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Dear Mark

Review of industry code governance

We welcome the opportunity to respond to the open letter regarding the scope of the review of industry code governance on behalf of National Grid Electricity Transmission (NGET) and National Grid Gas (NGG). NGET owns the electricity transmission system in England and Wales and is the GB System Operator. We are responsible for administering the electricity Connection and Use of System Code, the Grid Code and the System Operator – Transmission Owner Code. NGG owns and operates the Gas Transmission System and also owns four of the Gas Distribution Networks. In association with the three other gas Distribution Network Operators we also jointly provide for the administration of the Uniform Network Code (UNC) Governance arrangements via the Joint Office of Gas Transporters.

Is it time to look again at the effectiveness of code governance?

We agree that now is an appropriate time to review the effectiveness of code governance in light of recent statutory changes and to ensure code governance is aligned with Ofgem's decision making criteria. National Grid supports the desired outcome of the review; to see the industry codes develop in a way that will better protect the consumer interest and promote effective competition whilst addressing the changes to the wider statutory framework.

Additionally, we agree with Ofgem's aspirations for an effective code governance regime as described in the open letter and going forward we consider that these aspirations should be used as the assessment criteria for the review:

- promote inclusive, accessible and effective consultation;
- be governed by transparent and easily understood roles & processes;
- be administered in an independent and objective fashion;
- provide rigorous and high quality analysis of the case for and against proposed changes;
- be cost effective;
- contain rules and processes that are sufficiently flexible to circumstances that they will always allow for efficient change management; and
- be delivered in a manner that results in a proportionate regulatory burden.

We believe the issues outlined within the open letter should fall within the scope of a review and addressing these issues over time should allow industry participants to identify whether improvements can and should be made to the existing governance regimes in gas and electricity.

We understand the difficulties that the scale of the industry and governance arrangements present to small players and the gas and electricity industries by their nature are complex. We believe there is information and support for all parties, including smaller players, on how changes to the various “codes” can be progressed and indeed we often provide direct support in this area when asked. However, we consider there may be some room for improvement and application of best practice and this should be examined by the review.

Critical analysis of modification proposals

National Grid agrees that the critical analysis of modification proposals should form a major component of the review since quality detailed analysis is beneficial to the decision making process. Clarification of who is primarily responsible for the development and analytical assessment of a proposal and subsequently what is expected of those in a secondary role would be helpful.

We consider that the onus lies on the proposer to demonstrate how, and to what extent, their proposal facilitates the relevant objectives and to ensure that the scope of the proposal is clearly articulated. This will ensure time is not wasted at the industry discussion and development stage clarifying or defining the scope rather than understanding and/or challenging the results of any analysis. However, as mentioned earlier, the current governance arrangements do offer support to all parties, including smaller players in the development of their proposals prior to submission. This assistance is particularly beneficial where the proposer does not have access to all of the required data to undertake their own analysis.

It should also be noted there is often a conflict between providing detailed analysis in terms of timeliness of any governance process and the cost and consequently a balance needs to be found. This is especially the case when “urgent” processes are requested and granted. Our view is that the urgent processes are (and will continue to be) necessary but may need to be reviewed in order to ensure that there is sufficient time to develop the proposal and undertake the supporting analysis. In addition, it may be beneficial to consider the development of a process for prioritising proposals to allow sufficient industry time to be given to more pressing proposals. Also given the introduction of the “user pays principle” as part of the current Gas Distribution Price Control Review in relation to UNC developments, it would be useful if the review clarified who would be responsible for the costs incurred in completing the detailed analysis required to support a modification proposal, for example where the GT is asked by the proposer to assist in the demonstration of the potential benefits of a Modification, through an assessment of IT system impacts and the production of cost estimates. We also believe the review should include how the governance processes should account for the need to determine how, and from whom, the IS implementation costs will be recovered.

The relevance of code objectives – are they still fit for purpose?

We would accept that the gas and electricity industries and wider statutory frameworks have changed since the various code relevant objectives were originally developed and we appreciate the necessarily close interaction between these objectives and the code provisions. Consequently, it may be opportune to consider whether or not it is appropriate to supplement the existing relevant objectives to reflect not only Ofgem’s wider statutory duties but also other influencing factors, such as developments to the regulatory regime in Europe. Any revision to the relevant objectives would require, at least, a change to the licences of the relevant industry participants from which the objectives are derived under a statutory process. We therefore look forward to working with Ofgem and the industry to ensure appropriate objectives are maintained.

If this issue is taken forward as part of this review we believe that any deliberations on the introduction of new objectives should include careful consideration of the interplay with the existing objectives. For example, the introduction of an objective to promote sustainable development could potentially conflict with our existing objectives, particularly as our licences currently emphasise operating our systems in a co-ordinated, economic and efficient manner. Consequently we consider that such issues should also be included within the scope of the review, if relevant objectives are within its scope, to ensure further complexity is not created in the assessment process.

Charging Methodologies

We remain to be convinced of the benefits of including the various Charging Methodologies within the scope of the review. We believe that the Charging Methodologies should be developed by the network owners to ensure the fulfilment of their licence obligations and relevant methodology objectives enshrined within those licences. In our view we consider that the current Charging Methodology governance processes are robust, transparent, open to all industry parties and are broadly in line with the assessment criteria for this review. For example, in both Transmission (Gas and Electricity) and Distribution, industry forums have been established where any interested party can attend to express their views, suggestions and or concerns. If there is consensus that an issue needs further development a discussion paper is produced to which industry parties are invited to respond, prior to any formal consultation process and subsequent submission to Ofgem.

We agree that the Charging Methodologies have broad impacts on the market however we have concerns in allowing market participants to propose modifications to the Charging Methodologies and foresee potential issues such as modifications which are raised within year that impact upon charges which are typically set annually. In addition, we also foresee practical and timing issues, particularly if the volume of modifications to the Charging Methodologies increased due to such a change.

Other issues

We believe that the following issues should also be included in the project scope:

- We are concerned with the issue of the development of large scale and/or broad changes which cut across two or more industry codes and licences, such as DN Sales and Access reform. The associated governance arrangements that work well for assessing incremental changes and/or discreet packaged changes can start to struggle to accommodate and take account of such wider complications or fundamental changes. In the future a more flexible framework may be appropriate which can adapt to increasing complexities and external influences such as developments to the regulatory regime in Europe. Consequently, we believe that the need for codes to have the ability to consider cross functional issues and / or implement wider/wholesale industry projects should also form a major part of the scope of this review.
- Urgent modification process in the UNC - the current process can lead to underdeveloped and ill-defined proposals being issued for consultation and ultimately to Ofgem for a decision. Whilst retaining the beneficial flexibility of the current Urgency process we believe that the judicious application of some key governance steps would serve to reduce the inefficiency associated with inadequately defined proposals being presented to Ofgem for a decision.
- Clarification and guidance regarding Ofgem's role in relation to the development of proposals in the modification process and specifically in relation to its role in facilitating the effective and efficient undertaking of the governance processes. Additionally, increased transparency surrounding Ofgem's decision making process will provide the industry parties with a better insight into the reasoning behind decisions and would subsequently lead to provision of supporting evidence that aligns closer to that required by the Authority. With this in mind we believe that the recently published Ofgem consultation "Proposed revised guidance on impact assessments (Ref: 301/07)" should also be included within the scope of this review. The guidance document is seeking views on similar issues to those raised within the open letter, such as adopting best regulatory practice and cost-benefit analysis (including the valuing of carbon emissions). We agree with Ofgem that impact assessments are an integral part of the policy development and the decision making process and therefore they need to be consistent with earlier aspects of the change process.
- Consideration of appropriate self governance for 'lower grade' modifications (such as operational issues) through application of best practice from the UNC and the Distribution Connection and Use of System Agreement (DCUSA).

We believe that the other issues indicated in the open letter are valid issues to be considered by the review and developments should be made where possible in line with Ofgem's aspirations but are less of a priority compared to the main issues discussed earlier and the issues stated above. We also believe that the Panel structures are broadly correct and Ofgem and the Panels should ensure that their current roles, responsibilities and powers are fully understood by all involved and are being fully and correctly utilised.

In summary, National Grid suggests that the main focus of the review should be:

1. Critical and timely analysis of modification proposals – both benefits and costs;
2. An assessment of the continued relevance of the current code relevant objectives;
3. Governance and management of the implementation of cross industry code / licence and wider / wholesale industry changes; and
4. Clarification regarding Ofgem's role in the code governance process.

If you wish to discuss this further or have any queries please contact me, Chris Bennett on 01926 655949 or Phil Lawton on 01926 656448.

Yours sincerely

[By e-mail]

Paul Whittaker