

AW/PW/111

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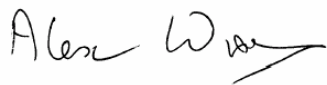
Dear Mark

**Re: Code Governance Review: Major Policy Reviews and Self Governance**

I have pleasure in providing NGN's response to your consultation. Please note that our response is focussed on gas distribution and the UNC and that we are not commenting on the appropriate approach for electricity; indeed, there is no reason to suppose that the best solution for electricity would apply for gas. NGN is broadly in favour of the proposals to move to a three-pronged approach for modification proposals. The attached response addresses each of the specific questions in your consultation.

Please let me know if you would like any clarification of any aspect of this response. Note that our response can be regarded as non-confidential.

Yours sincerely



Alex Wiseman  
Regulation Director

## **Code Governance Review: Major Policy Reviews and Self Governance**

### **CHAPTER: Two**

**Question 1: Do you agree with our assessment of the deficiencies of the codes governance arrangements and do you agree there is a case for reform? Are the proposed reforms a proportionate response to the problems with the status quo that we have identified?**

NGN agrees that there are some deficiencies in existing arrangements. However, some of the issues that Ofgem raises may be regarded as healthy, for example multiple proposals reflect the impact of competition and may result in a better final solution. Also, reform of governance arrangements may not prevent these deficiencies occurring as they can be driven by code signatories' legitimate desire to protect and enhance their regulatory and commercial positions. Furthermore, participants will appropriately seek incremental improvements to new proposals which can result in a piecemeal approach but may ultimately produce better solutions.

Nevertheless, undoubtedly improvements can be made to improve the quality of assessment and to ensure Ofgem's input is better focussed on critical issues. Consequently NGN broadly welcomes Ofgem's proposals. It is important, however, to ensure that the streamlined, targeted governance being sought does not add complexity, cost and time delays to industry governance arrangements.

**Question 2: Would the Major Policy Review Process enable key strategic issues to be progressed more effectively and efficiently with consequent consumer benefits?**

Implementing a Major Policy Review Process *would* secure a more effective way of progressing strategic issues, as identified policy areas could be formally advanced by Ofgem. This should also be the route used when Ofgem or Government promotes major industry change such as exit or interruption reform. It is important that the process includes full industry consultation and impact assessments to ensure that the most suitable and desirable industry solution is chosen.

**Question 3: Would a Self Governance route be suitable for a significant proportion of modification proposals?**

Self governance would provide a suitable route for a proportion of UNC modification proposals though it is difficult to say how many, perhaps 25% - 50%. However, any incremental improvement in governance that better targets industry resource is welcomed.

**Question 4: If both the Major Policy Review and Self Governance routes were implemented, is there a case for retaining an Improved Status Quo path?**

There is definitely a case for retaining an improved Status Quo path. There are many occasions in UNC when an Ofgem final decision is required, most obviously when proposals transfer risk between market segments (eg I&C and domestic). In such scenarios, Ofgem's involvement at the end of the Status Quo path is critical.

**Question 5: If this package of reforms of implemented, should it apply to all codes? If not all, which? Should the introduction be phased?**

The proposals are broad enough that they should be applicable to all codes, but NGN is not in a position to comment on electricity codes. Phasing would not be an issue for NGN but it may confuse those industry participants working across sectors as a mixture of distinct governance

arrangements (say between BSC and UNC), would require some organisations to operate within two (or more) quite distinct sets of arrangements.

## **CHAPTER: Three**

### **Question 1: Once a Modification has been raised, should the filtering decision be taken by Ofgem (with a panel recommendation) or by the relevant panel with an Ofgem veto?**

The most efficient approach would be for panels to recommend a filtering decision with a brief rationale and for Ofgem to have the opportunity to veto the decision. A recommendation should be between all three paths. In the event that there was not a majority vote by the panel for the appropriate route for a modification then the decision should be deferred to Ofgem. In the interests of expediency it is important that Ofgem makes a decision quickly with, say, no more than a week to decide whether or not to veto and a final decision in the event of a veto or deferral within one month of the panel meeting [are these timescales reasonable?]

### **Question 2: What criteria should be applied to assessing whether a modification falls into path 1 or path 2?**

NGN agrees with the listed criteria by which proposals would be considered under path 1 or path 2.

### **Question 3: How should we treat modifications that fall within the scope of an existing Major Policy Review?**

Ofgem discusses placing a moratorium on proposals linked to existing major policy reviews actively under consideration, however we do not believe that a complete moratorium is appropriate. NGN's view is that firstly it may be difficult to accurately define the boundaries of the review and secondly there may be valuable, perhaps relatively small, modifications that can be implemented during the review period. Our proposed approach is that there is a fourth filtering criteria during a major review and the panel can recommend (or Ofgem can direct) that a mod should not be progressed because it falls within the scope of the review.

## **CHAPTER: Four**

### **Question 1: What process should be adopted for Major Policy Reviews?**

As suggested in the Consultation paper, no fixed process should be created in advance of Policy Reviews. As indicated above, it is important that there is full industry consultation and an impact assessment that underpins Ofgem's final decision.

### **Question 2: What are your views for determining the outcome of a Major Policy Review? Question 3: How ought the outcomes of a Major Policy Review to be implemented?**

NGN favours option 3 as then Ofgem is in full control of the process through to legal text; in options 1 and 2 there is the possibility of misinterpretation between Ofgem and the industry. We agree with Ofgem that this should provide the speediest and most effective solution. Furthermore, a company such as NGN does not have the in-house resources to develop and fully draft complex mods.

We recognise Ofgem's concern that this may not make best use of industry expertise, however this expertise, as well as innovative thinking from the industry, could be tapped during workshops that Ofgem could hold during the review. Indeed, if one organisation was obliged to develop the code then innovation is less likely than under option 3.

There should be an additional stage in option 3 after legal drafting: an industry review, to ensure that the legal drafting is fully consistent with the Ofgem policy decision and that there will be no (or minimal) unforeseen consequences.

Option 3 will also avoid the proposed licence modifications to obligate the raising of mods and the backstop provisions for Ofgem to reject the mod if Ofgem believed it failed to reflect its policy conclusions.

**Question 4: What safeguards and appeals mechanisms should be in place?**

No additional safeguards need to be in place, outside of those currently available for appealing UNC modifications.

**Question 5: Should there be a moratorium on subsequent code modifications following the completion of a Major Policy Review?**

No: a blanket moratorium would prevent incremental improvements to major policy reviews. The filtering and Ofgem right of veto to proposals referred to previously would allow Ofgem the ability to prevent “same issue” proposals being resurrected during a major policy review.

**CHAPTER: Five**

**Question 1: If current panel/voting arrangements for any code are to be changed, which model is optimal?**

A representative panel (as per current UNC) is the optimal way to manage any new code arrangements. It would be difficult, if not impossible, to set up a truly “independent panel” with enough industry knowledge to adequately assess mods. Signatory voting provides an unnecessary layer of complexity and inefficiency which may lead to delays in progressing the majority of proposals. The UNC arrangements appear to work well with sufficient panel diversity to ensure appropriate assessment.

**Question 2: Should it be mandatory for panels to have a consumer and a small market participant representative?**

Each panel’s make up should be determined individually. NGN does not believe a voting consumer and small market representative is required or would be beneficial on the UNC. The panel is balanced at present with five transporter and five shipper representatives. A small market representative would often have the casting vote and would have a disproportionate amount of power. The current arrangement, with Consumer Focus able to attend but not vote at panel meetings, works well and enables their views to be heard and assessed. Our understanding is that Consumer Focus’s preference is not to have voting rights.

**Question 3: What voting procedures should apply governing code decisions?**

The existing UNC voting arrangements (including preference voting on alternates) provides sufficient transparency and guidance to Ofgem where its requirement to implement is still required. Under self governance arrangements the existing voting arrangements still provide the level of surety required, as no market segment (Shipper or Transporter) can carry a majority without the support of other industry participants. It should be noted that the panel members are fully independent of each other and frequently neither the transporters nor the shippers vote together as an industry body.

**Question 4: What appeal mechanisms should be in place? Should defined appeal arrangements be set out or should Ofgem have discretion over whether or not to hear an appeal?**

Ofgem lists four examples of how an appeal mechanism could operate. We suggest a combination of these:

Any industry participant should have the right of appeal providing it has pre-notified its concerns during the process or the decision would have a disproportionate impact on a class of signatories. Ofgem should have discretion on whether or not to allow the appeal to be heard. This would include rights of appeal for Consumer Focus or small participants.

The right of appeal to the Competition Commission should not apply to route 3, self governance mods, but only to route 1 and 2 mods.

**Question 5: Should a consumer and small participant representative have an automatic right of appeal?**

Yes, the above proposals should apply for all market participants.

**CHAPTER: Six**

**Question 1: Do you agree with our assessment of the package of reforms against the Review Objectives?**

NGN broadly agrees with the assessment made. Any well planned major policy review would be advantageous over piecemeal or multiple proposals which the industry has dealt with in recent years. Consequently, the reduction and better targeting of any impact assessments would be beneficial.

**Question 2: Do you agree with our quantitative assessment of the potential cost savings of reform?**

NGN agrees with the principles behind cost savings for major policy reforms and self governance, as both routes should deliver in most instances, swifter outcomes. The savings outlined from the two electricity case studies suggest direct cost savings of nearly £2m. It would be interesting to assess the equivalent costs had the enduring offtake reform process been subject to a similar quantitative assessment, as savings would also have been made in this area had a major policy reform route been followed.

In terms of self governance, the 50% value assigned to self governance proposals may be on the high side for UNC.

**Question 3: Do you agree with our assessments of the potential impact of reform on consumers, competition, and sustainable development?**

NGN agrees that any consolidation of the many industry workgroups will make consumer participation easier. That potential increased participation should lead to a beneficial positive impact on competition and sustainable development. NGN is not convinced however that consumer groups will become more actively involved, nevertheless any increased opportunity is welcomed.

**Question 4: Do you agree with our assessment of the potential unintended risks and consequences?**

The identified risks for self governance will be managed by Ofgem and Code Panel groups to ensure no inappropriate proposals are passed through without due consideration. Any filtering process will need to be sufficiently robust to err on the side of caution when proposals are being categorised to reduce this risk. The risk of inappropriate decisions is small and we agree that there are adequate mitigations in place.

The risk of ineffective decisions in a major policy review is lower than the risk with the current process and consequently this does not change the rationale of the proposed approach. Any major policy review is likely to bring consequential proposals which may be necessary for agreed improvement, or, as suggested, may undermine the proposal advanced by Ofgem. Nevertheless, these are risks and consequences the industry should allow. Proposals should not be disallowed simply because they don't directly match the view of the Regulator, and due process should ultimately determine the best approach.