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| Modification proposal: | <b>Connection and Use of System Code (CUSC) CAP190: Two-Thirds majority voting requirement for CUSC Panel recommendations on Amendments arising from licence obligations, Authority requests or obligations</b> |                      |     |
| Decision:              | The Authority <sup>1</sup> has decided to reject this proposal  |                      |     |
| Target audience:       | National Grid Electricity Transmission PLC (NGET), Parties to the CUSC and other interested parties   |                      |     |
| Date of publication:   | 13 December 2011  | Implementation Date: | N/A |

## Background to the modification proposal

CUSC Panel<sup>2</sup> members each vote to recommend to the Authority whether a CUSC modification should be approved or not. Their recommendations collectively provide the Panel's final recommendation to the Authority. Nine Panel members<sup>3</sup> are able to vote. The Panel's final recommendation to approve a modification requires a simple majority in favour of a proposal – one vote more in favour of a modification than against, excluding abstentions. Failure to achieve a simple majority leads to a recommendation to reject.

Should the Authority's decision on a CUSC modification differ from the Panel members' majority recommendation, an aggrieved party who wishes to legally challenge that decision may seek to bring an Energy Code Modification Appeal to the Competition Commission (CC)<sup>4</sup>. The appeals process was introduced by the Energy Act 2004 and is underpinned by secondary legislation. The CUSC is a designated code for the purposes of the CC's appeals process.

The circumstances in which an appeal may be brought are circumscribed - an appeal on a CUSC modification is excluded where the Authority's decision accords with a recommendation that is supported by the majority of those views of Panel members which are clearly expressed in the Amendment Report<sup>5</sup>. In these circumstances, an aggrieved party that wishes to challenge an Authority decision that accords with the Panel's recommendation may only do so by way of judicial review.

As a result of Ofgem's Code Governance Review (CGR)<sup>6</sup>, the Significant Code Review (SCR) process was introduced. This process allows Ofgem to initiate a discussion on significant changes to industry codes and licences which may be needed to address a specific issue with cross-code and cross-code/licence impact identified by Ofgem as a result of, amongst other things, its wider statutory duties. On the conclusion of a SCR process, the Authority may direct the relevant licensee to raise changes to relevant codes and the licensee is obliged to do so. In the case of the CUSC, NGET would be obliged, at

<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

<sup>2</sup> The CUSC Panel is established and constituted from time to time pursuant to and in accordance with section 8 of the CUSC.

<sup>3</sup> The voting members of the Panel consist of 7 elected industry members, 1 of the NGET appointed members and 1 consumer representative member. The Authority may appoint a Panel member but has not done so.

<sup>4</sup> Details of the appeals process for energy code changes are set out on the Competition Commission website: <http://www.competition-commission.org.uk/appeals/energy/>.

<sup>5</sup> SI 2005/1646 Article 6 (1). The Amendment Report is now known in the CUSC as the Final Modification Report.

<sup>6</sup> The Code Governance Review final proposals are available here:

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=297&refer=Licensing/IndCodes/CGR>.

the Authority's direction, to raise a CUSC modification(s) as a result of a SCR<sup>7</sup>. Once raised, the modification(s) would follow the normal industry process culminating in a Final Modification Report (FMR) being referred to the Authority for decision.

### **The modification proposal**

The proposer, Wyre Power, raised CAP190 in September 2010. The proposal seeks to amend the CUSC so that:

- when CUSC Panel members vote on their final recommendation for a CUSC modification resulting from an Authority request, direction or instruction, a two-thirds majority vote would be required to recommend approval instead of a simple majority. For all other modifications, a simple majority of Panel members would be retained. In the case of the current CUSC Panel, at least 6 members (out of 9) would need to support approval of the modification, if all Panel members voted, to achieve a two-thirds majority

The joint Workgroup established to assess the proposal and a similar Balancing and Settlement Code (BSC) modification (P264<sup>8</sup>) noted the circumstances in which a two-thirds majority vote would be required, namely where a CUSC modification is raised as a result of:

- an Authority or Ofgem request, direction or instruction (verbally or in writing, including email)
- where the Authority or Ofgem compels or coerces a party to raise a modification
- where the Authority or Ofgem is the effective progenitor of a modification

The Workgroup noted that this definition would cover both a modification(s) raised as a result of a SCR direction by the Authority and any modifications subsumed into, or suspended as a result of, a live SCR process<sup>9</sup>.

In the proposer's view, there is a risk that, for SCR directed modifications or those subsumed or suspended as the result of a live SCR process, the right of appeal on an Authority decision on those modifications would be affected without a higher threshold of Panel members voting to approve.

The Workgroup sought external legal advice on CAP190 and P264. In the meantime, work on CAP190 was placed on hold. As a result of the legal advice, a further CUSC modification, CMP196, was raised to clarify that references to 'recommendation' in the CUSC relate only to the Panel members' recommendation in the FMR. CMP196 was approved by the Authority in September 2011<sup>10</sup>.

On 20 July 2011, the Authority rejected P264. The CUSC Panel agreed by majority at its July 2011 meeting not to extend the Workgroup assessment of CAP190. No Workgroup consultation took place and the Authority did not seek proposed legal text. A Code

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<sup>7</sup> Standard Licence Condition C10.6 (aa).

<sup>8</sup> Details about P264 appear on Elexon's website: <http://www.elexon.co.uk/Pages/home.aspx>.

<sup>9</sup> As a result of the CGR changes to the CUSC, a proposal raised after a SCR is launched falling within the scope of the SCR can be suspended by the proposer or subsumed within the SCR on the direction of the Authority and may re-enter the codes process at the conclusion of the SCR process. The Authority may however exempt a proposal from being subsumed within the SCR so that it can follow the standard modification process.

<sup>10</sup> Details about CMP196 can be found on NGET's website:

[http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/amendment\\_archive/](http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/amendment_archive/).

Administrator consultation did take place and three responses were received, all supportive of the proposal.

### **CUSC Panel recommendation**

The CUSC Panel considered the draft FMR for CAP190 at its meeting on 28 October 2011. The Panel members voted by a majority that CAP190 better facilitates Applicable CUSC Objective (b). The full views of the Panel members appear in the FMR.

### **The Authority's decision**

The Authority has considered the issues raised by the modification proposal and the FMR dated 10 November 2011. The Authority has considered and taken into account the responses to the Code Administrator's consultation on the modification proposal which are attached to the FMR<sup>11</sup>.

**The Authority has concluded that implementation of the modification proposal will not better facilitate the achievement of the applicable objectives of the CUSC<sup>12</sup>.**

### **Reasons for the Authority's decision**

We note that the Workgroup did not fully assess the proposal and the only comments came through the Code Administrator consultation and the Panel members' views. We also note that the proposal is neutral against Applicable CUSC Objective (c).

*Applicable Objective (a) 'the efficient discharge by the licensee of the obligations imposed upon it under the Act and by its licence'*

We do not agree that the proposal would better facilitate this objective.

NGET's role under its licence obligation is to raise a CUSC modification(s) in line with the SCR directions made by the Authority. It would be for NGET to determine how to frame the SCR directed modification(s) it raises, taking account of the Authority's SCR direction. The Authority's direction may be high level principles or more detailed in scope<sup>13</sup>.

Once raised, the SCR directed modification(s) would follow the standard modification process and a Panel members' recommendation would be made to the Authority as already occurs. It would be the Panel members' majority recommendation and the Authority's subsequent decision that would give rise to any right of appeal to the CC.

It is not clear how a higher voting threshold for SCR directed modifications will make it more likely that the transmission company will raise a well considered robust modification as a result of a SCR direction. We note in the case of the CUSC that the difference between a simple majority and a two-thirds majority is marginal – a single vote. Equally, it is unclear how a higher voting threshold will lead to a lower risk of appeal. We do not

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<sup>11</sup> CUSC modification proposals, modification reports and representations can be viewed on the NGET website at <http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/>.

<sup>12</sup> As set out in Standard Condition C10(1) of NGET's Transmission Licence, see: [http://epr.ofgem.gov.uk/document\\_fetch.php?documentid=5327](http://epr.ofgem.gov.uk/document_fetch.php?documentid=5327)

<sup>13</sup> See paragraph 1.51 of Appendix 1 to our CGR Final Proposals dated 31 March 2010: [http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/CGR\\_Finalproposals\\_310310.pdf](http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/CGR_Finalproposals_310310.pdf).

consider that the proposal provides any assurance to NGET one way or another that it has discharged its licence obligation efficiently.

*Applicable Objective (b) 'facilitating effective competition in the generation and supply of electricity, and (so far as consistent therewith) facilitating such competition in the sale, distribution and purchase of electricity'*

We note the concerns of some Panel members that where the Authority directs the raising of CUSC modifications, specifically through SCR directions, appropriate checks and balances are needed because of the contentious nature of those issues to preserve the right of appeal of parties. We also note concerns that Ofgem will be acting as 'judge, jury and executioner' by initiating a SCR, making SCR directions on its conclusion (should directions result from the SCR process) and reaching decisions on any SCR directed modifications. We further note concerns that some materially affected parties who may not have the resources to engage with the SCR process may find they are disadvantaged once SCR directions are made and SCR directed modifications raised.

We do not agree that the proposal would better facilitate this objective. A SCR process is intended to be open, transparent and accessible to all parties. One of our concerns when initiating the CGR was that it was the lack of transparency and inclusivity of code change processes that may deter new entrants and small participants from involvement in energy markets. While the Authority leads the SCR process, we are committed to ensuring that each SCR is carried out in an open and inclusive way and that all interested parties can engage within the process to address the issues identified by the Authority.

At the conclusion of a SCR process, the Authority would, based on the evidence gathered during the process, determine whether any SCR directed modification(s) is needed. There is no requirement on the Authority to direct code changes and those changes which are directed may allow the relevant licensee some flexibility within the scope and intent of the direction, allowing for further development of proposals through the code governance processes. Ofgem would keep an open mind on the development of any SCR directed modifications prior to the delivery of the FMR.

Ofgem has recently launched two SCRs<sup>14</sup>. As neither has concluded, it is too early to say whether our and parties' expectations of the SCR process have been borne out. We will keep the present arrangements under review and have indicated that external factors may affect the future development of the code governance processes<sup>15</sup>. We consider that the arguments in favour of the proposal give rise to benefits that appear at best to be tenuous when compared against the applicable CUSC objectives and do not consider that the proposal addresses a genuine issue at this time. However, should we consider it appropriate to refine the SCR process further in light of experience, we would be willing to undertake a review with industry at the relevant time.

The CGR licence changes make it clear that any Authority direction(s) to a transmission licensee to raise a SCR directed modification do not fetter the voting rights of the CUSC Panel members<sup>16</sup> - the licence and the CUSC explicitly preserves the status quo in this regard.

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<sup>14</sup> A gas Security of Supply SCR was launched in January 2011 and Project TransmiT was launched as a SCR in July 2011. Details of both are available on the Ofgem website: <http://www.ofgem.gov.uk/>.

<sup>15</sup> For example, we referred to the implementation of the Third Package in our CGR final proposals.

<sup>16</sup> Standard Licence Condition C10(6C) "The Authority's published conclusions and directions to the licensee shall not fetter the voting rights of the members of the panel or the recommendation procedures informing the report described at paragraph 6(b)(v)." This wording is largely replicated in CUSC 8.17.6.

In light of this, no strong case has been presented of an obvious defect in the current governance arrangements. We can see no justification at this time to consider making it more difficult for the Panel to achieve a majority recommendation for licence directed modification proposals and for treating such proposals differently to other modification proposals with regard to voting thresholds.

CUSC Panel members are under a duty to act impartially and not represent any interests<sup>17</sup>. It is accepted that all CUSC modification proposals ought to be judged on their respective merits and whether a proposal better facilitates one or more of the applicable CUSC objectives. The recommendation made by the Panel should reflect this approach rather than a desire to preserve a party's ability to appeal a proposal by making it more difficult to achieve a majority recommendation.

For these reasons, we do not agree that the proposal would better facilitate the Applicable CUSC Objectives.

**Declan Tomany**

**Associate Partner Legal - Smarter Grids and Governance**

Signed on behalf of the Authority and authorised for that purpose

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<sup>17</sup> Section 8.3.4 (a) of the CUSC refers.