Industry participants, customers
and other interested parties

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Dear Colleague

The Code Administration Code of Practice

This letter sets out our final decision and approval of the Code Administration Code of Practice (CoP). The Code of Practice forms an integral part of our Code Governance Review Final Proposals which we published on 31 March 2010. The Code of Practice sets out the principles that we consider should underpin the administration of the industry code modification processes.

We have also published today statutory consultations to modify relevant licence conditions in order to give effect to our Final Proposals. These proposed licence modifications will place obligations on licensees to ensure that the industry codes, and any administrative body set up to oversee the codes, operate in a way that is consistent with the principles set out in the Code of Practice and more generally have regard to it. Subject to consultation responses, the licence obligations will take effect on 31 December 2010 and by this date the codes should be consistent with the principles set out in the Code of Practice.

The approved version of the Code of Practice is published alongside this letter.

Background

In June 2008 we published our decision on the scope of the Review of Industry Code Governance, one aspect of which was to reduce any unnecessary complexity and fragmentation of the existing codes governance. Such complexity is an obstacle for all market participants, but presents a particular barrier to new entrants and smaller parties seeking to engage in codes processes. We consider that removing barriers to participation for these parties is likely to promote competition and should stimulate innovation within the codes regulatory framework. We therefore invited industry participants to explore the potential for simplification and convergence of code modification processes in order to reduce complexity and encourage best practice across the codes.

This led to the creation of the Code Administrators' Working Group (CAWG), which looked at improvements which could be made to the code modification processes without structural change, for instance through modification to the existing rules or simply changing custom and practice. The CAWG provided Ofgem with its interim report in early 2009, which included, amongst other things, a recommendation that Code Administrators be subject to a Code of Practice. This report was consulted upon in our open letter of 20 April

2009[1], the responses to which subsequently influenced the thinking on our Code Governance Review Initial Proposals.

Following our Initial Proposals, the Code Administrators of the BSC, CUSC and UNC together produced a draft Code of Practice. This document built upon the principles agreed by the CAWG and set out a standard process that the BSC, CUSC and UNC modification rules should follow, generally simplifying the process. The CAWG was reconvened in November 2009 in order to consider the draft Code of Practice and templates. The group subsequently endorsed the document and recommended that it be subjected to a wider industry consultation. Therefore, on 31 March 2010 we issued an open letter consultation on the Code of Practice and associated Key Performance Indicators (KPIs) alongside our Final Proposals for the Code Governance Review.

During the consultation period we held a workshop on the 29 April 2010 to aid respondents in considering the proposals. Annex 1 to this letter sets out the responses to the consultation and the issues raised during the workshop along with our views on these points and any changes made to the final Code of Practice and KPIs in response.

Key Points

In general responses were supportive of the Code of Practice and the inclusion of KPIs. While not within the scope of this consultation we note that several respondents, while supportive of the Code of Practice, considered that it should have voluntary status, at least initially, with a view to making it mandatory at a later stage. This issue was consulted on as part of our initial proposals, with our decision being set out in our Final proposals that the Code of Practice should be underpinned by licence and afforded mandatory status.

Given its mandatory status, some respondents were concerned that there may be a conflict between the Code of Practice and the prevailing codes and questioned which, in this instance, would take precedence. We consider that as the Code of Practice expressly states that the codes take precedence there is no conflict. The licence drafting sets out a requirement to act consistently with the Code of Practice principles. In our view this does not alter the hierarchy as expressed. We note the interaction between the Code of Practice and the modification procedures within the codes themselves which means that changes to the Code of Practice are likely to be supported with code modification. This ensures that any changes will be carefully considered before implementation.

The majority of respondents agreed with our proposal to include KPIs within the Code of Practice, though there was significant discussion on what the precise nature of those KPIs should be. A common theme was that the current differences between the codes and the differences in custom and practice of the Code Administrators does not readily allow for direct comparisons to be drawn. We have included an initial set of KPIs in the Code of Practice and expect these to be measured by each of the Code Administrators in the coming year, though we accept the views of respondents that these should simply be a measure of how they are currently performing and should not seek to impose any targets at this stage. We have also recognised that the Code Administrators already, to varying degrees, seek to assess their own performance and we should not restrict their ability to do so. We therefore consider the KPIs set out in Principle 12 to be a baseline and should not preclude them from developing further KPIs, either collectively or individually.

Next steps

Subject to the licensees' acceptance of our proposals to modify their licences, we intend to direct the proposed licence modifications in early July 2010. The licence modifications will then become effective in the relevant licences on and from 31 December 2010. Therefore

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[1] See: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=41&refer=Licensing/IndCodes/CGR/CAWG

the deadline for the licensees to fully implement the resultant code changes to ensure that the codes are consistent with the Code of Practice principles will be 31 December 2010. We expect a number of code modifications to implement this requirement and the other conclusions of our Code Governance Review.

We do not anticipate that any further revisions to the Code of Practice will be made until a formal review is conducted under Code of Practice Principle 4.   However, if you would like to discuss any aspect of the Code of Practice, the KPIs or this letter, please feel free to contact either myself or Jon Dixon (jonathan.dixon@ofgem.gov.uk).

Yours faithfully

Mark Cox,
Associate Partner, Transmission and Governance

Annex 1: Summary of responses to consultation and our views

1. Do you agree with each of the principles listed in the Code of Practice?

There was general support from respondents for the principles set out in the Code of Practice (CoP). One respondent considered that the principles are unambiguous, complementary and (if followed) should lead to the simplification of the modification process. A number of respondents felt that some of the principles needed to be clarified or widened. Whilst we have not sought to widen the principles beyond those agreed about by the CAWG, we have sought to clarify the underlying text where appropriate. One respondent, while supporting the principles, felt that they would not aid understanding or engagement in the codes. They also thought that both the CoP and KPIs should be kept under review and if found not to be achieving their goal, they should either be changed or removed.

We consider that the principles will aid understanding and engagement in the codes and also that having one set of processes for modifying the three main codes with standard templates, rather than the current three different processes and differing templates, will greatly improve parties understanding of how to change the codes. The standard templates can be found on the Joint Office websites[2]. Also, by increasing accessibility through the use of plain English and encouraging better communication we believe the CoP will help parties to understand the implications of a modification and feel more informed and able to respond to consultations.

We agree that the CoP and KPIs should be reviewed regularly (at least annually) and this has been set out in Principle 4. By enabling reviews of the CoP and KPIs we can be confident that they will remain a 'live' document that is able to develop with the industry.

One respondent stated that they supported the high-level principles on the assumption that the obligation in the licence is to comply with the high-level principles and not every suggested method of fulfilling the principles as set out in the bullet points below the principles. We confirm that our intent is for the licensee to comply with the high-level principles of the code while having regard to the detailed aspects set out in the CoP. The bullet points which follow the principles have been developed to help facilitate a more common approach across the codes but licence drafting does not preclude the CA from exploring innovative ways to better meet those principles.

A suggested change to the 3rd bullet in Principle 2 was to reword it to say that "Technical language and use of acronyms will be accompanied by a supporting glossary when appropriate" to allow for the fact that markets and codes are by their nature complex. We do not believe that this change is required as we believe that the current wording allows for technical language and use of acronyms but requires that where they are used they are used appropriately and have a supporting glossary.

A respondent suggested that the 1st bullet point in Principle 6 should read "the proposer will have the right to veto any amendment to their modification proposal". We feel that current wording of the bullet allows the proposer to have control over any suggested changes to their proposal but also to change the proposal where they feel that it is necessary. There was also a suggestion that a bullet point should be added to Principle 9 to require further consultation if significant changes are made to the legal text. We consider that this is a reasonable requirement and note that it is already a feature in some of the Code's rules. We have therefore added this option to the sub-text of Principle 9.

A couple of respondents felt that Principle 8 was not clear on whose costs should be in the report. They felt that the report should include the costs for parties and not just CAs. However, at the CoP workshop that was held on the 29th April there was a recommendation

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[2] http://www.gasgovernance.co.uk/COP/templates

made that this principle should specifically relate to the central systems costs of implementing a proposal and should not include party's costs. This suggestion was made on the grounds that CAs cannot force parties to provide their costs and have no control over the accuracy of those costs. On top of that, parties are often not happy to provide this information especially if it might reveal sensitive company information. Those at the workshop agreed that it was best to reword the Principle to specify the costs as being Central Systems costs. CAs could provide party costs where provided. We agree with this approach and have made changes to the CoP to make this clear.

2. Is the description of the change process in the CoP sufficiently detailed?

Most respondents considered that the CoP was sufficiently detailed. Some respondents requested clarity of the stipulation under Principle 10 that consultations should each be 15 working days. We can confirm that the intent was for any consultation to be for 15 days, rather than an aggregate. The standardised process envisages only one consultation, but this does not necessarily preclude earlier or subsequent consultations if the panel in particular consider that is appropriate. 15 working days would be a reasonable period for each of these, though again, we do not seek to restrict the panel from exercising its discretion to allow for a shorter or longer timescale if appropriate for individual consultations. We have changed the CoP to clarify this point.

It was pointed out by one party that the 15 working day consultation period would cause the modification process to take longer. This would be due to the administration processes surrounding the development and consultation of the modification proposal and dealing with responses. Although, we do not seek to restrict the panel from exercising its discretion to allow for a shorter or longer timescale if appropriate for individual consultations we consider that the process is a standard one and should be complied with where possible and appropriate.

Some respondents raised a concern with the further guidance given in Annex 1 to the CoP that stated that proposers will be entitled to attend and to speak at panel meetings. This was also the subject of some debate in the recent BSC modification P247[3]. As set out in our decision letter for that proposal, we consider that the chair (and the modification arrangements themselves) already provide for the proposer to address the panel. We have therefore left the principle as drafted as we consider that the independent panel chair will have discretion to facilitate this process.

3. Is there anything missing from the CoP that you feel should be covered?

A number of respondents felt that Principle 4 needed to set out a clearer process for raising changes to the CoP and KPIs. The process should offer the same procedural protections as the process surrounding code changes. We agree that the process for changing the CoP needs to be robust, with opportunity for all interested parties to have their input. However, we do not feel that this process necessarily needs to be set out in detail in the CoP principles at this time. The CoP Principle 4 allows for flexibility in the development of a process of change. We also note the interaction between the CoP and the modification procedures within the code themselves which should give parties comfort that any changes will be carefully considered before implementation.

It was suggested by a respondent that the modification report should include the estimated administrative costs experienced by stakeholders taking part in the modification process. They considered that the estimate could be worked out through estimating the number of meetings required for the modification proposal. Estimating the time needed for them to consider the meeting papers, responses to consultations, etc. We believe that this information may be useful to parties when considering modification proposals and is an area that can be explored further. We have not included this change within the CoP at this stage.

[3] http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=88&refer=Licensing/ElecCodes/BSCode/BSC

A number of respondents were concerned that it was not clear what would happen if a CA was found to be in breach of the CoP and what sanctions there would be. We note that the licence drafting intends that the licensee ensures that there are arrangements in place to ensure that the CA is able to meet the requirements of the CoP.

4. Do you agree that the CAs should be required to report on their KPIs?

A couple of respondents pointed out that the KPIs may be useful but what they are measuring is not always within the power of the CAs to control. One felt that the KPIs needed to be clearer on which KPIs apply to the CAs and which apply to the Code Administration process. We note these concerns and agree that the CAs do not have control over all the processes measured by the KPIs. However, we feel that the aim of the KPIs is to measure the whole code administration process. We feel that it is unnecessary to separate out the KPIs that the CAs are responsible for and those that are measures of the code administration process. In any case we believe that the CAs do have some form of influence in varying degrees throughout the process.

A number of respondents suggested that the KPIs should not include targets in the first year, but simply gauge how each code was currently performing. This would allow a baseline to be established that would help in setting targets for future years. One respondent felt that it may be inappropriate to use the KPIs to draw comparisons between codes, but instead to measure a codes individual performance year on year. Their reasoning for this was the differing nature of the Codes and the parties to them.

While we agree that the codes have difference which make like for like comparisons difficult, there are some aspects on which comparisons can be made. The KPIs may highlight where one CA or regime is considered to be performing better or worse than the others in a particular aspect of their role. Further investigation should then identify whether these are due to intrinsic differences, or an aspect of the CAs (or parties') behaviour which could be improved upon, or taken to be good practice and adopted elsewhere, as the case may be. This practice may then be adopted within the CoP.

However, we agree that it is not appropriate or necessary to set targets in year one or potentially for future years as the measurement of performance will be useful in itself. We have amended the CoP accordingly.

5. Do you agree that the KPIs should be set out in the CoP?

The majority of respondents felt that the KPIs should be included in the CoP and that each KPI should be linked back clearly to the principle that it is measuring. One respondent also noted that this would be in line with one of the main objectives the CoP by simplifying market governance through keeping relevant material in one document.

6. Should the results of the KPI reporting influence future revisions to the CoP?

There was general agreement from parties that the KPIs should be used as a way of influencing future revisions of the code, and measuring its usefulness. A number of the respondents felt that the KPIs should be fully established before they are used for this purpose and should only be used where the KPIs have provided meaningful feedback.

7. Do you have any comments or suggestions on the proposed KPIs?

Some respondents suggested that the Authority's timeline for making a decision should also be included. We agree that the KPIs should provide a measure of the effectiveness of the change management as a whole. This KPI has been developed to include the final decision making process on modifications as part of the overall timeliness of a modification and reported on alongside the other CoP KPIs.

We note that there were a particularly high number of comments in relation to the number of decisions which accord with the recommendation of the panel. Several respondents suggested that this would be a useful measure, but echoed the point made in our consultation letter that a decision which deviates from the recommendation may not indicate any problem with analysis etc, but simply reflect a difference of views and/or stem from the Authority requirement to have regard to a wider set of duties than the panel.

A number of respondents also stated that they felt that qualitative measures should be given precedence over quantitative measures as these would give more insight into the behaviours behind the quantitative results. We recognise the limitations of both quantitative and qualitative measures and recognise that their limitations will need to be considered when drawing any conclusions from the results.

A few respondents noted that the KPI on the number of responses received to a consultation might reflect the nature of the modification proposal more than the abilities of the CAs to encourage engagement. They felt that it would be a useful measure but should not be targeted.

There was also a lot of concern on the KPI for the number of email bounce-backs in the CAs distribution list. It was felt that this was not an effective measure of the behaviour it was trying to encourage (better communication) and would more likely result in a perverse incentive for CAs to delete email addresses from their distribution lists if they bounce back rather than investigate the reason for the bounce back. We recognise that this may be the case and this measure by itself could promote the wrong behaviour, though coupled with other KPIs we consider that it will still be a useful measure. However, we also recognise that emails are only one means by which the CA may communicate with interested parties. We have therefore not sought to prescribe a specific measure in the CoP, but encourage the CAs to consider further how they can gauge the effectiveness of their communication.