

SLR Industry Codes Workgroup

Meeting 3, 19 January 2006

Minutes

Attendees:

Ian Anthony (Chair)	Ofgem	IA
Jill Ashby	Gemserv	JA
Roger Barnard	EDF Energy	RB
Dorcas Batstone	Elexon	DB
Jonathan Dixon	Ofgem	JD
Mark Duffield	National Grid	MD
David Edward	Ofgem	DE
Steven Eyre	British Energy	SE
Paul Finch	nPower	PF
Emily Hamilton	Ofgem	EH
John Lang	Centrica	JL
Samantha McEwen	Ofgem	SM
Clover Powell	energywatch	CP
Nicholas Rubin (Secretary)	Ofgem	NR
Abid Sheikh	energywatch	AS
John Sykes	SSE	JS
Alex Travell	E.ON	AT
Mark Watson	ERA	MW

Apologies:

Emma Carr	National Grid	EC
Alex Mackinnon	Scottish Power	AM

Introduction, Minutes and Outstanding Actions

1. IA welcomed the Industry Codes Workgroup (the Group) to its third meeting. The members of the Group were introduced. Apologies were received from EC and AM.

2. All outstanding actions were closed.

ACTION - MW agreed to present his research on the Civil Aviation Authority at the Group's next meeting.

3. The Group agreed the previous meeting's minutes.

Straw-man options

Model 1 – "Enforcement by Invitation model"

4. PF and RB introduced Model 1 (see paper 03/01).

5. PF explained that, following legal counsel, nPower had revised their previous proposal of a purely self-governing regime in favour of having an enforcement role for Ofgem on invitation from code panels and in predetermined circumstances. Consequently he and RB

had collaborated to develop Model 1. PF also said that Model 1 would remove the opportunity for 'double jeopardy' and was based on the principles of Better Regulation.

6. RB added that Model 1 would allow industry codes to "walk tall" in their enforcement functions. He considered that current regulatory compliance and enforcement arrangements do not encourage industry codes to develop their own arrangements. He drew the Group's attention to the proposed illustrative legal drafting.

7. The Group was invited to comment on Ofgem's written response to Model 1 (see paper 03/02). The paper considered four elements to the proposed model: double jeopardy, enforcement by invitation, enforcement in pre-determined areas, and the illustrative legal drafting.

Double jeopardy

8. Model 1 intends to address an aspect of the current enforcement arrangements that at the same time that a party is in breach of a code's arrangements it is also in breach of its licence. In such a case that party may be subject to simultaneous enforcement action both under the code and by Ofgem – double jeopardy – with the outcomes being independent of each other.

9. PF pointed out that the need to prescribe Ofgem's role is based on the potential for Ofgem to intervene in enforcement issues at its own discretion. RB re-iterated this point. On the other hand, CP and DE noted that Ofgem refrains from becoming involved in enforcement issues until self governance enforcement measures are exhausted. The Group noted the point in Ofgem's paper that, to date, a case of double jeopardy has not arisen in relation to enforcement of code compliance. However, it was noted that the arrangements do not preclude this and RB suggested that this policy decision not to intervene was less important than the fact that the legal powers enabled Ofgem to do so. JS reminded the Group that Ofgem has in the past taken action with regard to Transfer Objections without awaiting the results of any potential self governance measures.

10. RB pointed out to the group that the possibility of double jeopardy was undesirable, for the most part, as a point of legal principle. The group's discussions turned to consideration of Ofgem's role in enforcement and the proposal that this should only be initiated at the invitation from industry code panels.

Enforcement by invitation

11. AS pointed out that Ofgem has a number of statutory duties and that to fulfil these it must be able to take proportionate action wherever a material breach is determined to have occurred. DE added that Ofgem should be mindful of being proportionate when taking enforcement action. AS reminded the Group that Ofgem's decisions can be challenged by Judicial Review. RB said that it is widely recognised that the Judicial Review process is not without its difficulties.

12. JL said that the cost of Ofgem performing investigations into code breaches is high both internally and externally and that this kind of regulatory burden is what the SLR is seeking to reduce.

13. The Group broadly agreed that industry codes are likely to need their enforcement arrangements strengthened if Ofgem's role were to be limited to invitation only. Some members thought that industry codes would need to be modified before a licence change was made. Others thought that a leap of faith was required and that licences should be changed first so that industry codes would have the opportunity to develop enforcement arrangements accordingly. It was noted that the manner by which licences and industry

codes were changed was an implementation issue which would need full consideration should this proposal be adopted.

14. AS commented that Model 1 would not necessarily cause risks and uncertainties to decrease. Instead, risks related to regulatory involvement would be shifted to industry codes.

15. The Ofgem paper set out a number of concerns which the Group was invited to consider. These related to features that effective self-compliance arrangements should have.

16. Concern 1 related to the competence and independence that would be required of code panels. The Group acknowledged that these issues would need to be considered in proposed enhancements to industry self-governance and noted that certain code panels already carry out code enforcement activities.

17. Concern 2 was that industry code compliance arrangements should have a suitable appeals mechanism. This idea was broadly supported by the group, although some had reservations about Ofgem fulfilling such a role. It was noted that Ofgem would not necessarily need to be the appeal-hearing body. AS asked whether such a mechanism would consider substantive or process issues. RB and JS suggested that a robust appeals mechanism would probably consider both.

18. The Group discussed Concern 3 – Ofgem's comments on consistency between licence types. AT suggested that all licence types could be harmonised so that all industry participants had similar obligations. However JD reminded the Group that changes to other licences would need to recognise the differences between the licensable activities.

19. Concerns 4 and 6 suggested that escalation and compliance sanctions should have objective triggers and those sanctions should escalate proportionately according to the severity of the offence. The Group agreed with these principles.

20. Concern 5 related to the treatment of non-code participants and the requirement that careful consideration should be given to non-compliances that may affect them. Some members of the group supported this idea and suggested that, should codes become more self governed, code objectives could be updated to reflect these additional considerations. RB reminded the Group that some codes already allow energywatch to represent non-code parties at code panel meetings and to initiate code modifications.

21. At present Ofgem has powers under the Competition Act. Ofgem's Concern 7 related to whether Model 1, in reducing the role of Ofgem in enforcing compliance, might lead to code panels becoming more exposed to wider competition considerations or legislation. EH pointed out that Ofgem considers competition issues as one aspect of its primary duties, and carries out its role under the Competition Act as a separate function. RB considered that Ofgem, in its enforcement of code compliance, was doing so as a sectoral regulator rather than a competition authority. In general the Group did not feel that this would be an issue for code panels.

Enforcement in pre-determined areas

22. The Group considered Ofgem's concerns with regard to restricting its enforcement involvement to predetermined areas of industry codes. As opposed to taking an interest in all aspects of code compliance, PF explained that predetermining the areas in which Ofgem could become involved would assist Ofgem to focus on areas of particular interest or relevance.

23. RB said he sympathised with Ofgem's concerns given that it is very hard to determine what a customer facing issue is, now and in the future. AS added that in order to account for changing perspectives/interests, any model would need to be flexible enough to capture changes in attitude. PF considered that the identification of appropriate pre-determined areas could potentially be done without significant difficulty. He, together with RB, agreed to consider these pre-determined areas in more detail.

ACTION – RB and PF to revise Model 1 to consider the comments made by Ofgem in paper 03/02 and the Group.

Illustrative legal drafting

24. In paper 03/02, Ofgem noted that the current obligations that relate to the various industry codes are not necessarily consistent and that a more complex treatment of them may be required if the differences are to be maintained in any new licence condition. It was noted that the illustrative drafting proposes to standardise a number of existing SLCs and obligations. RB suggested that the reason for differences between SLCs and their obligations may have been the result of the circumstances and time in which they were devised. MD pointed out that the industry codes themselves vary in their level of sophistication and detail. Therefore careful consideration should be given to the individual nature of codes when determining whether each of these different obligations should be retained, removed or redrafted.

Model 2 – “Shipper licence model”

25. The Group considered whether a licence obligation similar to that found in SLC 3 of the Shipper Licence could apply generally to the industry codes. This would not require compliance with all aspects of codes but could, for example, require licensees not to prejudice or undermine the objectives of industry codes.

26. AT said that the SLC 3 of the Shipper Licence has been hard to enforce in the past. JL suggested that the Group consider previous enforcement work in relation to this condition, such as the St Fergus and Bacton Investigation performed by Ofgas in 1999¹. RB stated that the real difficulty in enforcing shipper SLC 3 was the need (unique to this licence) to ascertain and prove the licensee's state of mind (i.e. intent)

ACTION – Ofgem to research examples of previous enforcement of Shipper SLC 3.

26. It was noted that because the Network Code is a bi-lateral agreement between transporters and shippers the need to sign and comply may not be necessary. The same was not true of other industry codes.

27. RB said that whilst Model 1 may constitute an effective long term position, Model 2 may be neater and quicker to implement. He also said that although Model 2 would not remove the opportunity for 'double jeopardy', it would increase the burden of proof required before Ofgem could become involved in any enforcement issue. Consequently the Group expressed an interest in exploring in more detail how Model 2 might work.

It was questioned whether a licence obligation on this model would provide greater clarity or certainty about Ofgem's role and the point at which regulatory enforcement action might be triggered. It was suggested that clarity could be brought by the wording of the

¹ The investigation was into events at the St Fergus and Bacton entry terminals to the National Gas Transmission System (NTS). In particular the investigation related to the levels of available capacity being offered by Transco on its system and the nominations being made by shippers.

obligation by including, for example, references to code breaches or rebuttable presumptions.

ACTION – EH and RB to prepare a more detailed straw-man Model 2. Consideration should be given to the comments made by Ofgem, in paper 03/02, and the Group.

28. JD suggested that the reason for Shipper SLC 3 being quite stark may be that many of the obligations that govern the Network Codes can be found in Gas Transporters' Licences.

Model 3 – “Single condition model”

29. The Group noted the aims of Model 3, ie consolidating SLCs into one condition and therefore reducing the physical size of the Licence. It was also noted that this would not change the nature of any of the obligations and that the other proposals would achieve similar aims. It was decided not to progress this model, on its own, any further.

Additional obligations

30. IA brought the Group's attention to paper 03/04. He explained that so far the Group had primarily considered the obligations to sign and comply with industry codes. It has yet to consider the additional obligations that exist within the various SLCs set out in the Group's ToR, for example with regard to NETA and BETTA. These additional obligations will need to be considered as models are developed further.

The next meeting will be held at 10.30 am on 17 February at Ofgem's offices.