Promoting choice and value
for all gas and electricity customers

Code Governance Review (Phase 2) Proposals

Consultation

Reference:	123/12	**Contact:**	Lisa Charlesworth, ICL Manager
Publication date:	28 September 2012	**Team:**	Industry Codes & Licensing
Response deadline:	23 November 2012	**Tel:**	020 7901 7164
		Email:	industrycodes@ofgem.gov.uk

Overview:

Ofgem's Code Governance Review sought to update and improve the governance arrangements of the industry codes. The first phase of the review focused primarily on the electricity Balancing and Settlement Code and Connections and Use of System Code, and the gas Uniform Network Code. This second phase focuses on extending the Code Governance Review conclusions to the remaining industry codes.

Our proposals include:

- extending the scope and improving the effectiveness of self governance across the codes;
- applying Significant Code Review procedures uniformly, allowing for genuinely holistic cross-code reviews; and
- requiring codes to adhere to the principles of the Code Administration Code of Practice (CACoP).

Our consultation also includes proposed amendments and clarifications to the CACoP following the first annual review of this document and we put forward proposals in respect of the governance arrangements of the SPAA and a requirement on non-domestic suppliers to accede to this code.

Context

Better regulation is at the heart of Ofgem's work. We are committed to policies and processes that reduce regulatory burdens on industry while maintaining effective consumer protection. This review of industry code governance forms part of our work towards Better Regulation as detailed in our Simplification Plan 2012-2013.[1]

The industry codes are the contractual arrangements that underpin the electricity and gas wholesale and retail markets. They define the terms under which industry participants can access the electricity and gas networks. In recognition of the changes that have occurred in the gas and electricity markets since the codes were first created, particularly the increasing importance of new entrants and smaller parties, the Code Governance Review set out to ensure that governance arrangements including the code administration and modification processes remained fit for purpose.[2]

Our CGR final proposals led to a number of changes to the governance arrangements of the Balancing and Settlement Code, Connection and Use of System Code and Uniform Network Code. Self governance and Significant Code Reviews were introduced into the modification procedures of these codes. The Code Administration Code of Practice was also created in order to establish a common set of principles for code governance.

This second phase of the CGR proposes to extend these outcomes to further industry codes and agreements. We are publishing draft modifications to the relevant licence conditions alongside this document to demonstrate how the proposals outlined in this consultation would be brought into effect. A further statutory consultation on any licence changes would follow in due course.

Whilst outside of the scope of this project, we think there may be merit in extending these principles to nascent industry codes such as the Smart Energy Code. The Smart Energy Code is a new industry code being developed by Government as part of the Smart Metering Implementation Programme. We will continue to engage with Government, as appropriate, on the development of the Smart Energy Code, including on the extent to which it may be appropriate for it to reflect the outcomes of our code governance review.

We have previously acknowledged[3] that there may be scope for consolidation of existing codes, particularly with the development of the cross-fuel Smart Energy Code. Whilst consolidation of industry codes is not within the scope of this consultation, we do consider that the alignment of code modification rules in particular would facilitate future work in this area.

---

[1] Available at http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=12&refer=About%20us/BetterReg/SimpPlan

[2] CGR final proposals available at http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=297&refer=Licensing/IndCodes/CGR

[3] See 'Promoting Smarter Energy Markets: A Work Programme' p.28. http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=52&refer=Markets/sm/strategy

Associated documents

Ofgem Simplification Plan 2012-2013
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=12&refer=About%20us/BetterReg/SimpPlan

Open Letter – Second Phase Code Governance Review
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=392&refer=Licensing/IndCodes/CGR

CACoP Review 2012
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=375&refer=Licensing/IndCodes/CGR

Code Administration Code of Practice
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=328&refer=Licensing/IndCodes/CGR

Code Governance Review – Final Proposals
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=297&refer=Licensing/IndCodes/CGR

Licence modifications implementing CGR Final Proposals
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=330&refer=Licensing/IndCodes/CGR

Critique of the industry codes governance arrangements (Brattle Group / Simmons & Simmons)
http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/20080612%20Codes%20governance%20review%20final%20draft.pdf

Contents

Executive Summary

There are increasing challenges for the gas and electricity markets which suggest that the traditional governance arrangements of the industry codes may no longer be fit for purpose. There is a greater potential for widespread reform prompted by external drivers, whether at a national or European level, and the nature of participation is changing with a proliferation of smaller niche operators, particularly in generation and supply. Ofgem's Code Governance Review (CGR) sought to update and improve the industry code governance arrangements to ensure that they could meet these new challenges.

The CGR final proposals focused primarily on the Balancing and Settlement Code (BSC), Connection and Use of System Code (CUSC) and Uniform Network Code (UNC). This document sets out our proposals to extend the CGR outcomes into other industry codes. Our aim is to:

- improve transparency and accessibility for all industry participants, particularly smaller parties and new entrants, by better aligning the change processes and establishing common principles across the industry codes;
- reduce red tape by providing a greater role for the industry to govern itself and drive efficiencies, allowing Ofgem to step back from those parts of the code arrangements that have minimal impact on consumers; and
- ensure that the governance arrangements of all industry codes can effectively support the large scale and complex changes facing industry in coming years.

Our proposals are in line with our commitment to Better Regulation principles and to reducing regulatory burdens on industry while maintaining effective consumer protection.

This consultation also includes proposed changes to the Code Administration Code of Practice (CACoP) following a review of this document earlier this year,[4] proposed adjustments to the self governance processes implemented under the initial CGR, and we are consulting on our guidance for the discharge of appeals made against self governance decisions.

We also propose to extend the requirement to accede to the Supply Point Administration Agreement (SPAA) to non-domestic gas suppliers, and to clarify relevant code objectives for the Master Registration Agreement (MRA).

These proposals are put forward for consultation with all interested parties. In order to aid stakeholder understanding, draft modifications to licence conditions are provided alongside this consultation to indicate how these proposals would take

[4] Details available at http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=375&refer=Licensing/IndCodes/CGR

effect. This drafting may alter in light of comments received and/or progress made on modifications directly to the industry codes.

Summary of proposals

The table below summarises the headline proposals set out in this consultation:[5]

		DCUSA	iGT UNC	MRA	SPAA	STC	Grid Code	Distribution Code	BSC	CUSC	UNC
Code Administration	Require consistency with CACoP Principles	✓	✓	✓	✓	✓	✓	✓			
	Send back powers	✓	✓	✓	✓	✓	✓	✓			
	Require reasons for decisions	✓		✓	✓	✓	✓	✓			
Self Governance	Introduce or extend self governance	✓	✓			✓			✓	✓	✓
	Align appeal processes	✓	✓	✓	✓	✓			✓	✓	✓
Significant Code Reviews	Extend SCR to additional codes	✓	✓	✓	✓	✓	✓	✓			
Misc proposals	Insert relevant objectives			✓							
	Review governance framework				✓		✓	✓			

We recognise that not all of these changes would require modifications to the relevant licence conditions and that some could be implemented by parties raising code modifications. We are open to views on whether some of these proposals should be taken forward by industry as opposed to Ofgem prescribing these through the licences.

[5] Where our proposals do not extend to certain codes, this indicates either that these provisions already exist in this code, or that we are not proposing to make changes at this time.

1. Introduction

Chapter Summary

This chapter provides background on Ofgem's Code Governance Review (CGR) and sets out the purpose and structure of this consultation document. It also sets out our objectives in undertaking a second phase of the CGR, the scope of our proposals and indicative timings.

Background

1.1. The industry codes underpin the electricity and gas wholesale and retail markets. These are multilateral agreements or codes developed pursuant to licence conditions which contain many of the rules and commercial and technical obligations that govern market participation.

1.2. Licensees are required to maintain, become party to, or comply with the industry codes in accordance with the conditions of their licence.

1.3. As the codes define the terms under which industry participants can access the electricity and gas networks, they significantly impact the shape and development of the gas and electricity sectors. By extension, these codes affect Ofgem's ability to deliver markets that best protect the interests of consumers.[6]

1.4. In November 2007 Ofgem launched a review of the arrangements governing the industry codes (the 'Code Governance Review') to ensure that they were still fit for purpose given the wide range of changes that had occurred since their introduction as well as the scale of the challenges faced by the industry over the coming years.

1.5. We recognised that the nature of participation in the market had evolved. Concern had been expressed by small market participants that the code arrangements were too complex and inaccessible, particularly for new entrants. The existence of multiple codes, each with its own governance procedures, creates fragmentation which is a potential barrier to participation in the code arrangements.

1.6. The CGR final proposals,[7] published in 2010, included a wide range of changes that sought to make the existing governance processes more transparent and accessible, particularly to smaller parties and new entrants, and to improve the codes' ability to manage major industry challenges.

[6] The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.
[7] Available at http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=297&refer=Licensing/IndCodes/CGR

1.7. The final proposals summarised five work strands to be implemented through licence modifications and subsequent code modifications. These were:

- Significant Code Review
- Self Governance
- Role of Code Administrators
- Charging Methodologies
- Environment/Objectives

1.8. These reforms focused primarily on the three main industry codes (UNC, BSC and CUSC) as these were considered likely to be central to any major industry reform. However, we did not rule out extending these changes to the other codes at a later date. We are now consulting on a second phase of the CGR to extend certain outcomes into other industry codes.

1.9. In April 2012 we published an open consultation letter[8] ('April open letter') setting out our intention to commence a second phase CGR; responses to that consultation are discussed in the relevant sections of this document.

Objectives

1.10. Our aims remain consistent with those set out in the initial CGR. Broadly, these are to ensure that the code governance arrangements lead to more effective, efficient and robust decision-making and to enable industry and consumers to achieve full value from the code arrangements. The CGR produced a new baseline for code governance arrangements and this consultation seeks views on bringing other industry codes into line with the CGR principles.

1.11. Our proposals seek to:

- improve transparency and accessibility for all industry participants;
- reduce red tape by providing a greater role for the industry to govern itself; and
- ensure that the governance arrangements of all industry codes can effectively support the large scale and complex changes facing industry in coming years.

1.12. As part of our aim of promoting quality and value for all consumers, we consider that these proposals will increase industry efficiency and aid accessibility for new entrants and smaller parties. This plays an important role in promoting effective competition now and in the future.

[8] Open letter and non-confidential responses available at: http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=392&refer=Licensing/IndCodes/CGR

Better Regulation

1.13. This review of code governance forms part of our work under the Better Regulation banner as set out in Ofgem's Simplification Plan 2012-2013. Our Better Regulation duty requires us to have regard to the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed. We have a duty to minimise burdens on stakeholders as set out in the Regulatory Enforcement and Sanctions Act 2008.[9]

CGR Outcomes

1.14. In proposing to extend the reforms made by the CGR, it is important to consider the extent to which these have been successfully achieved to date. We have therefore sought to capture feedback and lessons learned in respect of the CGR, in order to aid further implementation of the key outcomes. We are not at this stage undertaking a post-implementation review of these outcomes.

1.15. In our April open letter we asked whether industry parties had noted improved analysis in code modification reports following the CGR, whether self governance had been effectively implemented, and whether the significant code review process had met stakeholder expectations.

1.16. In response to the April open letter there was support from industry parties both for the improvements made by the CGR and for the proposal to extend common governance arrangements to the other codes. The responses are discussed over the following chapters.

1.17. We have also taken account of views expressed by code panels[10] and feedback on the CACoP's implementation provided as part of a review of this document earlier this year (the 'CACoP review').[11]

1.18. One respondent to the CACoP review highlighted that some elements of the CGR have created complexity in the code arrangements. We recognise that there are additional processes and considerations for the code panels and administrators as a result of the CGR. However, we consider that these have been positive improvements to the code arrangements, enabling more effective change management and robust decision-making. We would encourage code panels to review the applicable modification rules where they have found conflict or confusion to exist, revising these to ensure that the code provisions use 'plain English' where possible.

[9] http://www.legislation.gov.uk/ukpga/2008/13/contents
[10] We use the term 'panel' throughout this document, although the body established to fulfil such a role may be referred to under different codes as a Committee, Executive Committee, etc.
[11] http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=375&refer=Licensing/IndCodes/CGR

1.19. In general, we would encourage code participants to ensure that the codes develop in a more user-friendly way. The governance arrangements play an important role in this by ensuring that parties can engage effectively with the change processes. We anticipate that through increased awareness and accessibility of the code governance arrangements all parties will be better informed and able to drive the changes they wish to see in the codes.

Scope of proposals

1.20. The intention of this second phase of the CGR is not to pursue new policy initiatives, but to apply the conclusions of the CGR to the wider industry codes. The headline proposals set out in this document are made in respect of the Distribution Connection Use of System Agreement (DCUSA), Independent Gas Transporter Uniform Network Code (iGT UNC), System Operator Transmission Owner Code (STC), Master Registration Agreement (MRA), Supply Point Administration Agreement (SPAA), Grid Code and Distribution Code.[12]

1.21. The National Electricity Transmission System Security and Quality of Supply Standard (NETS SQSS) is not being considered within the scope of this project. However, we do consider that the governance principles set out by the CGR could be adopted under the SQSS as part of a separate review in due course.[13]

1.22. The proposals set out in this consultation broadly cover the following three areas of the CGR:

- Self Governance;
- Significant Code Reviews; and
- Code Administration (including send back powers, requirement to provide reasons for recommendations/decisions, and consistency with the CACoP).

1.23. In addition, we propose some adjustments to the self governance processes introduced into the BSC, CUSC and UNC by the CGR, and we put forward proposals in respect of the governance arrangements of the SPAA and a requirement on non-domestic suppliers to accede to that code.

1.24. These proposals are accompanied by draft licence modifications, although we recognise that in many cases they could be given effect through changes to the relevant code modification rules alone. We also acknowledge and welcome the work that has been done to date to bring the remaining industry codes into line with our

[12] Refer to Appendix 3 for an overview of these codes.
[13] SQSS recently reviewed its governance arrangements, concluding March 2012: http://www.nationalgrid.com/NR/rdonlyres/5CA4E193-DB69-4B75-97DB-47555F9A16CA/52046/SQSSGovernanceReviewFinalConclusions.pdf

CGR conclusions.[14] We remain open to alternative means of ensuring that the conclusions of this review are also given full effect.

Impact Assessment

1.25. Where we are proposing to make a decision that is "important" [15] we are normally required to undertake an impact assessment (IA). Proposals are considered important where they make a major change to our activities, have a significant impact on parties engaged in relevant industry activities or on the general public, or have significant effects on the environment.

1.26. A comprehensive review of the code governance arrangements was undertaken under the original CGR and impact assessments were carried out in respect of our final proposals. The proposals set out in this consultation reflect the outcomes and principles of the CGR. As we are primarily extending the scope of the CGR conclusions, we do not consider these proposals to require an impact assessment. Therefore, we do not propose to conduct a further IA at this stage.

Structure of document

1.27. The remainder of this document is set out as follows:

- Chapter 2 - proposals to extend Self Governance within the industry codes;
- Chapter 3 - proposals to extend the Significant Code Review process to all industry codes;
- Chapter 4 - proposals regarding the quality of analysis and reporting undertaken in respect of modification proposals, and the Code Administration Code of Practice (CACoP);
- Chapter 5 - proposed next steps and timescales.

[14] For instance iGT UNC modification 046 and STC modification CA048
[15] Within the meaning of Section 5A of the Utilities Act 2000 (Duty of the Authority to carry out an impact assessment): http://www.legislation.gov.uk/ukpga/2003/30/section/6

2. Self Governance

Chapter Summary

This chapter set outs our view that Self Governance is proving to be an effective and efficient means of determining code modifications; allowing a degree of industry self regulation over issues that have low materiality or low consumer impact. We seek views on whether these self governance processes can be further improved in those codes which have them and should be extended into those codes which do not.

Question 1: Do you consider that a 'fast track' self governance process should be available in the industry codes for minor housekeeping changes?
Question 2: Do you agree that the Agency Charging Statement should fall under the governance of the Uniform Network Code, rather than the Gas Transporter licence?
Question 3: Do you agree that self governance should be introduced into the iGT UNC and STC, and increased in the DCUSA?
Question 4: Do you consider it appropriate to apply the same governance principles to the Grid and Distribution Codes as are applied to the 'commercial' codes?
Question 5: Do you consider that both the Distribution Code and the Grid Code should be modified to allow for an open governance framework? In particular, allowing code users to raise code modifications; enabling code panels to have a more formal role in evaluating and recommending code changes; and the governance procedures brought into the codes? Are there any other areas of governance that you consider could be improved in the Distribution Code and Grid Code?
Question 6: Should MRA modifications be subject to a materiality test, to determine whether Authority approval of changes is required?
Question 7: Do you consider that it is appropriate to obligate non-domestic gas suppliers to accede to the SPAA?
Question 8: Do you agree that SPAA modifications should be subject to a materiality test, to determine whether Authority approval of changes is required?
Question 9: Do you have any comments on Ofgem's guidance for discharging self governance appeals (Appendix 7), and on the proposed adjustment to the BSC, CUSC and UNC appeal windows?
Question 10: Do you consider that the ability to appeal a self governance determination should be consistent across all codes?

Introduction

2.1. We introduced self governance for certain modification decisions into the BSC, CUSC and UNC as part of the CGR in order to reduce costs and facilitate faster implementation of modification proposals. We recognised that a large number of modifications which were coming to us for a decision had little material impact upon consumers and/or were of limited relevance in terms of materiality to our other statutory duties.

2.2. Allowing a greater number of modifications to be determined by industry will allow us to better target our resources on matters of greater relevance to consumers, which is consistent with our Better Regulation duties. By removing an

unnecessary process step in appropriate cases, overall efficiency of the change process is also increased.

2.3. We noted that similar self governance procedures already existed to a greater or lesser extent in the more recently introduced industry codes such as the DCUSA, SPAA and MRA.

2.4. In our April open letter we sought views on:

- whether self governance had been achieved effectively in the UNC, BSC and CUSC; and
- whether it would be beneficial to introduce self governance (or a greater degree of it) into the remaining industry codes.

2.5. This chapter sets out our current thinking, which has been informed by responses to that open letter, and puts forward proposals in respect of:

- the CGR self governance processes;
- extending the scope of self governance; and
- the self governance appeals process.

CGR self governance processes

2.6. The role of the BSC, CUSC and UNC panels was enhanced by the CGR, allowing them to initially determine whether a modification proposal could be suitably dealt with under self governance, and to subsequently take the decision on whether to implement the proposal.

2.7. As part of the CGR process we estimated that approximately 50% of code modifications could be progressed via self governance. Since the necessary modifications were made to the BSC, CUSC and UNC on 1 January 2011, around a third of modifications to those codes have been determined by the panels and this proportion shows signs of increasing.

2.8. A key principle of self governance is that decisions made by the code panels should be no less robust than those made by the Authority. Proposed modifications should be assessed against the code's relevant objectives and published in a transparent manner. It is of note that thus far there have been no appeals against a decision of the BSC, CUSC or UNC panels.

2.9. In general, most respondents to our open letter considered the self governance criteria to be appropriate and implementation effectively achieved. In addition, there was support for increasing self governance, both in codes where this already exists and in those where there is presently no self governance provision.

2.10. We set out below a number of areas where we consider the arrangements introduced by the CGR would benefit from clarification or improvement.

Self governance criteria

2.11. The criteria which the panels must use to assess a modification proposal are set out in the relevant licence conditions. A modification decision may be made without seeking Authority approval where it would, if implemented, be unlikely to have a material impact upon consumers, competition, security of supply or sustainable development.

2.12. Although some respondents to our CGR initial proposals[16] considered that detailed guidance on applying the self governance criteria would be necessary, the majority suggested that it would be preferable to retain flexibility and adopt a pragmatic approach. Therefore, we did not propose guidance, preferring instead to consider each proposal against the criteria on a case by case basis and allow common practice to develop.

2.13. Whilst this approach appears to be working reasonably well, with each panel over time establishing certain parameters within which it would expect to operate, there is a degree of inconsistency across the codes. For instance, the UNC panel appear to have used the criteria as a more flexible framework when compared to either the BSC or CUSC. This may be at least in part due to the greater number of modification proposals being progressed through the UNC at any given time. There is also a difference of approach in terms of initial assessment; while the UNC panel generally considers every modification proposal against the criteria, we consider that the BSC and CUSC panel have, at least until recently, placed greater emphasis on the views of the proposer, being cautious in classifying proposals as self governance if the proposer has indicated that they would prefer the decision to be taken by Ofgem.

2.14. Some respondents to our open letter felt that the self governance criteria were too restrictive, unnecessarily limiting the number of modification proposals that could be determined this way.

2.15. We acknowledge that until further experience is gained, it may be difficult for the panels to strike the appropriate balance in selecting proposals for self-governance. While panels are on this learning curve, it is perhaps natural to err on the side of caution. However, we consider that it would be more beneficial in the longer-term if panels seek to expand the boundaries of matters which they could appropriately deal with. We will continue to have oversight of all proposals and will look to call in proposals if we do not agree that they meet the self governance criteria. This should create robust, yet flexible arrangements for the classification of modification proposals and over time establish a de facto threshold.

2.16. Accordingly, we remain of the view that detailed guidance in respect of the self governance criteria could unnecessarily fetter the panel's discretion, restricting rather than enabling modifications to follow the self governance process. Our

[16] Available at http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=198&refer=Licensing/IndCodes/CGR

preference is that each proposal is considered on a case-by-case basis. We would expect it to become increasingly likely that the self governance route is used as the panels grow more familiar with the arrangements and more confident in their interpretation of the criteria, as well as stakeholders gaining further confidence in the panels.

Self governance statements

2.17. We stated in our CGR final proposals that if a code panel considers that a modification proposal meets the criteria for self governance, it should be required to make a statement to Ofgem to that effect. One respondent to our open letter questioned whether a self governance statement in the form of a formal letter was required, given that Ofgem attend the panel meeting at which self governance is determined.

2.18. The requirement for a 'self governance statement' was reflected in the modifications to the Gas Transporters and Electricity Transmission licences; however, it was not our intent to create an additional administrative burden and we agree that an Ofgem representative would ordinarily be expected to be in attendance when the panel determines whether the modification should proceed under self governance.

2.19. We consider that it will be sufficient to record the panel's determination within the ordinary minutes of the meeting. Only in the event that an Ofgem representative was not present at the meeting and/or the minutes will not be available until some time after the meeting would we expect to be separately notified of the panel's determination. We have proposed a clarification to the licence definition condition to this effect. Illustrative licence drafting is published alongside this consultation.

'Fast track' self governance

2.20. During the CGR we noted that some of the licences already contained an option for the Authority to approve proposed changes without these following the modification process, ie by providing its consent to a change being made. We noted that we would only expect such a 'consent to modify' route to be used where the matter was manifestly minor, such as a change to a typographical error or an update to references, where it would seem disproportionate to follow a full modification process.

2.21. This creates a potentially anomalous situation insofar as the Authority is able to step back from decisions with low materiality that can be properly determined via self governance; however, for very minor housekeeping changes Authority consent is still required. We are therefore proposing that a 'fast track' self governance process be used so that very minor changes would be capable of being made by the panel without the need to consult with parties or to follow the full modification process.

2.22. Such a process already exists under some of the codes; for instance the SPAA panel are able to approve changes to Market Domain Data (MDD) without putting the matter to a full vote.

2.23. We are of the view that where a change can reasonably be considered to simply reflect a matter of fact, ie a change of address or an incremental change to references following an insertion of text, there appears to be little value in following a full modification process or consultation. This must still be subject to a degree of scrutiny and discussion by the panel and we propose that unanimity at the panel would be required. If the panel were not unanimous this would be an indication that the change is not manifestly obvious or a clear matter of fact, and therefore should be raised as a normal modification. We consider this to be a suitable approach as this process must be restricted to changes that are genuinely minor and not 'modifications' in the usual sense. We also propose that the opportunity for code parties to object should be provided, prior to the change taking effect.

2.24. **We would welcome views on whether a 'fast track' self governance process should be available in the industry codes.**

Uniform Network Code – Agency Charging Statement

2.25. The UNC has thus far embraced self governance very effectively. There is however an additional complexity under this code insofar as the funding of changes can be done in one of two ways: funded by the Gas Distribution Networks (GDNs) as part of their price control activities, or through what is referred to as a User Pays mechanism.[17]

2.26. Under User Pays, changes which are considered to benefit only a subset of code participants, and that might not ordinarily be accepted, may nonetheless proceed on the basis that the beneficiaries will fund the change and those who do not benefit can avoid the additional cost.

2.27. Whilst under self governance the decision on whether or not to implement a modification rests with the UNC panel, the allocation of costs for that change is dealt with separately through a change to the Agency Charging Statement (ACS). The ACS currently sits under the terms of Standard Special Condition A15 of the Gas Transporter (GT) licence, rather than the UNC. Changes to that statement may be made unilaterally by the GTs, subject to the Authority not issuing a veto within 28 days of being informed.[18]

[17] In January 2012 we published our conclusions of a review of xoserve's funding, governance and ownership arrangements. These User Pays arrangement are expected to be superseded when the conclusions of that review are implemented, though this may be a further 2-3 years away.
[18] It should be noted that arrangements apply only to the methodology itself, including the insertion of any new service line; changes to xoserve's published charges can be made in line with changes to its cost base without further reference to the Authority.

2.28. This issue was considered as part of the UNC334 Review Group,[19] which recommended that the ACS be brought under the governance of the UNC.

2.29. As part of the initial CGR the various charging methodologies were migrated into the codes which governed the products and services to which those charges relate. This gave users of those services the right to propose changes to the methodologies. Bringing the ACS under the UNC would be consistent with these principles and would aid efficiency in the panel's determination of self governance modifications.

2.30. **We would welcome views on whether changes to the Agency Charging Statement should fall under the governance of the Uniform Network Code, rather than the Gas Transporter licence.**

Extending the scope of self governance

2.31. We consider that under the current arrangements the Authority is required to approve many modifications that could effectively be dealt with by industry. This seems to add no particular value and does not represent an effective targeting of Ofgem resources as required under the principles of Better Regulation. Increasing the scope of self governance should make the industry code processes more efficient, leading to the quicker implementation of beneficial changes, as well as enabling Ofgem to target its resources at matters which have a material impact upon consumers.

2.32. We estimate that approximately 50% of modifications to the iGT UNC, Distribution Code, Grid Code, STC and current Part 1 clauses of DCUSA[20] could potentially be determined under self governance.[21] We have not included the SPAA and MRA in this assessment as these codes already contain self governance provisions which are routinely used.

2.33. Due to the nature of code modifications and the variability in their number and complexity, it would be difficult to establish an accurate figure for the cost savings of increasing the self governance provision in the industry codes. However, it is clear that the long-term benefits of increasing code self regulation are more significant than any immediate costs of implementing changes to the existing governance processes, which should not be substantive. These benefits could include not only the efficiencies in the processes themselves, but also the additional benefit accruing from the implementation of worthwhile proposals that much sooner.

[19] http://www.gasgovernance.co.uk/0334

[20] Part 1 matters under DCUSA are those specifically classified as such under the code, or which satisfy the Part 1 criteria, based on the materiality of the change.

[21] We have based this on a retrospective assessment of the 39 modification proposals to these codes that had been submitted (and determined) in a recent 24 month period, where it was considered that at least 19 of these proposals could have met the self governance criteria.

2.34. Two respondents to our open letter noted some concern about introducing self governance into codes where there is not currently suitable panel representation. Where the panel is already tasked with providing the Authority with a recommendation on whether or not to accept a proposal, we consider the self governance process would be substantially the same, simply replacing the recommendation with a decision. The specific panel constitutions are not within the scope of this review. These arrangements can be reviewed, if necessary, through the usual code modification processes.

2.35. Respondents to our open letter generally welcomed the introduction of more self governance in the codes. We set out our proposals to extend self governance in each of the relevant codes below.

DCUSA

2.36. From its inception the DCUSA has included a degree of self governance, being separated into Part 1 matters, which cannot be modified without the consent of the Authority, and Part 2 matters which can be modified with the majority agreement of the parties.

2.37. We consider that to date this self governance mechanism has worked reasonably well and therefore does not require significant reform. In particular, the criteria for determining whether a matter is Part 1 or Part 2 includes a consideration of materiality and are therefore broadly in line with later developments under the CGR.

2.38. However, the prescription of certain clauses as definitively being Part 1 matters does require a significant number of change proposals to be submitted to us for approval irrespective of their materiality. Whilst it may increase certainty for sections of code to be reserved for Authority consent, we consider it more beneficial to ensure that there is discretion available to the panel to use self governance where appropriate. A retrospective review of recently completed modifications suggested that around a third of Part 1 modifications could have been determined by self governance.

2.39. We consider that it would require a relatively small modification to the DCUSA processes to clarify that whilst the code may indicate conditions to which changes would typically have high materiality, the proposed change should be assessed against the materiality criteria by the DCUSA panel. We recognise that this would entail an expansion of the DCUSA panel's current role, but we consider this appropriate and consistent with the role undertaken by panels on other industry codes.

iGT UNC

2.40. The iGT UNC modification rules currently resemble those of the pre-CGR UNC; there is no form of self governance in respect of code modifications. A back-casting exercise of recent iGT UNC modification proposals suggested that 50-60% of

modifications to this code could be determined by self governance, based on the criteria established by the CGR.

2.41. We therefore consider that self governance would have a positive impact on the functioning of this code. Respondents to our April open letter shared this view, with one specifically highlighting the iGT UNC as being in need of self governance.

2.42. We recognise that some degree of self governance exists in respect of iGT UNC ancillary documents. We consider it appropriate to extend this to the code itself, in line with the CGR principles and to achieve consistency with the UNC processes.

STC

2.43. The STC panel undertook a review of the code modification procedures in light of the CGR and concluded that they would give further consideration to self governance once the CGR processes had bedded in.[22] One respondent to our April open letter suggested that a cost/benefit analysis should be completed prior to introducing such changes.

2.44. As stated above, we do not consider there to be substantive costs in adjusting the code modification processes in line with the changes introduced by the CGR. We would welcome any information parties put forward in this regard. Industry procedures leading up to and including the production of the final modification report should be robust and where that report contains a recommendation, we would expect the relevant body (in this case the STC panel) to have undertaken an assessment that is as thorough as that undertaken by Ofgem. That being the case, the only substantive difference is that the outcome is a decision to implement, rather than simply a recommendation to implement.

2.45. Whilst there are a relatively low number of modifications coming through the STC process, for example a total of 4 modifications raised in 2011, if up to 50% can be expected to fulfil the self governance criteria the benefits of self governance are likely to be realised in the longer term.

2.46. **We welcome views on our proposals to introduce self governance into the iGT UNC and STC, and to increase self governance in the DCUSA.**

Grid Code and Distribution Code

2.47. We recognise that there have traditionally been relatively few modification proposals raised to these codes each year. However, to the extent that each proposal requires substantial Ofgem resource in order to reach a decision, we are of the view that due consideration should be given to whether modifications to these

[22] http://www.nationalgrid.com/NR/rdonlyres/BC3D4F33-E375-42B0-82BE-5F1FECA13195/47366/STCCommitteeCodeGovernanceReviewv10.pdf

codes should be subject to the same materiality test as other codes, with those of low impact upon consumers, competition, security of supply or sustainable development being decided under a self governance mechanism.

2.48. We recognise, however, that the scope of necessary changes to the governance arrangements of the Grid Code and Distribution Code in order to enable self governance is greater than elsewhere. We also consider that there may be greater potential for improvement in these codes.

2.49. It may be impractical to introduce self governance under both the Grid Code and the Distribution Code at this stage, as the current arrangements do not provide for a panel recommendation and therefore there is no established process whereby the panel could instead reach a decision. Currently, the Authority is instead presented with a recommendation by the licensee. In keeping with the wider principles of the CGR it may be appropriate to replace this with a more inclusive recommendation from the panel as a whole. We understand that the licensees already seek to obtain panel consensus before presenting a recommendation; this proposal would place the panel recommendation on a more formal footing.

2.50. At present it is also only the licensee who may formally raise modification proposals, although users may raise issues for consideration. We would appreciate views on whether a more inclusive framework should be adopted, whereby all users have the right to raise a modification.

2.51. These codes are notably different to other industry codes in respect of their dealing with technical rather than commercial arrangements. Nevertheless these technical arrangements have commercial ramifications; an open governance framework may therefore have benefits and could increase network operator accountability under these codes.

2.52. If a properly constituted panel recommendation is written into the rules, we consider that it would be appropriate to address the anomaly of Authority decisions on these codes not being subject to appeal to the Competition Commission. Whilst this would be for the Secretary of State rather than the Authority, we anticipate that revisions to the appeal regulations will be made in the near future and that it would be a relatively straightforward matter to include these codes at that time.[23]

2.53. To support an open governance framework it may also be relevant to bring the modification rules into the codes themselves in order that these are subject to the same change processes, consistent with other codes.

2.54. One respondent to our open letter was against implementing self governance in the Distribution Code as this code defines connection point requirements regarding which Ofgem has a duty to determine disputes. It was put forward that because Ofgem presides over the process that weighs up the costs and benefits of technical

[23] Revisions are expected in respect of the designation of the Smart Energy Code (SEC).

requirements, it is more efficient for Ofgem to retain its role in determining all code modifications as without Ofgem sign-off these decisions would be more open to challenge.

2.55. Whilst we would agree that we should retain a degree of oversight, this does not necessarily extend to a need to sign-off each and every change. We do not consider that the option of extending the principles of self governance to these codes has any direct relevance to our role in determining connections disputes.

2.56. In the longer-term, we consider that certain changes to the technical codes could appropriately be governed by licensees, users and stakeholders. To enable this going forward, we are at this stage consulting on a more general review of the governance arrangements of these codes.

2.57. **Do you consider it appropriate to apply the same governance principles to the Grid and Distribution Codes as are applied to the commercial codes?**

2.58. **Do you consider that an open governance framework should be applied? In particular:**

a) do you consider that all code users should be permitted to raise code modifications?

b) do you consider that the code panels should have a more formal role in evaluating and recommending code changes to the Authority?

c) do you consider that the governance procedures should be brought into the code and be subject to the code modification process?

d) are there any other areas of governance that you consider could be improved in the technical codes?

MRA

2.59. Under the MRA's current self governance arrangements the vast majority of modifications are already effectively progressed without requiring Authority consent and these arrangements appear to be functioning well. We consider that the introduction of an objective materiality test may have benefits by providing further clarity on those modifications which should, and conversely should not, come to the Authority for a decision rather than be determined solely on a prescription of certain clauses as requiring Authority approval. This would be consistent with the approach now used on other codes and would therefore create a greater degree of certainty for parties.

2.60. **We would welcome views on whether MRA modifications should be subject to a 'materiality' text.**

SPAA governance

2.61. Like the MRA, the SPAA was conceived as a lighter touch agreement, being self governed wherever appropriate. So far this aspect of the agreement has been relatively successful; only a minority of the changes since its introduction in 2004 have come to the Authority. However, unlike the MRA, the SPAA is not a fully inclusive agreement. There is not currently a licence obligation for non-domestic gas suppliers to accede to the SPAA and so far few have done so voluntarily. The reluctance of such suppliers to accede has often been explained in reference to a concern that the SPAA process would favour the larger parties to the detriment of smaller players. This view is based at least in part on the fact that party votes are weighted based upon market share.

2.62. It is far from ideal that non-domestic gas suppliers are currently disenfranchised (albeit that they can voluntarily accede) from arrangements that impact upon them, for example, the governance of the Review of Gas Metering Arrangements (RGMA) documents and more recently the administration of the Meter Asset Managers Code of Practice (MAMCoP) scheme. We consider that this restricted participation may also inhibit the SPAA from providing effective governance to further industry protocols that are under development, such as those concerning theft of gas.[24]

2.63. Whilst we recognise that in due course the Smart Energy Code may provide an alternative means of governing such protocols it is by no means certain that its scope will extend to cover arrangements beyond those required to facilitate the smart metering roll out. Any such extension would in any case be several years away. In the meantime, the gas industry may be faced with either deficient governance arrangements or a further proliferation of narrow single purpose codes and agreements to govern emerging schemes/initiatives. We consider that this would be a retrograde step and essentially exacerbate the very problem that SPAA was originally set up to address.

2.64. Since the SPAA went live in 2004 there have been several attempts to encourage non-domestic suppliers' participation, but so far with little success. We also note that there are currently two further proposals which seek to resolve the issue.[25] The proposals have so far focused on the perceived inequity in the voting arrangements and have generally sought to give smaller parties an effective blocking minority in order to prevent the imposition of change by the so called Big 6 energy suppliers. Under the current arrangements, changes to mandatory schedules (or to those clauses specified in SPAA paragraph 9.1) will only be forwarded on to the Authority for its final consent where they achieve in excess of 65% support from all of the categories of party that declare an interest.[26] In the event that a change does

[24] www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Documents1/Tackling%20gas%20theft%20decision(1).pdf

[25] CP12/209: 'Amendment to Supplier Voting Constituencies' and CP12/217:'Creation of Small and Large Supplier Constituencies'

[26] Changes which have only a voluntary or elective status will need to pass the same voting threshold but do not require the consent of the Authority to be implemented.

not receive 65% support at the voting stage, the proposer and/or supporters of the proposal would then have to appeal to the SPAA Forum and if that appeal failed, subsequently to the Authority, in order for it to be approved.

Our proposals

2.65. Given that the issue of participation is increasingly inhibiting the contribution the SPAA can make to resolving industry matters such as theft of gas, we are now of the view that it would be appropriate for Ofgem to work more closely with Parties to find a solution. We consider that this wider review of the effectiveness of self governance is an opportune time to do this.

2.66. We acknowledge that smaller suppliers have concerns that the voting is weighted based upon the number of supply points held and the perceived inequity of this. It is therefore understandable that efforts so far have concentrated on establishing a constitution in which the Big 6 suppliers will not be dominant in at least one category, allowing for what would in effect be a blocking minority. However, we consider that relying solely upon a blocking minority as a safeguard for smaller suppliers' interests could stymie change and/or require a greater number of appeals to be brought to the Authority. This would not be effective governance, not least because an appeal process is more administratively burdensome to all concerned and would generally create greater uncertainty, over a longer period, than a normal determination.

2.67. There are existing safeguards within the SPAA, such as a second-tier voting system whereby the introduction of, or changes to, a mandatory provision requires the support of two thirds of Parties on a 'one Party one vote' basis, over and above the outcome of the weighted vote. However, we do recognise that the role of Ofgem in determining modification proposals, where the changes are assessed to have material impacts, provides a further degree of comfort to smaller parties that their interests will be fully taken into account. We consider that this could be achieved by more robust application of the self governance criteria, targeting Ofgem's participation in a consistent manner to other industry codes, rather than relying upon blocking votes or relying upon appeals.

2.68. To date, the role of the Authority in the SPAA has been mainly at arms' length, in keeping with our original intention; the SPAA process has generally allowed for changes that might have otherwise required Authority sign off to be progressed through self governance, rather than vice versa. The SPAA has adopted a materiality test[27] for self governance decisions, whereby the proposer indicates their view on whether the proposal requires the Authority's consent, rather than relying solely upon prescription of certain 'protected' clauses within the document. However, whilst

[27] Change Proposal 08/120 which was implemented in February 2009 modified the SPAA such that regardless of whether the proposal impacted upon a 'protected' clause, the proposer should indicate whether they considered the change would require the Authority's consent or not and their reasoning.

it is appropriate for the proposer to make such representations, we consider that this should be a determination for the SPAA panel,[28] consistent with other codes.

2.69. We therefore consider that the SPAA change provisions should be amended such that an assessment should be made of each modification proposal against self governance criteria, and any change considered to have material impacts against these criteria will come to the Authority for a decision, regardless of whether it passes an initial vote.

2.70. For the avoidance of doubt, we do not seek to prejudge the outcome of the current SPAA change proposals (CP12/209 and CP12/217) or seek to prescribe how the various constituencies within SPAA should be defined. We consider that our proposals would complement any change to the constituencies, or indeed the voting arrangements more generally.

2.71. We also recognise that any change control will be fundamentally undermined if there is no effective means of ensuring that parties subsequently comply with the decisions made. We note that concerns have been raised that while non-domestic supplier accession to the SPAA remains voluntary, any such Party that did not wish to comply could ignore the decision in the knowledge that the SPAA itself has few remedies. In the extreme, it could simply leave the SPAA.

2.72. We therefore propose to migrate the provisions relating to the SPAA that are currently set out in Standard Licence Condition 30, within Section B of the Gas Suppliers licence, which is applicable only to domestic suppliers, to Section A which would capture all Gas Suppliers. Recognising the lack of non-domestic participation in the SPAA to date, we propose that the licence would clarify that compliance is limited to the 'relevant provisions' of the SPAA, as may be further detailed within the SPAA itself. This would not only allow the SPAA to retain a domestic-only focus where appropriate, but ensure that non-domestic suppliers have the opportunity to vote upon and influence the development of any new or existing provisions before they are applied to them. We propose that the relevant licensees would lead on the development of consequential code modification proposals to this effect.

2.73. **We would welcome views on whether it is appropriate to obligate non-domestic suppliers to accede to the SPAA.**

2.74. **We also welcome views on whether all modification proposals which are assessed as having a material impact (on consumers and competition, etc) should be subject to Authority determination, in line with other codes.**

[28] Or by the SPAA Change Board, a committee of the panel formed to consider proposed amendments to the code.

Self governance appeals process

2.75. In our CGR final proposals we consulted on the proposition that all code parties, including consumer groups, should have the right to appeal any decision made under self governance. The majority of respondents to our CGR consultation agreed that this is an important safeguard, particularly where a party's competitors may be responsible for the decision. This is most acute where the decision is taken by a panel of relatively few people; although the need for a safeguard applies equally to those who may be in the minority interest when a matter is put to a vote of all parties.

2.76. We have drafted guidance on the appeals process, focusing on those aspects which will be for Ofgem to administer and therefore sit outside of the codes. Our aim is for this appeals process to be streamlined and, as far as practical, common across all industry codes. This guidance is attached as Appendix 7.

2.77. Furthermore, in light of feedback from code administrators, we are proposing an amendment to the original CGR licence modifications to change the appeal window for self governance decisions. This is currently 15 working days 'from decision' and we propose to amend the appeal window to begin 'from publication' in order to ensure that all parties have the benefit of the published final modification report and reasons for the panel decision from the outset of the appeal window. In light of this clarification, we would also welcome views on whether a 10 working day window would be more beneficial to avoid adding an unnecessary delay to the implementation of self governance modifications.

2.78. **We would welcome views on the self governance appeals guidance and on the proposed amendments to the appeal window.**

2.79. We also propose to seek better alignment of the appeal processes across the codes. The DCUSA appeal mechanism is currently limited to a point of process, namely that a proposal should have been treated as a 'Part 1' rather than a 'Part 2' matter, rather than an appeal against the eventual decision itself. We consider that this is an unnecessarily restrictive scope of appeal and that parties who do not consider a modification proposal to have been correctly categorised should submit a representation during the course of a normal consultation, highlighting their concerns to both the DCUSA panel and Ofgem at an earlier stage.

2.80. Under MRA and SPAA, code provisions which set out the eligibility for an appeal to be raised are more restrictive than those set out under the CGR. An appeal can only be made where a party believes the change may unfairly prejudice their interests or put them in breach of the relevant code or licence. As with the DCUSA, a decision cannot be appealed on the basis that a party disagrees with the assessment whether the change better achieves the relevant objectives.

2.81. **We would welcome views on whether the ability to appeal a self governance decision to the Authority should be applied equally across all industry codes.**

3. Significant Code Reviews

Chapter Summary

Ofgem's Code Governance Review introduced the Significant Code Review (SCR) mechanism to facilitate complex and significant changes to the industry codes. Initially implemented only in the BSC, CUSC and UNC, we are now consulting on proposals to extend SCRs to all codes.

Question 1: Do you agree with the proposal to extend the Significant Code Review process to DCUSA, iGT UNC, MRA, SPAA, STC, Grid Code and Distribution Code?

3.1. The CGR defined a role for Ofgem to lead complex changes to the industry codes with the introduction of Significant Code Reviews (SCRs).[29]

3.2. The code arrangements had been severely tested in key areas significantly impacted by public policy issues such as sustainable development and security of supply. The CGR recognised that further strategic issues were likely to arise over the coming years which would have a significant impact on the code arrangements. It was considered that the incremental and 'bottom up' approach to change was not effective for the large-scale reform this would require.

3.3. The CGR sought to ensure that significant code changes could be facilitated more quickly and effectively, particularly given the challenges presented by the government's social and environmental energy goals, and the possibility of changes required as a result of European legislation. The inefficiencies and potential delays we identified could hamper implementation of important code reforms and could therefore have direct negative impacts on, for example, competition, new entrants and ultimately consumers.

3.4. The SCR process was thus established to deal with matters which:

- could be given effect wholly or mainly through modification of the relevant industry codes; and
- the Authority considers to be of significance in relation to its principal objective and/or statutory duties and functions or obligations arising under EU law, including in particular matters:
  - likely to have a significant impact on gas and electricity consumers or on competition (this may be based on a qualitative assessment); and/or
  - likely to have a significant impact on the environment, sustainable development or security of supply; or
- are likely to create significant cross-code or code-licence issues.

[29] See Appendix 2 of the CGR final proposals: http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/CGR_Finalproposals_310310.pdf

3.5. During the CGR we consulted on whether to prioritise implementing SCR procedures within the BSC, CUSC and UNC only, or to roll these out to all of the industry codes. Views were fairly evenly divided between the two options. We subsequently decided that it would be pragmatic to prioritise the BSC, CUSC and UNC as major policy reform was most likely to be implemented through changes to these codes. However, we did not rule out that an SCR would affect other codes and that the SCR process may be extended to other codes in due course.

3.6. To date we have launched three SCRs covering:

- Gas Security of Supply arrangements;[30]
- Electricity Charging arrangements (Project Transmit);[31] and
- Electricity Balancing.[32]

3.7. In our April open letter we asked for views on whether the frequency, timings and process of the SCRs to date had met with industry expectations based on what we outlined in the CGR.

Respondents' views

3.8. Feedback was generally positive in terms of how the process has met with stakeholder expectations although a number of respondents highlighted that it was too soon to provide a full appraisal of the SCR process as one has yet to be fully completed.[33]

3.9. Most respondents were satisfied with the guidance Ofgem has provided in respect of the SCR process. There was some criticism that the SCR process thus far has been too long. It was however also recognised that a balance should be struck between allowing sufficient time to reach robust conclusions and completing the process in a timely manner. Some respondents expressed views that the process had improved as it has 'bedded in', particularly in terms of greater industry involvement.

3.10. There was some support for extending SCRs to other codes, particularly in light of forthcoming work on European network codes and smart grids, although others suggested that provisions already exist for consequential changes to be made to other relevant codes, meaning that further SCR provision may not be necessary.

[30] Information about the gas Security of Supply SCR is available on our website: http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/GasSCR/Pages/GasSCR.aspx
[31] Information about TransmiT is available on our website: http://www.ofgem.gov.uk/Networks/Trans/PT/Pages/ProjectTransmiT.aspx
[32] Information about the Electricity Balancing SCR is available on our website: http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/electricity-balancing-scr/Pages/index.aspx
[33] The Authority published its conclusions on Project Transmit on 4 May 2012. Subsequent code modifications are pending.

Our proposals

3.11. In order to ensure that complex or cross-code changes are achieved most efficiently going forward we consider that it would be beneficial to incorporate the SCR process into all remaining codes. We do not believe this will cause substantial costs as only small changes to the prevailing modification rules to reflect the existence of the SCR process will be required. The likely costs associated with any subsequent SCR would be fully assessed prior to its launch.

3.12. Our guidance on the SCR process indicated that these would take approximately 12 months to complete. We appreciate that this may be a tight timeframe for especially complex issues and should be taken as a guide only. An extended timeframe may sometimes be required in order for sufficient analysis and consultation to be conducted. The actual timetable will be determined by the circumstances of the SCR and the proposed timetable set out in the launch statement.

3.13. We acknowledge that provisions for consequential modifications have in the past been effective in updating related arrangements in other industry codes. However, we do not consider that relying on this is the most efficient way of ensuring that significant change is effected throughout the codes. The SCR process approaches change in a holistic manner, incorporating non-urgent modifications on related matters; this enables more timely, streamlined and coordinated change to take place. Furthermore, although it is less likely, there remains a possibility that an SCR may be required that does not impact on the BSC, CUSC or UNC.

3.14. We have not yet undertaken an SCR which has impacted on more than one code. However, we recognise the potential for significant cross-code issues to arise in the future. For example, the work Ofgem has initiated to identify potential market developments arising from Smart Metering[34] and future implementation of European Network Codes could impact across a number of technical and commercial codes and is unlikely to be restricted to the BSC, CUSC and UNC.

3.15. We consider that the principles set out by the CGR in respect of SCRs are fit for purpose and we will continue to consult with stakeholders on potential SCRs before deciding whether to proceed. We do not consider that amendments to the process are required in order to roll this out to other codes, however, we do appreciate feedback provided on the SCR guidance and will consider whether appropriate refinements to this can be made in due course, especially around management of expectations on timing and resource commitments.

3.16. **We welcome views on our proposal to extend SCRs into the code modification processes of DCUSA, iGT UNC, MRA, SPAA, STC, Grid and Distribution Codes.**

34 http://www.ofgem.gov.uk/Markets/sm/strategy/Documents1/Promoting%20smarter%20energy%20markets%20-%20a%20work%20programme.pdf

4. Code Administration

Chapter Summary

This chapter considers how improvements made to the code governance processes as a result of the CGR could be extended to other industry codes.

Question 1: Do you agree that all industry code panels (or their equivalent) should provide substantive reasons for their recommendations/decisions?
Question 2: Do you agree that the MRA should contain objectives against which code modifications are assessed?
Question 3: Do you agree that the Authority should be able to 'send back' final modification reports in all codes, where a deficiency/flaw in the report is identified?
Question 4: Do you agree with the proposal to require all codes to have regard to and, to the extent relevant, be consistent with the CACoP principles?
Question 5: Do you consider that a requirement on code administrators to fulfil a 'critical friend' role should be set out in the relevant licence?
Question 6: Do you agree with the amendments to the CACoP (Appendix 2) and do you consider that the standard process and templates described by the CACoP should have the status of guidance (rather than being mandatory) at this stage?

Introduction

4.1. The CGR considered ways in which the performance of code panels and code administrators might be improved in respect of governance structures, quality of analysis and quality of service.

4.2. The CGR final proposals identified a number of improvements which were subsequently implemented into the BSC, CUSC and UNC, including:

- a requirement upon code panels to provide reasons for their recommendations/decisions in respect of code modifications;
- the introduction of 'send back' powers;
- the introduction of the Code Administration Code of Practice (CACoP); and,
- the concept of a code administration 'critical friend'.

4.3. Since their introduction to the BSC, CUSC and UNC these initiatives have made a marked improvement to the governance of those codes, with an increased focus on critical analysis. We consider that similar benefits could be achieved in the other industry codes.

Reasons for recommendations and decisions

4.4. The initial CGR introduced licence requirements in respect of certain codes requiring an evaluation of whether any revision to the code would better facilitate achievement of the relevant objectives.[35] The extent to which code panels provide substantive reasons for this assessment does however differ; the absence of a supporting rationale could undermine the value of a recommendation.

4.5. A similar issue exists in those codes in which matters are determined by a vote of all parties rather than an appointed or elected panel, insofar as there is often very little by way of supporting reasons. Knowing which is the more popular view is not in itself sufficient when the Authority makes its subsequent decision, which in most cases must be based on an assessment of whether the modification would further the objectives of the code as well as our principal objective and broader statutory duties.[36]

4.6. We consider it important for consistency and certainty that a recommendation is made to the Authority on the same basis as the subsequent decision, ie based on an assessment against the same criteria,[37] being the code relevant objectives. We also consider that panel members, when acting as representatives of code parties, should be accountable for their voting decisions, whether in determining self governance modifications or making a recommendation in respect of modifications being referred to the Authority for decision.

4.7. The CGR final proposals specifically required BSC, CUSC, UNC and iGT UNC modification reports to contain explanations of whether, and if so how, the proposed modification would better facilitate the code's relevant objectives. This requirement was introduced to help ensure rigorous and high quality analysis and increase transparency by imposing discipline on panel members to explain their reasoning. This aids both clarity and understanding. In the case of decisions that are appealed, it is particularly important to ensure that the basis for decisions is clearly documented.

4.8. Our April open letter sought views on whether this requirement had been effective in improving analysis to support code changes.

Respondents' views

4.9. Respondents noted that improvements have been achieved in the quality of modification reports following the CGR, particularly in the UNC processes, ensuring that the panel recommendations are robust and transparent. Some respondents commented that they had not detected improved reporting, but noted that BSC and

[35] In addition to BSC, CUSC and UNC, the initial CGR also required iGT UNC, DCUSA, STC, Grid Code and Distribution code to assess changes against the relevant objectives.
[36] The MRA does not presently define relevant objectives.
[37] The Authority must also take account of its statutory duties, but this is not a requirement on code panels/parties.

CUSC panels already recorded reasons for their recommendations prior to the CGR final proposals being implemented.

4.10. It was commented that the requirement on panels to provide reasons for their recommendations has been a positive step, along with 'send back' powers (discussed below), to enhance the change and decision-making processes. One respondent said that the information given by panels in the final modification report is useful in assisting code parties to communicate change internally. It was further suggested that this has also encouraged proposers and workgroups to provide information demonstrating the advancement of the relevant objectives.

Our proposals

4.11. We propose to introduce (or in the case of the codes that already have them, to clarify) obligations within the code owners' licences such that the reasons for recommendations and decisions must be contained within the final modification report submitted to the Authority (or in the case of self governance, in the final decision document). These recommendations must be based upon and explained in reference to the relevant objectives,

4.12. We acknowledge that some panels do already provide reasons for their recommendations, although the rigour applied to those reasons differs significantly between codes, as does the extent to which they are recorded with explicit reference to the code's relevant objectives. The different approaches may owe as much to the custom and practice that has evolved over the years as the differing requirements formally placed upon the panels. For instance, under the current DCUSA and SPAA arrangements the code panels do not provide a recommendation to the Authority, rather the recommendation on whether to accept or reject a proposed change is formed pursuant to a party vote.

4.13. Where the codes provide for the final decision/recommendation to be taken by a party vote, we nonetheless consider that these principles can be applied. It would be beneficial if the modification report upon which votes are sought contained an initial assessment of whether or not the proposal better meets the code's relevant objectives and the reasons for this evaluation. This function is generally fulfilled by the workgroup in compiling the modification report (or in the absence of a workgroup, by the code administrator, subject to approval of the relevant panel). Respondents should then be asked to comment on that assessment when issuing their vote, stating whether or not they agree that the change furthers the relevant objectives rather than simply whether they support the implementation of the proposal.

4.14. In this respect we propose to clarify that the DCUSA, MRA and SPAA procedures should allow for parties to submit their vote on whether to accept or reject a proposal, having first had the opportunity to consider the modification report, and having considered whether the proposed change would better facilitate the relevant objectives as compared to the baseline.

4.15. Under the current arrangements of the Grid Code and Distribution Code, the panel recommendation is advisory and the formal recommendation to the Authority is made by the licensee(s). We consider that clear and transparent reasons for recommendations are also required in these codes.

4.16. We consider that this proposal is proportionate as it will enhance transparency and ensure that rigorous high quality analysis is undertaken through the code modification process. We do not consider that there should be any material costs incurred by formalising this reporting requirement.

4.17. **We therefore seek views on placing a specific obligation on all panels (or their equivalent) to provide substantive reasons for their recommendations and/or decisions.**

MRA Objectives

4.18. We also welcome views on our proposal to introduce objectives into the MRA, in line with other industry codes. It appears an anomaly that the MRA is the only industry code which does not state relevant objectives against which changes to that code should be assessed.

4.19. We consider that introducing such objectives would improve transparency and aid more robust analysis of the justifications for a change. Measures to improve quality of analysis are consistent with other proposals we have made under this consultation. The removal of unnecessary differences between similar codes also reduces complexity and therefore aids party engagement in the code arrangements.

4.20. The objectives we have proposed are consistent with existing provisions of the Distribution licence in respect of the MRA, and are aligned with the objectives of the SPAA.[38]

4.21. **We welcome views on our proposal to clarify the existing arrangements by formally setting out the MRA relevant objectives.**

Send back powers

4.22. As set out in the CGR final proposals, we consider that where the Authority is unable to properly make a decision on a proposed modification, whether for reasons of insufficient analysis or flaws in the accompanying legal text, the modification process should allow for corrective action to be taken. This is preferable to the sub-optimal choices of either accepting a flawed proposal or rejecting one which is sound in principle.

[38] The SPAA performs equivalent functions in the gas market.

4.23. A recent example of where the current arrangements were not effective is DCUSA change proposal DCP088, which was rejected by the Authority on the basis of insufficient legal text.[39] As no send back process presently exists within this code, it was not possible to return the modification report for this matter to be corrected.

4.24. It should also be noted that the use of 'send back' powers is envisaged only as a last resort[40] and we would, wherever practical, ensure that any concerns we have are appropriately raised at an earlier stage in the process. However, there may be occasions where new issues come to light, or issues could not have been reasonably foreseen by us (or indeed the panel) earlier in the process.

Our proposals

4.25. At a practical level, we consider that the inability to take corrective action on final modification reports in some codes can lead to inefficiencies in both time and costs incurred by industry in re-raising a modification proposal and again pursuing it through the modification process. This could be avoided by the send back provision. We therefore propose that the remaining industry codes should provide for the revision and re-submission of the final modification report if the Authority determines that it cannot properly form an opinion as to whether the proposed modification would better facilitate the relevant objectives.

4.26. We consider that the costs of adopting these provisions would be marginal, and quickly offset with greater savings, although we would welcome comments on this, particularly from those with practical experience of the send back process and/or the issues it is designed to address.

4.27. **We seek views on our proposal to implement 'send back' powers into the code modification procedures of DCUSA, iGT UNC, STC, MRA, SPAA, Grid Code and Distribution Code.**

Code Administration Code of Practice (CACoP)

4.28. During the CGR we identified that the code arrangements were highly fragmented. Market participants needed to devote significant resources in order to understand, let alone engage in and influence, policy outcomes. This placed an administrative burden and associated costs upon all parties, although we considered that the problem was particularly acute for new entrants, smaller participants and consumer representatives.

4.29. We were particularly concerned that this complexity was constraining the degree of participation in the codes process and that this may hinder competition,

[39] http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=79&refer=Licensing/ElecCodes/DCUSA/Changes

[40] To date, three Final Modification Reports have been returned by the Authority for further analysis or to correct defective legal text.

insofar as it stymied the extent to which new entrants and incumbents alike could stimulate innovation. This could lead to inefficiencies, and moreover, it may act as a barrier to entry and growth by creating a distorted perception of the risk of operating in the market.

4.30. The facilitation of small participant engagement in the industry code processes was a consistent theme throughout the CGR and became the driver for several initiatives, including the concept of a code administration 'critical friend'.[41]

4.31. The CACoP was developed from the recommendations of a Code Administration Working Group (CAWG), which set out to explore, identify and subsequently progress opportunities to make the code modification processes more accessible, usable and transparent for all parties. The CAWG focused on improvements that could be made without significant structural change; for instance through modifications to existing code rules or simply by changing established custom and practice.

4.32. CACoP established certain principles that are considered to capture the key elements of best practice in the administration of code modification procedures. It also provides a template for the ongoing convergence and simplification of existing code rules. For instance, by referring to the CACoP alone, any participant should understand the fundamentals of the modification processes that apply under the UNC, BSC and CUSC to a sufficient extent that they can participate in those processes without having to familiarise themselves with three disparate sets of modification rules.

4.33. Whilst the CGR final proposals focussed primarily on the BSC, CUSC and UNC, we considered that the principles of the CACoP could appropriately be applied to all industry codes. Indeed, we understand that the CACoP principles are currently being followed in other codes on a voluntary basis.

4.34. Our April open letter sought views on whether adherence to the CACoP should be implemented under all industry codes.

Respondents' views

4.35. Responses to both our April open letter and our earlier consultation facilitating the CACoP review showed support for the CACoP. Respondents stated that consistent processes and promotion of greater stakeholder engagement have been positive outcomes of its implementation, as well as an increased focus on the involvement of smaller parties. The clarification of the role of the code administrator was also welcomed and it was noted that the CACoP aids delivery and understanding of code governance arrangements, helping parties to engage across several codes.

[41] The 'critical friend' licence condition describes a requirement on the code administrator to provide assistance to parties, on request and insofar as is reasonably practicable, in relation to drafting a modification proposal, understanding the operation of the code, and their involvement in the modification processes (amongst other things). Particular reference is made to small participants and consumer representatives.

4.36. Views were mixed on whether a formal roll out of CACoP to other codes would be helpful. Some respondents, whilst in principle supportive of a wider roll out, suggested that aligning all processes with the 'standard' process set out in the CACoP could be a significant piece of work, the administrative burden of which could outweigh any benefits that would be introduced. Some respondents thought that as the codes are inherently different, a strict 'one size fits all' approach may not produce significant benefits over and above streamlining at a higher level. Others disagreed, stating that it would be useful to incorporate the CACoP into the remaining codes to encourage standardisation of processes. Again, the degree to which the smaller codes had voluntarily adopted the principles was noted.

Our proposals

4.37. It remains our long-term aspiration for all industry code modification procedures to converge, with variations between modification rules only remaining where they fulfil a specific need or create a benefit. Whilst such convergence is not directly within the scope of this consultation, we consider that this long-term aspiration will (subject to the caveat set out above) be facilitated by an initial requirement upon all codes to have regard to the principles set out in the CACoP. Irrespective of whether this aspiration is ever achieved, we consider that adherence to the principles set out in the CACoP will make the governance of the codes more robust, facilitate a greater degree of participation, and generally lead to more effective decision-making.

4.38. To the extent that these principles are already being adhered to, we do not consider that there is any additional burden in placing this on a more formal footing. However, we foresee a benefit in introducing a licence requirement to ensure compliance on an enduring basis, so that the principles are not subject to changes in custom and practice that might be expected over time.

4.39. **We seek views on our proposal to require DCUSA, iGT UNC, STC, MRA, SPAA, Grid Code and Distribution Code to have regard to the CACoP to the same extent as the UNC, BSC and CUSC.**

Critical Friend

4.40. As mentioned above, the 'critical friend' role was introduced into the BSC, CUSC and UNC as part of the implementation of the CGR, enacted both through modifications to the relevant licence conditions and by way of the requirement to adhere to Principle 1 of the CACoP.[42]

4.41. We envisaged that, at a minimum, this role would provide assistance to smaller participants and consumer representatives with the drafting of modification proposals, where requested. This could extend to guidance on legal text and providing a plain English explanation of the relevant code arrangements. As smaller

[42] CACoP Principle 1 states that 'code administrators shall be critical friends'.

parties and consumer representatives may suffer from an asymmetry of information compared to the larger parties, we also considered that code administrators had a duty to provide access to such information where reasonably available to them.

4.42. The critical friend role should also ensure that any issues or queries that have been raised by small participants or consumer representatives are appropriately addressed regardless of whether they are able to physically attend subsequent workgroups and panel meetings themselves.

4.43. Our April open letter sought views on whether the requirement for relevant code administrators to act as a critical friend had been effectively embraced.

Respondents' views

4.44. A number of respondents felt that the critical friend role had been successfully implemented by the code administrators of the BSC, CUSC and UNC. Some also felt that the remaining codes had successfully taken on this role, including the MRA, Distribution Code, iGT UNC and DCUSA.

4.45. One respondent commented that the expertise of the code administrators reduces wasted time, delivers better quality proposals and supports smaller parties. Another welcomed the increased focus that had been brought to the code administrator role.

4.46. Whilst generally supportive of the 'critical friend' concept, a number of respondents did not consider it should be a requirement of the remaining codes.

Our proposals

4.47. We remain of the view that the critical friend role is central to improving accessibility to the codes for all market participants, and therefore ultimately will have a positive impact on competition. Notwithstanding that some codes may have successfully taken on this role on an informal basis, formalising this requirement is relevant to ensuring transparency, clarity and consistency in the performance of the role.

4.48. We recognise that the requirement to provide reasonable assistance to parties may have some direct financial impacts due to the way that different codes are funded. However, we consider these to be relatively minor as the fundamental requirement is the provision of expert code-specific advice. We also note that some codes are already voluntarily adopting this principle and therefore should not incur additional costs in formalising this role.

4.49. We would not necessarily expect the extent of assistance offered to be consistent across all of the codes, as we recognise that some code administrators will be better placed and better resourced than others to fulfil this role. However, stakeholder feedback may be a useful indicator of what is particularly effective and (potentially) where code administrators should focus their efforts. At a minimum, we

would expect the critical friend to provide a degree of initial feedback and quality assurance on modification proposals. A well-drafted proposal can be progressed more efficiently and this should save time and resources for all concerned, including the code administrator, which could more than offset the initial administrative burden.

4.50. We do recognise that with the critical friend concept being set out in the licence and subsequently adopted as a CACoP principle there is a degree of duplication of this requirement. However, as set out above, we consider the critical friend role to be of fundamental importance and therefore believe it would be appropriate to retain the obligation in the licence.

4.51. Given the limited participation of parties other than transmission licence holders, we consider that the critical friend concept may not be required in STC.

4.52. **We would welcome views on whether a requirement on code administrators to fulfil a 'critical friend' role should be set out in the relevant licence.**

CACoP Review

4.53. In cooperation with the relevant code administrators a review of the CACoP was undertaken earlier this year. Views were sought on how well it had been implemented and how effective the principles were in practice. We provide details of this review as Appendix 2.

4.54. Whilst changes to the CACoP are not strictly within the scope of this review, we consider that this document provides an appropriate opportunity to consult on the proposed changes, particularly in the context of the CACoP's proposed extended coverage. We do not consider the changes proposed to be material.

4.55. **We would welcome views on the proposed amendments set out in Appendix 2, as well as the additional clarification around the status of the standard modification process and templates referred to in the CACoP.**

5. Way forward and timetable

Chapter Summary

This chapter highlights next steps and sets out the proposed timetable for relevant licence and code changes to take effect.

Question 1: Do you agree with the timetable proposed?

5.1. Some responses to our April open letter commented on the timing of this review, querying whether it is a priority at the present time in light of the forthcoming volume of change to the regulatory framework.

5.2. We recognise that there are key strategic issues facing industry over the near- and long-term resulting in an increasing industry workload. It is important that industry and Ofgem are able to manage this workload effectively, and the code governance arrangements play an important role in this. We therefore consider that these forthcoming challenges make it all the more urgent that the governance framework is as robust and efficient as possible.

5.3. Recognising industry feedback on managing the changes that would be required as a result of this second phase CGR, we would welcome specific views from parties on the proposed implementation timescales.

5.4. The initial CGR allowed for approximately six months from statutory notice of licence modifications to implementation of subsequent code modifications and we have proposed similar timings for the second phase. Notwithstanding that implementation of the second phase should be eased by the fact that the code modification processes are already established in the BSC, CUSC and UNC, which can therefore be used as a model for the smaller codes to adopt.

5.5. The proposed timings below are as follows:

- Responses to this consultation – 23 November 2012
- Publish conclusions/way forward and statutory consultation on licence modifications – January 2013
- Licence modification directions issued – February 2013
- Licence modifications take effect – April 2013
- Code modifications made by – July 2013

5.6. **Do you agree with the indicative timetable proposed?**

5.7. We propose to hold a workshop for interested parties on Friday 2 November 2012 as a forum to discuss these proposals and draft licence conditions. If you would like to attend please email us at industrycodes@ofgem.gov.uk by 24 October.

Appendices

Index

Supplementary appendices

Appendix 1 - Consultation Response and Questions

1.1. Ofgem would like to hear the views of interested parties in relation to any of the issues set out in this document.

1.2. We would especially welcome responses to the specific questions which we have set out at the beginning of each chapter heading and which are replicated below.

1.3. Responses should be received by 23 November 2012 and should be sent to:

- industrycodes@ofgem.gov.uk; or
- Industry Codes & Licensing, Ofgem, 9 Millbank, London SW1P 3GE

1.4. Unless marked as confidential, all responses will be published by placing them in Ofgem's library and on its website www.ofgem.gov.uk. Respondents may request that their response is kept confidential. Ofgem shall respect this request, subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.

1.5. Respondents who wish to have their responses remain confidential should clearly mark the document(s) to that effect and include the reasons for confidentiality. It would be helpful if responses could be submitted both electronically and in writing. Respondents are asked to put any confidential material in the appendices to their responses.

1.6. Any questions on this document should, in the first instance, be directed to:

Lisa Charlesworth
Industry Codes & Licensing
Ofgem, 9 Millbank, London SW1P 3GE
0207 901 7164
industrycodes@ofgem.gov.uk

Questions

CHAPTER: Two

Question 1: Do you consider that a 'fast track' self governance process should be available in the industry codes for minor housekeeping changes?

Question 2: Do you agree that the Agency Charging Statement should fall under the governance of the Uniform Network Code, rather than the Gas Transporter licence?

Question 3: Do you agree that self governance should be introduced into the iGT UNC and STC, and increased in the DCUSA?

Question 4: Do you consider it appropriate to apply the same governance principles to the Grid and Distribution Codes as are applied to the commercial codes?

Question 5: Do you consider that both the Distribution Code and the Grid Code should be modified to allow for an open governance framework? In particular, allowing code users to raise code modifications; enabling code panels to have a more formal role in evaluating and recommending code changes; and the governance procedures brought into the codes? Are there any other areas of governance that you consider could be improved in Distribution Code and Grid Code?

Question 6: Should MRA modifications be subject to a materiality test, to determine whether Authority approval of changes is required?

Question 7: Do you consider that it is appropriate to obligate non-domestic gas suppliers to accede to the SPAA?

Question 8: Do you agree that SPAA modifications should be subject to a materiality test, to determine whether Authority approval of changes is required?

Question 9: Do you have any comments on Ofgem's guidance for discharging self governance appeals (Appendix 7), and on the proposed adjustment to the BSC, CUSC and UNC appeal windows?

Question 10: Do you consider that the ability to appeal a self governance determination should be consistent across all codes?

CHAPTER: Three

Question 1: Do you agree with the proposal to extend the Significant Code Review process to DCUSA, iGT UNC, MRA, SPAA, STC, Grid Code and Distribution Code?

CHAPTER: Four

Question 1: Do you agree that all industry code panels (or their equivalent) should provide substantive reasons for their recommendations/decisions?

Question 2: Do you agree that the MRA should contain objectives against which code modifications are assessed?

Question 3: Do you agree that the Authority should be able to 'send back' final modification reports in all codes, where a deficiency/flaw in the report is identified?

Question 4: Do you agree with the proposal to require all codes to have regard to and, to the extent relevant, be consistent with the CACoP principles?

Question 5: Do you consider that a requirement on code administrators to fulfil a 'critical friend' role should be set out in the relevant licence?

Question 6: Do you agree with the amendments to the CACoP (Appendix 2) and do you consider that the standard process and templates described by the CACoP should have the status of guidance (rather than being mandatory) at this stage?

CHAPTER: Five

Question 1: Do you agree with the timetable proposed?

Appendix 2 – CACoP review outcomes

2.1 We initiated a review of the CACoP in December 2011, a year following its implementation. We sought to gain feedback from code administrators who have adopted the CACoP and users of those codes. We particularly sought to gain views on how successfully the CACoP had been implemented and how effectively the principles are being achieved in practice. Responses received to this consultation are published on the Ofgem website.[43] This user feedback provided the basis for the potential amendments to be considered by a working group convened to review the CACoP as per Principle 4 of the document.

2.2. A meeting of the BSC, CUSC and UNC code administrators was held on 7 March 2012 to discuss issues raised following the CACoP's implementation and the results of the Key Performance Indicator (KPI) reporting. This was also an opportunity for the code administrators to discuss best practice in the application of the CACoP principles.

2.3. On 24 April 2012 a working group was convened to review the CACoP, discussing the various issues that had been raised by code administrators and code users. This working group was referred to as a 'Code Administrators' Working Group' (CAWG) for this purpose. We set out below a summary of the issues considered, Ofgem's views and our proposed way forward.

Code Administration KPIs

2.4. Ofgem agreed with industry feedback that targets against the code administration KPIs contained in the CACoP should not be set at this stage.

2.5. A small number of minor changes were suggested to the specific KPIs measures, in order to aid reporting:

- It was agreed that the KPI measuring 'effective communication' in terms of code modification reports would be better reported as a qualitative measure. It was suggested that a question could be included in the code administrators' user surveys each year; this would enable code administrators to review the responses and learn from them.
- There was general agreement that rather than measuring the 'percentage' of reports sent back by the Authority it should be the 'number' of reports sent back only.

[43] http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=375&refer=Licensing/IndCodes/CGR

2.6. Ofgem supports these changes and we propose implementation as soon as practicable for each code administrator (ie either current or next reporting year). We consider that the next review of the CACoP could take a more detailed look at the KPI measures, refining these where needed to ensure that there is a core set of common KPIs that all codes can usefully report on and that will inform the development of best practice.

Standard Templates

2.7. There was discussion on the status and format of the standard templates that were produced alongside the CACoP. One participant put forward specific amendments to the templates for consideration.

2.8. Views were divided on whether the templates should form part of the CACoP and be the required format for modification proposal forms and reports. One view was that these should be adopted by all codes in the prescribed form and should be subject to amendment along with the CACoP itself. Other views were that the templates should be considered as guidance only to allow for some flexibility between codes where appropriate. The majority opinion was that a standard structure is beneficial to set out what, as a minimum, must be included in the modification documents, but that the templates are more useful as guidance rather than a fixed format. A balance between flexibility and convergence therefore seemed appropriate.

2.9. Ofgem's view is that the modification document templates should be considered guidance at this stage. We recognise that whilst individual differences exist between the code modification processes, there is a need for flexibility in the form of code modification documentation.

2.10. We suggest that the code administrators can adjust the templates where necessary for their individual code's usage. We anticipate that code administrators will work openly in discussing and developing best practice and that these templates will be reviewed from time to time, in discussion with code users, in seeking to establish a common set of minimum requirements for all code modification documentation.

2.11. We are supportive of the views expressed by one work group member that code modification analysis and reporting should be submitted to the Authority in one complete document in order that it is clear to parties what information has been provided to the Authority for decision.

Standard Modification Process

2.12. As part of this review it was commented that if the original intention of the CACoP was to develop a standard modification process across the codes, the CACoP should take precedence over the codes if this was to be achieved. Another view was that this wasn't needed but that industry parties would need to ensure that the

standard process is implemented by raising modification proposals to the individual codes.

2.13. The 'standard modification process' does not form part of the 12 CACoP principles. Ofgem's view is that codes should adopt this at a high level, however individual differences between the codes (such has how they are funded or whether they allow for party voting on code modifications) may mean that individual differences justifiably continue to exist.

2.14. We maintain our view that the convergence and simplification of code processes is beneficial and should remain the long-term aim. We do not consider that complete uniformity across the codes is necessarily required in order for the present arrangements to be improved. Provided that the codes follow the set of high level principles and demonstrate clear, common stages of modification progression, some individual differences between codes may remain relevant and would not necessarily be detrimental to participation in those processes.

2.15. In terms of the indicative timetable accompanying the 'standard modification process', it was discussed at the working group that the timeframe for raising modification proposals should be made clearer to specify that these 'should' rather than 'must' be received eight days prior to a code panel meeting. We consider this wording should be amended to add clarity as in some cases late agenda items may be accepted.

Pre-modification processes

2.16. The CAWG discussed how the codes' pre-modification processes were working. There were no strong views on this, but it was suggested by one participant that a standard format may be helpful.

2.17. We consider that pre-modification processes are a key part of the overall governance processes and, if used effectively, will help code panels and administrators to ensure that modification proposals are well formed and fully considered prior to submission. This may be particularly beneficial with regard to open governance of charging methodologies where proposers may require additional information and guidance.

2.18. We encourage code administrators to share best practice and seek user feedback to ensure that their pre-modification processes are clear and accessible and that their profile is raised as a useful 'first step' in the code modification process. Best practice could be developed and housed in the CACoP through future reviews.

CACoP Review Process

2.19. There was general agreement amongst the CAWG participants that a process of consultation followed by engagement with a working group and a final consultation on change proposals is appropriate for maintaining the CACoP.

2.20. It is a requirement of the relevant licences that code administrators, in collaboration with each other, "maintain, publish, review and (where appropriate) amend" the code of practice. We recognise that Ofgem can play a useful role in co-ordinating future reviews, however, we anticipate that code administrators will take an appropriate lead in maintaining the CACoP. It would be practical for the code administrators to utilise their annual user surveys to seek feedback and prompt requests for changes to the CACoP, maintaining a log of changes to be discussed at the next review. We would also be supportive of the code administrators conducting reviews of the CACoP by way of a cross-code forum, or similar, to engage code parties on neutral terms, or by agreement amongst the code administrators to rotate responsibility for leading on the maintenance of the CACoP.

Compliance with the CACoP

2.21 As a result of the CACoP review, it became apparent that some uncertainty exists around the extent to which the codes are required to comply with the contents of the CACoP.

2.22 The relevant licence conditions require the code modification procedures to be consistent with the 12 high-level principles set out in the CACoP, to the extent that they are relevant. The code administrators are also required to have regard to, and to the extent relevant, be consistent with these principles.

2.23. The CACoP expands upon the 12 principles by adding a level of detail on how they may be adhered to. As stated above, the CACoP also sets out a standard process that the codes can be expected to follow, which aims to simplify the process for those who would otherwise have to familiarise themselves with differing sets of rules and procedures. A complementary set of standard templates are aimed at further clarifying and simplifying the process.

2.24. Whilst we expect the codes to be administered consistently with the 12 principles, the CACoP does not seek to prescribe how those principles will be achieved. Where the CACoP sets out a finer level of detail for each principle, and provides accompanying process and document templates, this should be considered as current best practice which the licensee must have regard to but does not preclude alternative and innovative approaches. Indeed, we would encourage licensees and code administrators to constantly improve upon current practices and we anticipate that the CACoP will evolve to reflect this.

2.25. We have been clear that should any conflict arise between the code modification rules and the CACoP, the relevant code shall take precedence. However, we do expect code administrators and licensees to proactively identify any areas of potential conflict and take reasonable steps to resolve them as appropriate, whether through modifications to their own code or by seeking revisions to the CACoP.

Appendix 3 – Code Overviews

DCUSA

3.2 All licensed electricity distributors are required by SLC 22 of the electricity distribution licence to ensure that the DCUSA is in force.

3.3. The DCUSA panel manages the modifications process. It consists of two persons elected by Distribution Network Operator (DNO) parties, one person elected by the Independent Distribution Network Operator (IDNO)/Offshore Transmission System Operators (OTSO) parties, two persons elected by the Supplier parties, and one person elected by the Distributed Generator (DG) parties. Ofgem can appoint an additional member if it deems that a category or interested party is not adequately represented.

3.4. Panel powers do not extend to recommending (or in the case of self governance, approving) code modifications, as the DCUSA provides for a party vote on all proposed code changes. Furthermore, the DCUSA panel do not play an active role in the drafting of the modification reports (or 'change reports' under current DCUSA terminology).

3.5. Electralink provides administrative and secretarial support to the DCUSA panel under contract to DCUSA Ltd.

3.6. DCUSA is funded by suppliers and distribution networks proportionate to their number of meters. Any code party can raise a modification proposal, as can the National Consumer Council, National Grid and any person designated by the Authority from time to time.

3.7. The panel Chair is elected by the panel from the panel members and does not have a casting vote.

iGT UNC

3.8. Independent Gas Transporters (iGTs) are required by SLC 9 of the gas transporter licence to create individual Network Codes. Ofgem implemented the iGT UNC under SLC 9 to streamline and co-ordinate the individual network code arrangements as far as possible. The independent gas transporters still maintain their own individual network codes for the requirements that are not contained within the iGT UNC.

3.9. The iGT UNC modification panel manages the modification process of the iGT UNC and the individual Network Codes. The panel consists of a non-voting independent chair appointed by the iGT UNC Operators, three iGT UNC Operators' representatives, and three Pipeline Users' representatives. A consumer representative, suppliers' representative, large transporters' representative and an Ofgem representative may also attend panel meetings.

3.10. Gemserv acts as the panel secretary and as the iGTs' representative, carrying out many of the functions of a code administrator.

3.11. This code is funded by the iGTs in proportion to their number of meters and all code signatories can raise modifications to the code.

MRA

3.12. The MRA is a requirement of SLC 23 of the Electricity Distribution licence. It is funded two thirds by suppliers and one third by DNOs, proportionate to their number of meters. Any party can raise a modification proposal.

3.13. The MRA Executive Committee consists of one DNO member, two Supplier members and one BSC representative. Management of the modification process is delegated to a Change Board.

3.14. Gemserv fulfils the secretariat role under contract to MRA Service Company Ltd.

SPAA

3.15. Section B SLC 30 of the gas supply standard licence conditions requires domestic gas suppliers to be a party to, comply with and maintain the SPAA.

3.16. The SPAA Executive Committee (SPAA EC) manages the modification process for the SPAA. The SPAA EC consists of two Non-Domestic Supplier Members, two Large Domestic Suppliers, one Small Domestic Supplier, two Large Transporters, and one Small Transporter. The National Consumer Council and an Ofgem representative may attend panel meetings.

3.17. Any party and the National Consumer Council can raise modifications. Electralink acts as the code secretariat under contract to SPAA Ltd.

STC

3.19. All onshore electricity transmission licensees are required by SLC B12 of the transmission licence to "have in force a STC". Offshore electricity transmission licensees are required by SLC E13 of their transmission licences to be a party to the STC Framework Agreement and comply with the STC.

3.20. The modification process for the STC is managed by the STC Committee which consists of a Chair (appointed from one of the STC parties), up to two representatives from each onshore STC Party and up to two representatives who are elected annually by Offshore Transmission Owner (OFTO) parties to represent all OFTO parties. A Committee Secretary and an Ofgem Representative also attend panel meetings.

3.21. National Grid performs the role of STC Committee Secretary and provides the administrative support to the Committee. Funding is provided through the relevant price control.

Grid Code

3.22. National Grid is required by SLC C14 of its Transmission Licence to prepare and at all times have in force, implement and comply with the Grid Code.

3.23. The Grid Code Review Panel (GCRP) consists of a Chair and up to four members appointed by National Grid, three representatives of Large Generators in excess of 3GW capacity, one representative of Large Generators with a total capacity of 3GW or less, two representatives of Distribution Network Operators in England and Wales, one representative of Distribution Network Operators in Scotland, one representative of Suppliers, one representative of Non-Embedded Customers, one representative of Generators with Small and/or Medium Power Stations, one BSC panel representative, one representative of the Externally Interconnected System Operators, one representative of Generators with Novel Units, and two members representing Relevant Transmission Licensees regarding specific aspects of the Grid Code. Each member has a vote with the Chair having a second (casting) vote in the case of a tied vote. An Ofgem Representative may attend meetings.

3.24. The GCRP aims to keep the Grid Code under review and considers suggestions for changes to the Grid Code made on request by the Authority or a user. Only National Grid may recommend changes to the code. National Grid appoints the Grid Code Secretary to provide administrative support for the panel. Funding is provided through the relevant price control.

Distribution Code

3.27. Electricity distribution licensees are required to ensure that the Distribution Code remains a code approved by the Authority that complies with the requirements set out in SLC 21 of the distribution licence.

3.28. The Distribution Code Review Panel (DCRP) maintains the Distribution Code and consists of up to four members from DNOs and one member from an IDNO (one of these must also be member of GCRP), two members from embedded onshore generators operating in Balancing Mechanism, two members from other embedded onshore generators, two members from other connected users (not suppliers or generators), one member from suppliers and one OTSO member. A consumer representative and Authority representative may also attend meetings.

3.29. Only DNOs can collectively review the Distribution Code and propose changes to the DCRP for discussion and consultation with authorised electricity operators. The DCRP produces a report recommending changes to the Authority. Other users may raise a request for change for the panel to consider.

Appendix 4 – The Authority's Powers & Duties

4.1 Ofgem is the Office of Gas and Electricity Markets which supports the Gas and Electricity Markets Authority ("the Authority"), the regulator of the gas and electricity industries in Great Britain. This Appendix summarises the primary powers and duties of the Authority. It is not comprehensive and is not a substitute to reference to the relevant legal instruments (including, but not limited to, those referred to below).

4.2 The Authority's powers and duties are largely provided for in UK statute (such as the Gas Act 1986, the Electricity Act 1989, the Utilities Act 2000, the Competition Act 1998, the Enterprise Act 2002 and the Energy Acts of 2004 and 2008) as well as arising from European Union legislation. References to the Gas Act and the Electricity Act in this Appendix are to Part 1 of each of those Acts.[44]

4.3 Duties and functions relating to gas are set out in the Gas Act and those relating to electricity are set out in the Electricity Act. This Appendix must be read accordingly. [45]

4.4 The Authority's principal objective when carrying out certain of its functions under each of the Gas Act and the Electricity Act is to protect the interests of existing and future consumers, wherever appropriate by promoting effective competition between persons engaged in, or in commercial activities connected with, the shipping, transportation or supply of gas conveyed through pipes, and the generation, transmission, distribution or supply of electricity or the provision or use of electricity inter-connectors.

4.5 The Authority must when carrying out those functions have regard to:

- the need to secure that, so far as it is economical to meet them, all reasonable demands in Great Britain for gas conveyed through pipes are met;
- the need to secure that all reasonable demands for electricity are met;
- the need to secure that licence holders are able to finance the activities which are the subject of obligations on them;[46]
- the need to contribute to the achievement of sustainable development; and

[44] Entitled "Gas Supply" and "Electricity Supply" respectively.
[45] However, in exercising a function under the Electricity Act the Authority may have regard to the interests of consumers in relation to gas conveyed through pipes and vice versa in the case of it exercising a function under the Gas Act.
[46] Under the Gas Act and the Utilities Act, in the case of Gas Act functions, or the Electricity Act, the Utilities Act and certain parts of the Energy Act in the case of Electricity Act functions.

- the interests of individuals who are disabled or chronically sick, of pensionable age, with low incomes, or residing in rural areas.[47]

4.6 Subject to the above, the Authority is required to carry out the functions referred to in the manner which it considers is best calculated to:

- promote efficiency and economy on the part of those licensed[48] under the relevant Act and the efficient use of gas conveyed through pipes and electricity conveyed by distribution systems or transmission systems;
- protect the public from dangers arising from the conveyance of gas through pipes or the use of gas conveyed through pipes and from the generation, transmission, distribution or supply of electricity; and
- secure a diverse and viable long-term energy supply.

4.7 In carrying out these functions the Authority must also have regard to:

- the effect on the environment of activities connected with the conveyance of gas through pipes or with the generation, transmission, distribution or supply of electricity;
- the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed and any other principles that appear to it to represent the best regulatory practice; and
- certain statutory guidance on social and environmental matters issued by the Secretary of State.

4.8 The Authority has powers under the Competition Act to investigate suspected anti-competitive activity and take action for breaches of the prohibitions in the legislation in respect of the gas and electricity sectors in Great Britain and is a designated National Competition Authority. The Authority also has concurrent powers with the Office of Fair Trading in respect of market investigation references to the Competition Commission.

[47] The Authority may have regard to other descriptions of consumers.
[48] Or persons authorised by exemptions to carry on any activity.

Appendix 5 - Glossary

A

ACS

Agency Charging Statement.

April open letter

Open letter consultation on our intention to conduct a second phase Code Governance Review, published 26 April 2012.

B

BSC

Balancing and Settlement Code.

C

CACoP

Code Administration Code of Practice.

CAWG

'Code Administrators' Working Group'. The original CAWG was formed under the CGR. A second CAWG was formed in 2012 as working group to review the CACoP.

CGR

Code Governance Review.

CGR Final Proposals

Conclusions of the Code Governance Review, published 31 March 2010.

Code Governance Review

Ofgem led review of industry code governance, concluding in 2010.

CUSC

Connection & Use of System Code.

D

DCRP

Distribution Code Review Panel.

DCUSA

Distribution Connection & Use of System Agreement.

DG

Distributed Generation.

DNO

Distribution Network Operator.

F

Final modification report

The report submitted to the Authority in order for a decision to be made on a code modification. In the case of self governance, the report containing the final decision on a code modification.

G

GCRP

Grid Code Review Panel.

GDN

Gas Distribution Network.

GT

Gas Transporter.

I

IDNO

Independent Distribution Network Operator.

iGT

Independent Gas Transporter.

iGT UNC

Independent Gas Transporters' Uniform Network Code.

K

KPI

Key Performance Indicator.

M

MRA

Master Registration Agreement.

O

OFTO

Offshore Transmission Owner.

OTSO

Offshore Transmission System Operator.

S

SCR

Significant Code Review.

SPAA

Supply Point Administration Agreement.

SQSS

Security and Quality of Supply Standard.

STC

System Operator – Transmission Owner Code.

U

UNC

Uniform Network Code.

Appendix 6 - Feedback Questionnaire

6.1. Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Please add any further comments.

6.2. Please send your comments to:

Andrew MacFaul
Consultation Co-ordinator
Ofgem
9 Millbank
London
SW1P 3GE
andrew.macfaul@ofgem.gov.uk