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for energy consumers

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Date: 04/07/2017

Decision on First Tier Portfolio Reward for the Low Carbon Networks Fund

This letter sets out our¹ assessment process and determination of the financial reward for the First Tier Portfolio Reward (FTPR) of the Low Carbon Network Fund (LCNF).

The intent of the LCNF is to enable DNOs to explore and implement innovative and cost effective methods of facilitating the networks' low carbon transition. The FTPR seeks to imitate the commercial and financial benefits of innovation by rewarding DNOs for successful innovation.

It rewards DNOs for demonstrating 'exceptional performance' for their First Tier Projects. The FTPR is not designed to reward companies for successfully delivering their First Tier projects in line with the governance requirements.

On March 2017, we received four Distribution Network Operators (DNOs) submissions for the LCNF FTPR from ENWL, WPD, UKPN and SSE. An Expert Panel reviewed the applications against the reward criteria set out in our Guidance Note² of October 2016 and produced a report recommending those LCNF portfolio applications that should qualify for the FTPR.

The total amount of money available for the FTPR is £15 million. Based upon the Expert Panel's recommendations, we have determined a total reward of £5.5 million across three DNOs.

The Discretionary Reward was dependent upon the extent to which DNOs FTPR applications met and exceeded the reward criteria.

The assessment process

The format of the submissions and the approach used in assessing the FTPR submissions is set out in LCNF Governance Document³ and the Guidance Note.

It requires the Expert Panel to evaluate the FTPR submissions against a list of Discretionary Reward Criteria.

¹ References to "Ofgem", "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.

² <https://www.ofgem.gov.uk/ofgem-publications/104292>

³ <https://www.ofgem.gov.uk/ofgem-publications/94379/lcnfgovdocv7-finalclean-pdf>

The 2016 Guidance Note further elaborates on the Reward Criteria set out in the Governance Document and requires the DNOs to demonstrate exceptional performance of the portfolio against the following criteria:

- A. Degree to which the portfolio has accelerated the development of a low carbon energy sector and has delivered net financial benefits to future and/or existing customers;
- B. Level of investment of the DNO's own money (over and above any compulsory funding) to enable the portfolio of projects to be successfully delivered; and
- C. Level of learning from the portfolio that has been maximised for the good of all DNO customers.

The percentage weighting that has been assigned to each criterion is as follows:

- Criterion A: 80% (£12m potentially available across all DNOs)
- Criterion B: 5% (£0.75m potentially available across all DNOs)
- Criterion C: 15% (£2.2m potentially available across all DNOs)

Following the Expert Panels assessment of the First Tier Portfolio Reports, each submitting DNO was invited to a bi-lateral meeting (May 8-9th 2017) with the Expert Panel to present on its First Tier Portfolio Report as well as answer any supplementary questions from the Expert Panel.

The Expert Panel then reviewed each DNO submission, taking into account the additional information from the bi-lateral meetings, to produce the First Tier Portfolio Reward Recommendation Report, which outlines Expert Panel's recommendations regarding which DNOs it considers eligible to receive a First Tier Portfolio Reward, the reasons for this view and the monetary value of any rewards.

We have considered the First Tier Portfolio Reward Recommendation Report against the Discretionary Reward Criteria and have determined to accept the recommendations of the Expert Panel including the monetary value of the FTPR rewards.

The Expert Panel

The Expert Panel was made up of experts from a range of backgrounds, chosen for their skills and expertise in environment, innovation, engineering and consumer affairs issues. The panel members were:

- Dr Robin Bidwell; Founder of Environmental Resources Management (Chair)
- Sharon Darcy; Associate at Sustainability First
- Professor Nicholas Jenkins; Director of the Institute of Energy within the School of Engineering at Cardiff University.

Summary of Expert Panel's assessment of LCNF FTPR submissions

Based on its evaluation, the Expert Panel produced the First Tier Portfolio Reward Recommendation Report. In the Expert Panel’s assessment as to whether a DNOs’ portfolio of work could be described as exceptional, using the criteria set out in the Guidance Note, they have concluded the following:

Electricity Distribution Network Company	Expert Panel View	Expert Panel Reward Recommendation (£m)
UKPN	<ul style="list-style-type: none"> - The early work on the Hemsby Storage scheme provided a strong basis for learning for subsequent storage projects and the results were well disseminated. - The other three projects all provided useful learning that assisted the integration of Low Carbon Technologies (LCTs) and informed later LCNF and related work. - The Panel considered the dissemination and engagement of stakeholders to have been well constructed and delivered. <p>The Expert Panel concluded that overall the portfolio had provided some valuable learning to the industry, however it did not consider it had demonstrated exceptional performance against the assessment criteria.</p>	No reward
ENWL	<ul style="list-style-type: none"> - ENWL’s submission demonstrates a well-constructed and well managed portfolio largely focussed on some real network problems that were a potential barrier to LCT roll out. - There were significant outcomes both in terms of products (resulting from exceptional supplier collaboration) and changes in network practices. - The dissemination to other DNOs, academics and the wider industry was well carried through. - The results of the work had the potential to offer cost savings to customers. <p>The Expert Panel concluded that the portfolio included innovative work, providing valuable outcomes to the industry, and the results were extensively disseminated. ENWL’s portfolio was considered to have provided a significant contribution and, as such, the Expert Panel has recommend a First-Tier portfolio reward.</p>	£1.75m

WPD	<ul style="list-style-type: none"> - WPD's extensive portfolio was well focused and addressed issues that enabled new solutions and operational changes in practices to be developed. - WPD had addressed some issues that have been less well examined by DNOs elsewhere: in particular, engaging with communities to find local solutions. - There was a strong emphasis on effective communication to other DNOs and the wider industry. <p>The Expert Panel concluded that WPD's portfolio was considered to have provided a significant contribution and, as such, the Expert Panel has recommend a First-Tier portfolio reward</p>	£1.75m
SSEN	<ul style="list-style-type: none"> - SSEN presented a comprehensive and well-constructed portfolio that addressed a number of fundamental barriers to the Carbon Plan. As a result it should be possible for a considerable increase in other LCTs (domestic and commercial) to connect onto the network without the need for reinforcement; - Their work on Demand Side Management (including their work on electric vehicles) has also provided valuable learning on how domestic equipment and vehicles can be used to avoid capacity constraints from peak loading; - The work undertaken by SSEN (along with similar work by other DNOs) will provide considerable benefits to customers; - SSEN have made a strong effort to fully disseminate the results of their work. <p>The Expert Panel considered that the Tier 1 projects had made a significant contribution to the Carbon Plan and would create considerable financial benefits to customers; and on that basis, the Expert Panel recommend that SSEN should receive a Tier 1 reward.</p>	£2m

Ofgem determination on financial rewards for the DNOs

Having consulted with the Expert Panel and reviewed the First Tier Portfolio Reward Recommendation Report, we have decided to accept the Expert Panel's reward recommendation and have determined a total financial reward of £5.5m across three DNO groups (£1.75m for ENWL, £1.75m for WPD and £2m for SSEN).

The table below shows the allocation of the financial reward between each DNO group's licenses.

DNO Group	Licensee	Reward (£m – 2017/18)
Electricity North West Limited (ENWL)	ENWL	1.75
Western Power Distribution (WPD)	WPD West Midlands plc (WMID)	0.4375
	WPD East Midlands plc (EMID)	0.4375
	WPD South Wales plc (SWALES)	0.4375
	WPD South West plc (SWEST)	0.4375
Scottish and Southern Electricity Networks (SSEN)	SSE Scottish Hydro (SSEH)	1.00
	SSE Southern Electric (SSES)	1.00

Next steps

As outlined in the Electricity Distribution Licence (paragraph 2J.3 of CRC 2J), Ofgem will issue a direction (the Funding Direction) that will set the recoverable value for each licensee in December 2017.

If you have any queries about this letter please contact Kelvin Hui at Kelvin.Hui@Ofgem.gov.uk or on 0207 901 7185.

Yours faithfully,



Geoff Randall

**Associate Partner
RIIO Networks**