

AW/PW/112

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Dear Mark

Re: Code Governance Review: Role of code administrators and small participant/consumer initiatives

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 do not have the experience to comment on the appropriate approach for electricity. Overall, we believe that the existing governance arrangements work effectively and efficiently for the UNC. Furthermore, the UNC is a contract between gas transporters and shippers and, although we believe that other parties should have full opportunity to comment and to make representations, we would be concerned if other parties had too intrusive a direct influence on the UNC, in particular voting rights.

It is noteworthy that the Brattle report commented that "the costs associated with electricity code governance were significantly higher than those associated with gas code governance". Both shippers and transporters give positive feedback on UNC administration. We would urge Ofgem not to impose change in gas simply for consistency with electricity arrangements. Additionally, we are not in favour of changes that may compromise the Joint Office's reputation for impartiality and independence.

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: Role of code administrators and small participant /consumer initiatives

CHAPTER: Two

Question 1: Are the Authority's concerns regarding the quality of analysis undertaken through the code modification route justified?

We agree that modification proposals should carry appropriate levels of evidence and analysis to back a case for implementation and in most cases this is true. The quality of analysis provided within UNC proposals does vary significantly, but it is our strong belief that it is the responsibility of modification proposers and the parties seeking to influence a proposal's outcome to present a case with the best analysis available. It is not the role of the code administrators to provide the analysis, and indeed the code administrators do not (and should not) have the requisite comprehensive industry knowledge. That responsibility sits with code signatories, and any other party who wishes to provide evidence and views for consideration.

Question 2: Are some code administrators more accountable than others?

NGN believes the Joint Office is directly and fully accountable for the administration and governance of the UNC to all code signatories and it is fully independent. Indeed, because the Joint Office has no other primary responsibilities apart from code administration, it is able to focus on this activity. We are not in a position to comment on whether other administrators are more or less accountable.

Question 3: We consider that code complexity is a problem, particularly for small participants, new entrants and consumer representatives. Do you agree? How can the complexity be reduced?

The energy industry is complex and consequently the codes governing arrangements between participants of necessity are complex. It is not clear to us that any of the proposed reforms in this consultation would reduce complexity. Code complexity is not necessarily the reason why small participants, new entrants etc are less active in the code governance process. While we would support the reduction of any unnecessary complexity, changing governance arrangements would not reduce complexity.

Question 4: Do small participants, new entrants and consumer representatives find it difficult to engage with the code modification process?

We are unable to comment; this is a question for the relevant parties.

CHAPTER: Three

Question 1: Do you agree that the quality of analysis in code modification reports could be improved? Should the role of the code administrator be changed to help enhance the quality of code modification reports?

There are some reports where undoubtedly the quality of analysis could be improved but this is not the responsibility of the code administrators. As the custodian of the process they should encourage and suggest refinements to code signatories' analysis, but they should not be formally tasked with making improvements in this area.

Question 2: Which of the options for changing the role of the code administrator in the modification process (critical friend or active secretariat) is most appropriate? Should different options be chosen for different codes?

We believe that the role that the Joint Office currently undertakes is broadly in line with the critical friend role proposed by Ofgem.

A further shift to the active secretariat model is inappropriate. The scope and potential volume of work involved to correctly perform this role would not only add significant costs to the administrator, but would also inappropriately blur the independence of the highly successful and respected administered role currently undertaken.

Question 3: Should the roles of the administrators of the BSC, UNC, CUSC, Grid Code, SPAA and MRA in respect of central systems management be harmonised i.e. should all code administrators either be made responsible for the related systems or should this responsibility be removed from them all?

NGN opposes any move to make the Joint Office responsible for the central systems management and related systems. The criticisms levelled at the lack of transparency of costs and timeliness of system cost provision may have some basis, however these concerns can be addressed and such information provision improved through improved communication links with xoserve and other service providers. Aside from the funding issues associated with the transfer of responsibilities in this area to the Joint Office, this would not on its own resolve any of the issues raised. However, making the Joint Office responsible for related systems would result in conflicting responsibilities for the Joint Office and prejudice its independence.

CHAPTER: Four

Question 1: Should code administrators be independent of network owners? If so, is it sufficient to have management unbundling or should the code administrator be an independent company?

Independence from network owners is proposed to ensure that no conflicts of interests occur. The Joint Office has demonstrated beyond any doubt its complete impartiality since 2005 in its running of the UNC process and this view has been formally expressed by the UNC modification panel. We believe it appropriately follows the “management unbundling” model described in the consultation. There is a licence requirement on transporters to operate joint governance arrangements and so the Joint Office can never be truly independent.

However, the Joint Office is a small body of six staff. The expense and bureaucracy of making it a separate limited company would not be justified by any benefits. The governance provided by the JGAC, composed of transporter representatives, works effectively and has ensured that the Joint Office remains independent and impartial and we see no need to change these arrangements.

Question 2: Should all the major codes have the same corporate governance structures? What is the most appropriate governance structure?

NGN does not believe there is a case for all of the major codes to have the same corporate governance structures. Alignment, purely for consistency is not appropriate and the regimes and structures as well as the requirements of each industry differ. The current governance structure for the Joint Office has proved effective over the three and a half years of its existence and we see no need for change. We cannot comment on the appropriate governance structures for other codes.

Question 3: Are code administrators and the management teams for CUSC, UNC and BSC sufficiently accountable in terms of costs and performance? Do they have clearly defined objectives and measurable performance targets?

The Joint Office is accountable via the JGAA in terms of cost and performance. The JGAC (the governing committee consisting of transporter representatives) exercises tight and effective budgetary control on the Joint Office. Performance can be judged by delivery of the infrastructure to ensure modifications are appropriately debated, communicated, voted on and implemented. In this regard, the Joint Office has proven itself as an effective deliver of its services. The Joint Office is accountable from all code signatories for its key role in the code governance process.

Question 4: Code administrators are currently funded by cost pass through, service contracts or price controls. Which of these funding arrangements is the most transparent and accountable?

Cost pass through is a favoured option for us as a transporter as it reduces the risk. However, we recognise that this provides less accountability. Consequently price control is appropriate, however, it is important that the price control recognises any new obligations that may be imposed by Ofgem on the administrator. As with other controllable costs, the decision of whether or not to award a service contract should be the responsibility of the owners who will assess the most efficient means of meeting their obligations. We agree that service quality is important and perhaps should be measured, however there has been no degradation in quality despite the Joint Office taking on additional obligations such as administering some xoserve industry meetings.

Question 5: Is there an argument for considering the service contract approach to funding for more codes if a degree of self governance for a code is introduced?

As noted above, a service contract approach should not be obligated. The move towards self governance does not in itself imply preference for a service contract.

Question 6: Should the funding for the code administrators for the CUSC and UNC be removed from the relevant network owner price controls?

We agree with Ofgem's consideration that, for an operation of less than £1m per year, it would not be proportionate to remove funding of the UNC from network owners.

CHAPTER: Five

Question 1: Should Ofgem have powers to send in and call back modification proposals? What are your views on the send in and call back options?

Any intervention that increases the accuracy and completeness of a proposal and the ability for a timely implementation is welcomed. NGN agrees with a process, whereby a 'completed' proposal could be sent back for additional work by Ofgem, to assist in a final implementation decision. Such a move would prevent unnecessary duplication of effort whereby rejected proposals had to be re raised with minor changes reflecting Ofgem's concerns. We would expect these powers to be exercised only occasionally.

Question 2: Should all code Panels have to publish the reasoning behind their recommendations?

Determinations by the UNC panel whether to implement a proposal are based on whether it better facilitates the relevant objectives set out in the UNC and Licence. NGN supports the

formal recording of these views and any other substantive reasons offered at the time of recommendations.

Question 3: Should code administrators be able to raise modifications themselves? If so, should there be limits on what modifications they can raise or should they have to gain consent of the code Panel to the raising of the modification?

An independent administrator should not be allowed to raise modifications as this ability may compromise its independent status. There is an argument that the Joint Office could be allowed to raise 'Consent to Modify' modifications only, to ensure the UNC does not have inappropriate clauses or redundant text, but on balance we believe that even these tidying up modifications should come from one of the parties to the contract.

Question 4: Would it be useful to develop a code of practice applying to all code administrators? Should it be voluntary or binding?

It would be good practice and would aid transparency to develop a voluntary code of practice providing it did not increase costs for currently effective administrators.

Question 5: What are the most appropriate mechanisms to evaluate the performance of code administrators? Is a scorecard approach appropriate?

NGN favours benchmarking to compare organisations and agrees that a qualitative assessment is appropriate given the range of service offered by the various code administrators. Direct feedback from code signatories would give a comparison across administrators and should provide feedback for administrators to improve performance. The use of a scorecard would be particularly interesting for Users who used more than one code, where a direct ranking would be shown. Whilst recognising that timeliness is a key issue, we would caution an over reliance on measuring the time to turn around reports etc, if this compromised the quality and thoroughness of reports which Ofgem are keen to see improve.

CHAPTER: Six

Question 1: Do small participants, new entrants and consumer representatives face significant hurdles in engaging with the code governance processes?

Industry arrangements are, of necessity, complex and there are hurdles in engaging but these are not due to the code governance processes.

NGN is unaware of any evidence that the class of parties referred to are concerned that the governance processes preclude their participation. Large Gas Transporters have presented UNC code updates as a consistent agenda item to the Gas Customer Forum in recent years and have received little or no feedback on any concerns about these parties' lack of involvement or the reasons why they are often passive in such developments.

Question 2: What are the key issues that need to be addressed in order for small participants and others to better engage with the code governance processes?

We are unaware of specific issues. It is unclear that there is a real appetite for direct involvement in code decision making. Engagement can be accommodated through existing structures such as the Gas Customer Forum.

Question 3: Do you have any views on the issues highlighted in this chapter? Do you have any views on the advantages and disadvantages discussed under each option?

The issues in this chapter rely on the premise that a key number of industry views (and participants) are excluded from the existing governance process because of cost and complexity. Additionally, this chapter implies that any perceived improvements in this area would directly correlate to increased participation and different contributions from the market sectors in question.

We do not believe code administrators should be compelled to take additional steps to consider any party's views, nor should they be required to take positive action to provide extra communication routes to any designated industry area.

NGN opposes any move to fund a central funding pot from which selected industry participants could draw funds. If a fund is to be provided to subsidise these participants it should be provided by Ofgem or Government, not from other industry participants.

The UNC panel currently has five transporter representatives and five shipper representatives (who represent all gas shippers). A consumer representative with voting rights would carry too much power on voting matters and would frequently have the casting vote. This power would be particularly inappropriate given that many proposals do not impact on consumers, and it would be unrealistic to expect such a representative to have a sufficiently informed view to vote in such cases. Crucially, it is unclear that groups such as Consumer Focus wish to be active code participants with all of the responsibility that entails. Furthermore the UNC is a contract between gas transporters and shippers and third parties, while having full opportunity to comment and to make representations, should not be able to vote on modifications.

A small participant would need to be defined very carefully. For instance a small participant whose parent company was a major company would not face the same resource constraints as an independent small participant.

The mechanics and timeframes associated with funding being allocated would potentially add timescales to proposals that were raised requiring swift debate.

Question 4: Which options, if any, do you consider will allow small participants and others to engage better with the code governance processes?

NGN believes Ofgem's current Consumer First Panel and Consumer Challenge group are most appropriately placed to assess and influence proposals directly in debates or via written representations. This approach would correctly allow targeted assessment of issues, rather than a blanket approach where the vast majority of issues may not require such input.

Question 5: Are there other options we have not yet considered which may assist small participants and others to play a fuller part in the codes governance processes?

Small participants are best placed to determine what changes (if any) will serve their interests best in playing a fuller part in the code governance process. Encouraging consumers to attend meetings like the Gas Customer Forum which addresses UNC issues will assist in promoting and informing those who choose to be part of the process.

Appendix 3

Question 1: Do you agree with our assessment of the various options for reform against the Review objectives? Question 2: Do you agree with our qualitative and quantitative assessment of the benefits and costs of the reforms?

The costs and benefits for active administrator and critical friend appear reasonable however we would point out that it may be difficult to find all the requisite knowledge for the active administrator role in 1-2 UNC recruits whereas transporters and shippers can call on a depth of industry experience within their organisations to undertake this role on specific mods.

We broadly agree with the remaining analysis except that under the discussion on introducing independent code administrators or panel chairmen, we believe that the UNC is already “administered in an independent, transparent and objective manner”. Furthermore, there is likely to be additional costs for an independent chairman as this is currently undertaken by the Chief Executive of the Joint Office as part of his duties.

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

We believe that the benefits suggested for small participants, new entrants and consumer representatives can be obtained without changing voting arrangements or code administrators’ obligations. Existing industry forums, particularly the Gas Customer Forum, enable engagement by these groups. Ofgem has suggested no sustainable development benefit for gas codes of changed rules and we concur that there is unlikely to be a sustainable development benefit.

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

We would suggest a further consequence is a reduction in the perceived independence of the Joint Office, and hence its effectiveness, if it was to be an “active administrator” or if it was expected to propose modifications.

Additionally, it is important to note that an unintended consequence of providing a vote for a consumer or small participant representative is that this vote would have substantial and inappropriate power as it would frequently be the casting vote in a deadlocked situation.