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Review of Industry code Governance

Dear Mark,

Thank you for the opportunity to comment on your letter regarding a “Review of Industry Code Governance”.

The present structure of governance for ‘Industry Codes’ was born out of the New Electricity Trading Arrangements (NETA) and has been developed and refined over time with the addition of new codes. We would strongly make the point that these arrangements have not failed the industry, far from it, we have one of the most robust energy systems in the world, with a diversity of players that we should be proud of. The governance arrangements has played no small part in delivering this, so our initial view of the ‘Review of Industry code governance’ is that, we welcome it but would not expect significant changes to a regime that has and is delivering the benefits described above.

We would also make the point that we operate in a complex industry which at times requires complex rules. We are supportive of reducing complexity and increasing transparency but only where doing so brings clear benefits to the industry and customers it serves.

As regards your comments regarding smaller players; we welcome smaller players and the benefits they bring but do not advocate favouring one segment over another.

We are not supportive of including environmental objectives within industry codes, we would argue that the addition of such objectives would add to the complexity of decision making at a level that would not be appropriate.

We have structured our more detailed comments under the headings used in your letter.

Effectiveness of Code Governance

The code governance structures and processes appear to “work” better for some codes and less so for others. Understanding the differences in the various processes would provide a view across the codes as to which process components are advantageous and which ones are more likely to hinder efficient and effective code

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governance. This analysis should then help to form a view of best practice.

There have been instances where codes and agreements have not worked well together where a change has crossed code boundaries; it is true to say that this has not been the case for all change requests. There may be benefits at looking at this area more closely but we recognise this in itself is a significant piece of work.

The review could also consider;

- The scope and extent of the Code arrangements - each code requires clear definition as to its role in terms of industry arrangements.
- The time taken to assess modification proposals - in this context there may be certain changes which can be expedited while others require more detailed consideration and assessment. It would be helpful if the modification process enabled the code administrator and Panel to fast track certain low impact changes while other more significant changes can be subject to a longer assessment process.

Critical analysis of modification proposals

Modifications proposals can vary in the quality of the initial description and supporting analysis provided. We believe that the development of robust modification proposals is an important stage in the process which should be subject to a more rigorous process, perhaps some form of a formal pre-submission review. An example of where we believe this works well is the Grid Code Review Panel where draft proposals are discussed and formed into firm proposals or withdrawn.

The ability to have the option of withdrawing a modification seems sensible and worth exploring further, there would need to be a process in place that detailed when and how this could be done.

Ofgem's role within the different code groups varies from one of active participation to one of merely being an observer. An example of where this seems to work well is the Grid Code Review Panel where there is active discussion from all parties early on in the process. We understand that Ofgem does not want to fetter its discretion when it comes to making a decision, but a clearly defined role early on in the process may lead to a more efficient result.

We do not entirely agree with Ofgem's comments regarding the quality and depth of analysis provided. The industry has at times provided much in depth analysis as was the case during gas exit reform. However, it was unclear as to the status of this evidence when it came to the final decision¹. In this context we welcome the publication of guidance on the conduct of impact assessments by Ofgem which we believe should take into account objective evidence submitted during the assessment processes.

The review could also consider;

- The role of working groups in modification assessment and definition - working groups are an important element in delivering modification proposals and the role of such groups requires clear and consistent definition. In addition, the role of working group members requires consideration, in particular as to whether members are code "experts" or party representatives.
- The expected content of working group reports - given the increased emphasis on impact assessment the expected content of working group and change reports requires consideration.

¹ We note that Ofgem state in the "Revised Guidance on Impact Assessments", Ofgem, December 2007, paragraph 5.12 that "Ofgem will, however, expect views to be substantiated with firm evidence. We will carefully assess any representations we receive because the possibility exists that parties opposed to a particular policy option might exaggerate their view of the cost or downplay the potential benefits (and the reverse might occur if they support it)".

- The use of “expert resources” such as consultants in developing modification proposals - typically the Code panel can refer modification proposals to working groups. However in certain circumstances “expert resources” such as economic consultants can provide important analysis that facilitates the assessment of modification proposals.

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

It should be noted that the code objectives reflect in many cases the objectives set out in the transmission and distribution licences and any review will require a critical appraisal of the relevant objectives set out in these licences. The review should be mindful that there may be good reasons for having differing objectives and we would caution expanding objectives without good reason as this is likely to increase cost and complexity to the industry.

Charging Methodologies

We note that the System Operator and network owners have obligations under their licences to keep charging arrangements under review and to conform the charging arrangements with any modification to “core industry documents”. In addition with respect to BSC modifications and CUSC amendments, National Grid has an obligation to conform documents to allow implementation of the proposed changes.

Whilst there is a case that code changes may require consequential changes to the charging methodologies, the case that the charging methodologies themselves should be subject to an industry change process is more questionable. In particular a wider change management process could give rise to material changes in transmission or distribution tariffs with consequential impacts on parties and customers. In addition, tariff fluctuations could increase the risk for all market participants. We would also make the point that charging methodologies should be completely transparent so that customers understand why they are being charged a given figure. Furthermore any change to charges, should be well trailed so that suppliers can factor them into their own pricing decisions.

Other issues

Under this section we have used the sub headings to provide our comments;

- **Fragmented code administration and multiple code administrators**
 - Some administrators (e.g. Elexon, National Grid and the Joint Office) provide analytical support; we would not want to lose this.
 - The role and independence of the code administrator varies across the codes, again there may be good reasons for this so each code should be assessed on the effectiveness of their arrangements.
 - We have also observed variable quality in the code web-sites and this may be an opportunity to consider best practice across the codes.
- **Scope for self-regulation within codes**
 - This varies between codes, with DCUSA and MRA allowing some changes without Authority consent with SPAA, BSC² and UNC requiring all modification changes to be approved by the Authority. There may be scope for considering best practice across the codes in relation to more self regulation.
- **Is the structure of the code Panels and other committees appropriate?**
 - We would agree that this could be examined and where appropriate best practice adopted more widely.
 - Should industry panels be “independent” (e.g. BSC) or “representative” (e.g. Grid Code?)

² Excluding changes to code subsidiary documents, which do not require authority consent.

- one of the overriding objectives of NETA was to create an “independent” arrangement for panel membership and membership of associated working groups. This has been achieved under the BSC, CUSC and UNC.

We look forward to participating in the review; in the meantime please call if you have any questions regarding our response.

Yours sincerely

Alan McAdam
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