

Electricity Distribution Innovation Roll-out Mechanism submission guidance

This guidance should be used by licensees intending to seek funding under the Electricity Distribution Innovation Roll-out Mechanism	From To Date	Ofgem Licensees 17/02/2016
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1. Introduction

- 1.1. Before applying to use the Innovation Roll-out Mechanism (IRM), licensees should read the IRM provisions set out in Special Condition CRC 3D. If there is any inconsistency between this document and the IRM licence condition relevant to the licensee then the licence condition shall take precedence.
- 1.2. The criteria for assessing applications are set out in Special Condition 3D. All applications must be made by serving a notice on the Authority containing the relevant information as set out in Special Condition 3D of the Licence. This notice may take the form of the pro forma as referred in the pro-forma guidance (paragraph 2.9).
- 1.3. This document is not a governance document and does not carry the weight of the licence. However, where this guidance says the licensee must do something or shall do something then this requirement exists within the licence. Where the guidance says the licensee is expected to do something, we will consider whether it has done so when reaching a decision.
- 1.4. The document is set out as follows:
 - Part 1: Introduction
 - Part 2 Proposing a Relevant Adjustment to Ofgem: Application process – explaining the timings for applications.
 - Part 3: Pro-forma guidance – describing the content that needs to be provided in licensee’s application.
 - Part 4: Award notification – explaining how Ofgem will make its decisions regarding funding.

2. Proposing a Relevant Adjustment¹ to the Authority

- 2.1. The licensee may propose a Relevant Adjustment by providing the Authority with a notice, under Part D of the IRM conditions, during one of two application windows.

For the RIIO-ED1 price control:

- the first application window opens on 1 May 2017 and closes on 31 May 2017; and
- the second application window opens on 1 May 2019 and closes on 31 May 2019.

¹ Capitalised terms in this document are either defined within this document or the relevant licensee’s licence.

- 2.2. The format of the notice may take the form of the pro-forma as referred in paragraph 2.9.
- 2.3. Part B of Special Condition 3D includes the qualifying criteria against which we will assess applications for funding. Any decision taken by the Authority will reflect its assessment of the submission against these criteria. Part 2.8 of this document provides further guidance on how the Authority will assess the licensee's submission(s) against each of the evaluation criteria and the information that should be provided to inform our assessment.
- 2.4. In addition to the criteria set out in part B of the IRM conditions, the notice served by the licensee to the Authority must in all cases include all those other requirements outlined under Part E of the licence condition respectively.
- 2.5. Ofgem may request a preliminary meeting ahead of the submission deadline to discuss the nature of any applications which the licensee is expecting to make.
- 2.6. Ofgem also expects to request meetings with the licensee to discuss the content of its submission(s), and may ask for further supplementary information to be provided. The failure of the licensee to provide adequate information for Ofgem to complete its assessment would result in an application being rejected.
- 2.7. Ofgem will consider appointing consultants to review the application and provide additional evidence to consider in developing a recommendation for the Authority. Any appointed consultants may also request further communication with the licensee regarding the content of submissions.

Pro-forma guidance

- 2.8. Please use the default font (Verdana size 10) when completing the pro-forma. It is up to the licensee to decide how much information to include under each section. The overall length of the submission (including appendices) should be proportional to the overall size of the project portfolio.

Section 1: Application Summary

1.1 Application title

Please give the submission a title for future reference and to distinguish it from any other applications.

1.2 Estimated total cost

This is the amount that the licensee expects to spend on the whole roll-out (innovation roll-out costs must meet the materiality requirement under Appendix 1 of Special Conditions 3D).

A Relevant Adjustment during either or both of the two application windows specified in Part C of Special Conditions 3D.

1.3 Total funding request

This is the amount being requested for funding under the IRM.

1.4 Start date/ end date and date of Relevant Adjustment

The start and end of the project/scheme taking into account the timing and the date from which it is proposed that the Relevant Adjustment would have effect (“the adjustment date”) and the Regulatory Years to which the Relevant Adjustment would apply.

1.5 Application executive summary

This section should outline the issue or improvement that the roll-out is designed to target. It should clearly identify the Proven Innovation and the desired impact.

Section 2: Application Description

Building on the application summary, this section should provide a more detailed high level description of the roll-out. This should be presented in a manner that enables someone with limited experience of energy distribution networks to understand the material, and should focus on:

- The issue or improvement that the roll-out of Proven Innovation will address;
- The Proven Innovation that the licensee plans to roll-out to resolve this issue;
- The expected outcome of the roll-out;
- The criteria that would need to be met to adopt the project approach into normal business and the assessment of these to give an understanding of the viability of the innovation over the long term once funding through the mechanism ends; and
- The ultimate impact of the roll-out on consumers after implementation.

This section should also include a technical description which complements the high level description and provides greater depth at a more expert level.

Section 3: Application business case – why IRM funding is necessary for rollout

The Authority will only provide funding where we are satisfied IRM funding is required to implement the rollout before the next price control review. The licensee should explain why its existing price control allowance will not allow it to implement the proposed rollout without additional IRM funding.

Licensees should also explain why the innovation it proposes to roll out could not have been considered when it developed its original business plan. Licensees should not simply state that the proposed Innovation was not funded within its original plan. Licensees should also explain why, if they have generated a surplus in another area of the business, the IRM is necessary to roll out the proposed solution.

Licensees must present a clear business case justifying the merits of undertaking the roll-out and must set out how it links to changes it wants to make to its business in the long term.

In addition, this section should also include:

- i. An analysis of how the total costs are estimated, and the potential inaccuracies in this figure (supplementary information can be provided in the appendices);
- ii. How the licensee will recover any granted funding through distribution/transmission Use of System charges; and
- iii. How the licensee will ensure that the timing of apportioning these costs will be appropriately reflected in distribution/networks charges and that only costs incurred during the relevant price control period will be recovered.

Section 4: Evaluation Criteria

We set out below in more detail how the Authority will assess the submission against the evaluation criteria. A submission will have to provide sufficient information to convince the Authority that each of the evaluation criteria has been satisfied. There will be a high threshold for the award of any funding, and licensees will need to provide a convincing business case and robust information against each of the below criteria.

The things the Authority will consider will be inclusive of but not limited to the following and licensees will need to demonstrate that the roll-out:

a) Will deliver additional carbon, environmental or any other wider benefits

The Authority will assess whether the application has clearly demonstrated the additional carbon, environmental or wider benefits against the following criteria:

i. Carbon Benefits:

- How the roll-out will make a contribution to the Government's most up to date strategy for reducing greenhouse gas emissions.
- The application should explain how the innovation will facilitate the Government's plan to transition to a low carbon economy and how it will do this. The application should also explain how the innovation will deliver additional benefits in greater volume and/or faster than the most efficient alternative currently in use in GB.
- A qualitative explanation and estimated quantification of the carbon benefits should be included in the application.

Or

ii. Environmental benefits:

- How the roll-out will deliver wider additional environmental benefits to customers. In particular the application should evidence and reference calculations that demonstrate the additional environmental benefits.
- A qualitative explanation and estimated quantification of the environmental benefits should be included in the application.

b) Will provide long-term value for money for energy consumers

The Authority will assess whether the application explains how the scheme provides long term value for energy consumers against the following criteria:

i. Costs & benefits

The licensee should set out an explanation of the business case for the investment. It should include:

- A description of the potential additional benefits that are expected from the innovation. This may also include estimates of the financial returns.
- The timeline expected for these additional benefits to materialise.
- An explanation of the costs of the project over the period.
- Any benchmark information and explain how these affect the parties involved.
- Set out the usage and pricing assumptions that are set out the business case.
- A justification that the scale/cost of the roll-out is appropriate in relation to the additional benefits that are expected to be captured.
- What expected proportion of the additional benefits will accrue to the network operator of the system as opposed to other parts of the energy supply chain, and what evidence has been used to derive the proportion of expected additional benefits.
- Why it is considered that the IRM is the most appropriate source of funding for this project (E.g. compared to the NIA or NIC)?

We expect licensees to submit CBAs to justify all proposed roll-outs. The analysis and evidence provided should be proportionate to the expenditure and Relevant Adjustments proposed.

The benefit of submitting a CBA model is that it assists the Authority in understanding the costs and benefits of a proposal, along with other alternative options that might otherwise be used to deliver the same outputs.

This guidance ensures that licensees employ a consistent framework in line with the latest thinking on how to conduct CBA in a regulated context. Licensees should use the latest version of the RIIO-ED1 CBA Tool and associated guidance² as part of their justification for all proposed roll-outs.

DNOs may choose to carry out a CBA at the following levels:

- Asset category/class
- Project level

At the asset category/class level it may be useful to group CBA analysis where the same/similar characteristics are displayed. Where projects within expenditure categories are homogenous in terms of the costs and benefits involved, we expect these projects to be considered as part of one CBA decision. Schemes where costs and benefits are specific to the scheme or project being proposed, may require consideration under a separate CBA model.

Where CBAs are referenced in the worksheet guidance below, figures for costs and benefits should be derived from an up-to-date version of the DNO's completed RIIO-ED1

² [RIIO-ED1 CBA Tool Guidance](#)

CBA Tool for that particular solution or scheme. CBAs should be undertaken as, and when, any decision support tool would be used for the DNO's own investment purposes or business decisions, for example when making or changing a policy, or when evaluating options for a particular scheme.

Licensees are expected to take reasonable steps to ensure CBAs are kept up to date to account for:

- new or updated information that is materially different from the assumptions in the most recent RIIO-ED1 CBA tool, or
- any other material change to a driver or input in the RIIO-ED1 CBA Tool.

ii. Impact on wider energy operations

- Where applicable, how the roll-out will have an impact on the wider energy system operations. E.g. A detailed description of how the innovation could relieve network constraints.
- The approach to ensure that the business adopts the investment

iii. Ex-post evaluation of the project – How the licensee plan to assess whether the innovation has been successful?

- The process that will be employed to ensure that the roll-out is delivered at a competitive cost.
- Once the roll-out has been implemented, how will it be demonstrated that the innovation has been successful?

c) Will not enable the licensee to receive additional commercial benefits which are greater or equal to the cost of implementing the Proven Innovation

Using the following criteria, evidence detailing why the licensee will not receive any commercial benefits from the innovation.

The licensee must explain:

i. Costs

- The financial impacts on the current scheme, and whether funding will cause greater/lesser costs to be incurred under the current RIIO incentive packages;
- The implications for any other areas of the licensee's businesses;
- The measures the licensee will employ to minimise the possibility of cost overruns or shortfalls resulting in indirect additional benefits;
- How it will ensure that only those costs incurred up to the maximum funding allowance will be passed through to network/ transmission charges;
- The relationship between the total amount requested for funding and the total cost of the roll-out, referencing the above criteria.

ii. Ex-post evaluation of additional commercial benefits

- How the cost that is incurred under the IRM can be managed and reported to Ofgem (for example a separate account that manages funding for each application).

d) Will not be used to fund any of the ordinary business arrangements of the licensee

The Authority will assess whether the licensee has evidenced that roll-out will not fund any ordinary business arrangements and will use the following criteria when making that assessment:

i. Innovation roll-out costs

- An explanation of how roll-out funding will be kept separate from business-as-usual expenditure; and

ii. Ex-post evaluation of funding

- A description of the means by which costs associated with the roll-out and use of any funding will be tracked.

Please note that we also encourage applications to address how the innovation will enhance competition within the market. Information to consider include:

i. Additional benefit to the market

- Explanation of the potential market for the innovation, giving details of the potential size, scope and how this would be realised.
- Provide a description of how competition in this market will evolve as a result of the roll-out of this innovation and any potential arrangements that could limit this.

ii. Ex-post assessment

- Details should be provided on how the licensee will quantify how the innovation has enhanced competition within the market.

Consistent with Special Condition 3D to receive funding for any application, the licensee must also demonstrate that the roll-out:

e) Involves Proven Innovation and warrants limited funding support

The IRM is specifically targeted at the roll-out of Proven Innovations that are not within the Ordinary Business Arrangements of the licensee. The licensee should demonstrate that the Rollout it is seeking funding for is novel, and not within the definition of an Ordinary Business Arrangement. This is to prevent licensees from receiving additional funding for investment that should already be undertaken. When evaluating proposals we will consider any justification and evidence provided by the licensee to the effect that the proposed roll-out does not fall within the definition of an Ordinary Business Arrangement.

The Authority will assess whether the application is for an innovation that is proven and requires limited funding and the following criteria should be followed when providing this evidence:

i. Funding requirement – Ordinary Business Arrangements

- The roll-out is innovative and is not viable under business-as-usual operations within the current RIIO-ED1 price control;
- The roll-out can only be undertaken with the support of the IRM, including reference to the specific risks e.g. commercial, operational, or regulatory associated with the roll-out.

ii. Technology Readiness level – Evidence

The method that will be used to assess whether the innovation is 'proven' is the Technology Readiness Level (TRL) measure as set out in Annex A. Under this measure a proven technology will be classed as TRL 9.

f) is ready to be rolled-out with any funding provided being used in the price control period.

The Authority will assess whether the innovation is ready to be rolled-out and that funding will be for the RIIO price control period based on the following criteria:

i. Project plan

- A detailed project plan including timeframes and evidence that these can be achieved;
- The resources (human, IT etc) that will deliver the roll-out, which should be of a sufficient size and quality to be reasonably expected to ensure its delivery

ii. Risk

- An identification of all appropriate risk mitigation processes, including:
- a risk register;
- risk management and mitigation plans; and
- contingency plans

Section 5: Regulatory issues

Licensees must explain whether it believes the proposed roll out will require;

- a derogation or any other decision (from the Authority) under any relevant licence provision; or
- changes to the regulatory arrangements

In addition, the licensee should also raise any potential negative impacts on customers, and any financial or logistical implications on generators and suppliers that may result from the proposed roll-out. The licensee should also set out any consultations or discussions it has had with customers regarding the roll-out.

Any expected requirement for a derogation or change to regulatory arrangements will be taken into account by the Authority when deciding on whether to approve funding for any applications.

Section 6: Appendices

In the event that technical detail of a type not provided for in the pro-forma is necessary, licensees should submit this in appendices, listing the titles and a very brief summary of the content.

The licensee is free to include any further supplementary information it wishes in the appendices. Below are some examples of what could be included in the appendices:

- Any diagrams to help explain the technical detail of the roll-out;
- A project organogram; and
- Further detail on the methodology that the licensee has used to calculate the costs.

3. Award and Notification

3.1. The Authority's determination of a Relevant Adjustment and determination of revisions to the IRM value are set out under the Part F of Special Condition 3D. The determination by the Authority of revisions to IRM values is set out under Part G of Special Condition 3D.

Appendix A

Technology Readiness Level (TRL)

This is the measure used to assess the maturity of evolving technologies. The TRL measure is graded on a scale from 1 to 9 (see below). The terms 'proven' and 'late stage' are used to refer to innovations that are understood to be at Technology Readiness Level 9.

- TRL 1: Pure research that is theoretical or experimental work undertaken to acquire new scientific or technical knowledge for its own sake rather than directed towards an application
- TRL 2-3: Applied research driven by a desire to broaden scientific and technical knowledge for application on the network, related to an identified problem. It typically includes investigating the underlying foundation of phenomena and observable fact
- TRL 4-6: Development activities with a more commercial application including technology validation and or demonstration in a working environment
- TRL 7-8: Full scale demonstration in a working environment to test and improve technologies so they are ready for commercial deployment
- TRL 9: Application of technology in its final form, i.e. the technology has been proven.