significant cash flow impacts on SME project partners. We strongly recommend that Ofgem amends the NIA governance document to provide a guaranteed timescale of response from the Authority to licensee regarding the CEP and DPS.

Change Request Process

The second area which we believe Ofgem can improve is regarding the project change request process. The current process for going through a project change request is difficult and time consuming and can see projects stalling for a number of months whilst Ofgem review the request. Although we can understand the need for Ofgem to undertake a more detailed review of some of the more complex change requests, we would welcome some form of process to allow projects which only require a minor change request to progress whilst we await formal approval. Similar to the delay in gaining approval for the CEP and DPS highlighted above, putting a project on hold whilst Ofgem undertakes its review of a change request can lead to significant impacts on SME project partners. A

further possibility which we would recommend Ofgem to consider for improving the change request process would be to establish some form of 'fast-track' process utilising either a small 'approval panel' or fast-track from process?

Question 2: Should we give more of an indication of where we consider innovation is required or is that inappropriate?

We believe that a careful balance needs to be struck. It would be useful if Ofgem could provide some guidance on the regulatory and wider market priorities as this would provide network licensees with valuable input in deciding on innovation priorities. However, on the other hand, the network licensees are well placed to determine where innovation is required in order to address issues associated with the development of their networks. The feedback and insight which we receive from Ofgem on innovation projects and submissions is very valuable. We recommend that Ofgem should focus its attention on providing positive engagement with the network licensees on the innovation projects as well as providing direction on where it foresees innovation to be required. This direction should be given with an open mind to prevent the risk of hindering innovative thinking.

Question 3: Should the focus of the NIC and NIA be broader and cover the broader energy system?

As we mentioned above, from our experience we feel the NIC and NIA funding mechanisms are working well. However, one potential benefit to the funding mechanisms would be to amend the governance documents in order to allow these funding mechanisms to work alongside other available innovation funding which is available for innovation projects, such as the Scotland Local Energy Challenge Fund (LECF). This fund was launched by the Scottish Government in August 2014 to demonstrate the value and benefit of local community led low carbon energy economies. The LECF aims to support large-scale local low carbon demonstrator projects which show a local energy economy approach linking local energy generation to local energy use. SSEPD have played an active role in the Selection Panel for the LECF and have provided direct support and advice to the projects planned for the SHEPD area.

Question 4: Can we improve the process for deciding on which projects to approve and if so how?

The process seems to be working effectively. However, one recommendation we have is in relation to the follow-up questions we receive from Ofgem. We believe it may be more effective if these were handled through a follow-up clarification call. We believe this would help to progress Ofgem's approval of innovation projects in a more stream-lined and efficient way.

Question 5: How can we improve participation in the NIC?

The NIC process is a very demanding and labour intensive process for network licensees due to the competitive nature of the NIC process and the funds available through this funding mechanism. From our experience in NIC and LCNF tier 2 projects, we strongly recommend that earlier feedback, more engagement from Ofgem and increased opportunities to discuss possible NIC projects would be beneficial and would support network licensees' participation in the NIC process.

As we already outlined in our response to question one above, the change request process for the NIC is a very time consuming process and we would reiterate the recommendations we made in our response to question 1 again as a potential factor for improving the participation in the NIC process.

Question 6: Please comment on your experiences if you have worked with licensees when implementing NIC and NIA projects or when transferring innovation into business as usual.

SSEPD has worked with other network licensees when implementing a number of our innovation projects. As we outlined above, the knowledge transfer between DNOs has improved and the number of collaborative innovation projects has increased. Events such as the LCNF conference have been extremely beneficial for sharing and transferring knowledge and experiences gained from NIC and NIA projects. Also, the GB Smarter Networks Portal developed by the ENA designed to act as a repository for innovative projects has been extremely useful in supporting network licensees with the both internal and external knowledge sharing.

One particular issue we have experienced when working with project partners on innovation projects is around the finance categories for labour (i.e. the contractual or internal labour categories). Staffing changes can occur quite frequently for innovation projects and we would welcome more flexibility between the categories in order to avoid raising a change request.

Question 7: Are there any other issues we and the independent evaluator should consider as part of the review?

The innovation funding mechanisms are operating effectively and we are starting to see some very beneficial projects emerging which will have significant influences on the energy industry, for example our Active Network Management (ANM) and Constraint Managed Zones (CMZ) deployment into Business as Usual.

As we have indicated in our responses to the consultation questions above, there are a number of areas of the governance document which we would recommend should be part of the review, in particular the change request process and the uncertainty surrounding the timescales for gaining approval of the CEPs and DPS.

We would encourage Ofgem and the independent evaluator to focus on the tangible and intangible benefits which are being realised across DNOs as a result of the innovation funding mechanisms. In particular we believe the review should focus on the importance of the useful outputs being delivered as a result of innovation projects and the rolling out of these innovation projects in to business as usual activities.

We also wish to draw attention to the matter of Intellectual Property (IP) Rights as our experience has been that this area leaves room for a range of interpretation. This often introduces delay in progressing worthwhile innovative projects where IP is likely to be created. The effective management of Intellectual Property creation and commercialisation is a complex area and is often a fundamental building block of business value for third party companies such as SMEs. We suggest that the matter of Intellectual Property Rights is reviewed with the intention of making this more clear and facilitating the development of commercial value to the benefit of UK stakeholders. We would welcome the opportunity to discuss this matter in greater detail with Ofgem.

Another area which we would recommend Ofgem and the independent evaluator to consider as part of the review is the mitigation of potential future risks, for example the potential for the future development of electric and hydrogen vehicles.

Question 8: To what extent do you consider that the LCN Fund has succeeded?

We believe the LCNF fund has been very successful, as it has allowed network companies to undertake innovation initiatives which would otherwise have not been trialled. The market is starting

to see the benefits of these projects, with both the regulator and the network companies confident that savings will be materialised already during the current pricing control period, RIIO-ED1.

We have a number of projects which have been funded by the LCNF are delivering real savings and benefits.

Our experience in Active Network Management, ANM, has been adopted by a number of players in the industry and it's continuing to deliver benefits to generators and networks, as well as helping to deliver the carbon plan by facilitating the connection of green generators.

Also, our Constraint Managed Zones initiative has taken learnings from a number of projects, both ours and other DNOs', to utilise flexible solutions in the networks as an alternative to traditional reinforcement. This realises benefits to the customers both in terms of deferral of investment and also on taking advantage of optionality elements of large capital expenditure: CMZ could help us avoid sunk costs in the network and assess the real investment needs once the future energy scenario is clearer.

Our projects also help us prepare for the future: Our I2EV project (also known as "My Electric Avenue") has demonstrated that there could be a number of potential issues in the network if the take up for Electric Vehicles grows faster than anticipated. My Electric Avenue has provided us with the tools to prepare for such a future scenario.

The three examples mentioned above are only a few case studies for the wider benefits achieved to date by the Innovation Stimulus currently available to network licensees.

Question 9: To what extent do we need to continue incentivising innovation by DNOs?

There is an unquestionable need for Ofgem to continue to incentivise innovations by DNOs. The energy industry is moving into a key period of change and with key milestones expected to be delivered in the very near future such as the smart meter roll out and the continuing need for network licenses to adapt to the challenges presented by climate change. It is therefore essential that Ofgem continues to incentivise DNOs to ensure that the benefits of this change are realised and to ensure that we continue to look for ways to improve our network and deliver benefits to customers and wider stakeholders.

Question 10: Are there any other issues we need to consider as part of the LCN Fund benefits review?

Some of the benefits of the innovation funding mechanisms are spread across the whole energy industry, for example our ANM project has delivered significant benefits for generators and wider stakeholders.

There are a number of innovation projects which are being driven by stakeholders, for example our ACCESS project on Community Energy, which is in response to customers' desire to manage their network. The ACCESS project in Mull will match locally generated renewable energy to local energy demand within a Virtual Private Network (VPN). The project will help around 100 Mull homes currently using oil, wood or inefficient electrical heating to upgrade to smart electric heating systems. These heating systems interact with the local renewable generation through the VPN to balance generation and demand. This type of Community Energy initiatives could help to alleviate fuel poverty by reducing the bills of participating residents. The ACCESS commercial model would allow small-scale generation to connect to the network when capacity is at its limit.

The innovation funding mechanisms have opened doors for network licensees to engage with stakeholders, academics, councils and business and really help these parties learn from each other and transfer invaluable knowledge and experience. This demonstrates the invaluable benefits of the innovation funding mechanisms which are extremely difficult to put a value on, however it is crucial that the review takes these into account.