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Our Ref: CJA

Your Ref:

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Dear Lesley

Code Governance Review (Phase 3) Initial Proposal - Northern Powergrid's Response

Northern Powergrid is the electricity distribution (DNO) business for the Northeast, Yorkshire and parts of northern Lincolnshire, operating through its two licensed subsidiaries, Northern Powergrid (Northeast) Ltd and Northern Powergrid (Yorkshire) plc.

We thank Ofgem for the opportunity to comment on its initial proposals for this latest phase of the review of code governance published on 23 October 2015 and I have attached our answers to Ofgem's specific questions in Appendix 1 to this letter. In parallel, we note that the findings from the Energy Market Investigation by the Competition and Markets Authority are likely to impact on the Ofgem position. As such, we are ensuring that the views we share with you are reflected in that other consultation process.

Overall, we consider there is opportunity to make changes to code governance that could ultimately improve benefits for customers by delivering quicker and more effective design and implementation of industry changes. We recognise that some of the proposals are likely to lead to increased cost. This is acceptable if the benefits are commensurate to these costs but we need to maintain a focus on efficiency - it is customers who will ultimately carry any increased cost burden in their bills.

We highlight the following headline points from our detailed responses to the questions:

- We think there is value in more self-governance on low-materiality changes, including the potential to give Ofgem more time to focus on policy development and providing strategic direction. However, there may always be certain types of code changes that require an Ofgem decision, including for changes that are likely to affect mass-market supply customers materially and changes where licensee's positions and opinions will inevitably be split by party type and where a change creates the potential for material winners and probable losers;
- Some of the proposed measures to enhance the governance of the larger commercial codes may not be appropriate for the technical codes;
- We agree that code panel members for the larger commercial codes should be impartial and agree that independence is not required. For the technical codes we believe there is no such requirement for impartiality (or independence) as maintaining a

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'representative' approach is necessary to maintain the direct involvement of the parties mainly affected by any changes;

- Where measures to improve the Critical Friend role could add costs to code governance, we believe these should be trialled to test their effectiveness against intended outcomes and that they provide the expected cost benefits, prior to blanket application across all codes; and
- We see benefits in some of the proposed changes for governing charging methodologies, including centralised publishing of information on use of system charges. However, we think there may be merits in going a step further by considering bringing the Distribution Charging Methodology Forum Methodology Issues Group (DCMF MIG) under formal DCUSA governance.

I hope our responses to your questions prove helpful however, if you require anything further please contact us.

Yours sincerely

Chris Allanson

Market Strategy Manager

Appendix 1: Northern Powergrid's responses to Ofgem's specific questions.

Chapter 2

Question 1: Do you agree that Ofgem should have the ability to lead an end-to-end SCR process, including the development of code change and legal text?
Yes, but obviously in consultation with industry representatives so that any proposed changes are sufficiently scoped and appropriately drafted so as to avoid the change stalling in the relevant code governance processes, either during the development or implementation phases.
Question 2: Do you agree it is appropriate to clarify that Ofgem may set timetables for the code change process under an SCR, when the existing, industry-led code development route is used?
Yes. However, consideration needs to be given to whether any existing code rules on change timetables clash with Ofgem's required timetable. Discussion with the relevant code administrator(s) prior to Ofgem setting the timetable on a change should resolve this. Ofgem could ask code administrators whether any existing rules on timetables need to be changed to permit different timetables to support an SCR.
Question 3: Do you have any comments on the licence drafting set out in Appendix 3?
The proposed drafting appears to reflect the intent.
Question 4: Should Ofgem be able to directly raise a modification proposal under the standard process (option 2A)?
Yes. However, as with all modification proposals raised by code parties there is usually merit in scoping a proposal through discussion with other parties or the code administrator prior to formally submitting a modification proposal.
Question 5: Do you have any other proposals for changes to the SCR process?
Not at this time.

Chapter 3

Question 1: Do you agree that requiring a positive identification of why Authority consent is needed (rather than why it is not) could result in additional modifications being developed under self-governance?
<p>We think there is value in more self-governance on low-materiality changes, including the potential to give Ofgem more time to focus on policy development and providing strategic direction. However, there may always be certain types of code changes that require an Ofgem decision, including for:</p> <ul style="list-style-type: none">• Changes that are likely to affect mass-market supply customers materially;• Changes where licensee's positions and opinions will inevitably be split by party

<p>type and where a change creates material winners and probable losers; and</p> <ul style="list-style-type: none"> • Changes that don't have a unanimous or majority vote and where there is no definite view emerging from the panel. <p>We would highlight that existing rules have been designed to guide or prescribe for code panels how to decide whether certain modification proposals require Ofgem consent or not; it would seem to be these rules that need reviewing in order to significantly change the proportion of modification proposals that do not need an Authority decision.</p> <p>Further consideration is needed on what code rule changes are required to accommodate a positive identification of why Authority consent is needed as the code rules and decision criteria will drive the decision process. Additional consideration may also be required on whether new rules need to be approved by the authority for each code and on who, within each code process, makes the decision against those rules, for example is the decision making to be by:</p> <ul style="list-style-type: none"> • The proposer of the modification; • The code administrator; or • The code panel.
<p>Question 2: Do you agree that guidance on the materiality criteria may assist industry in its assessment of whether a modification should be self-governance or require Authority consent?</p>
<p>Yes, please also see our answer to question 1 in Chapter 3. Materiality criteria could be part of the code rules that drive self-governance.</p>
<p>Question 3: Do you agree that any potential guidance is something that panels and code administrators should develop, based on experience to date of using self-governance?</p>
<p>This would seem to be a sensible starting point, but may lead to different outcomes for different codes (i.e. in terms of the proportion of changes that require authority decision or can be decided upon via self-governance). It may be prudent for Ofgem to provide a set of principles to the code panels to guide their considerations and to endorse the resulting decision making rule changes for each code.</p>
<p>Question 4: Do you have any other proposals that may improve the self-governance processes under the codes?</p>
<p>Not at this time.</p>

Chapter 4

<p>Question 1: Do you agree that updating the guidance in CACoP and ensuring best practice across all codes would enhance the role of the Critical Friend?</p>
<p>Yes and we fully recognise the need to find ways to facilitate better engagement with codes by smaller or newer parties. However, we still believe that measures to improve</p>

the Critical Friend role, where those measure could add costs to code governance, should be trialled to test for effectiveness within each code (i.e. in terms of outcomes for code parties, prior to blanket application across all codes whether via the CACoP or otherwise). This should avoid any well intentioned measures that might increase the cost of code governance in general without actually delivering the intended outcomes or benefits.

Question 2: Please provide your suggestions as to how the Critical Friend role could be better advertised and what information each code administrator should include on its website.

We see merits in better advertising of the Critical Friend role, but we note that code administrators already provide opportunities to improve engagement, including via code and industry education sessions. However, we think this question is really important and should be better answered by the smaller and newer parties and also by the relevant code administrators. We would not wish to second guess or inadvertently pre-prescribe what smaller parties might benefit from in support of their key business drivers.

Question 3: Could a self-governance process be introduced for the CACoP?

Before this is considered in detail we believe it would be essential to ensure that the code administrators (and where necessary code panels) had clear drivers on cost controls and an objective to ensure that the development of code administration was done against guiding principles aimed at balancing benefits, costs, efficiency and effectiveness. We would obviously not support continued enhancement of code governance at any cost. Under a CACoP self-governance process there would need to be clear ownership of cost responsibilities and clear responsibility for approving appropriate and necessary enhancements to code governance. In addition, there needs to be an appropriate balance between the code administrator's responsibilities to support the steady-state operation of the codes and any drivers to enhance administration, including through proposing additional services.

Question 4: How often should the CACoP be reviewed?

An annual review seems appropriate, with the administrators of the larger codes taking it in turns to lead the review. This would avoid each of the administrators each triggering a review every year.

Question 5: Do you agree that greater visibility of the CACoP can be achieved by having clear links available on all code websites to a dedicated CACoP page?

Yes, it should increase visibility, but we are unsure whether this in itself would lead to any intended wider benefits or different outcomes.

Question 6: How could the quantitative metrics be improved?

Benchmarking the different codes on a purely quantitative basis can be a useful indicator of general efficacy. However, we are unsure whether performance metrics can actually be used to achieve fully effective comparison of the different code administration processes. The nature of the support that code administrators provide to parties and the code panels for the different codes will drive resource levels and costs irrespective of the volumes and the actual costs of the change process itself. We wonder whether any additional qualitative measures (other than surveys) could help better inform any metric based approach. We also wonder if there could be a matrix based approach that could be used to compare the features of each code's change process and the level of intervention by the code administrators.

Question 7: Should a single body send out one qualitative survey across all codes? If so, who would be best placed to undertake this role?

Please also see our response to question 6. We question whether surveys are sufficient in themselves in identifying any qualitative differences between the code administrators given that all the administrators we engage with provide a broadly effective service.

Question 8: Do you agree that the modification process and template should be standardised across all codes?

A common process and template with a standard format and structure may help smaller and newer parties and also new recruits to larger parties. However, the use of different forms for different codes does not present material issues for us currently.

Question 9: Is it appropriate that all panel chairs be completely independent of industry?

It is important to ensure that panel members, including the chair, have relevant expertise and we agree that independence from the industry is not required; it may even be counter-productive.

We do not see the merits of having panel chairs that are completely independent of industry as we believe that all members of panels that govern change processes should have some level of industry expertise. However, we do see the merit of requiring panel members to act independently of the interests of their own employer organisations (i.e. to be impartial). We would add further that we are unconvinced that the merits of this approach for some larger commercial codes are automatically transposable onto smaller codes and technical codes. If having independent, but expert, chairs is to be a consistent feature of the governance of the larger commercial codes then it will need to be done so on the basis of a balance of benefits and costs. The independent expert chairs will need to be appropriately and reasonable remunerated and mechanism needs to be put in place to ensure continued value for money.

Question 10: Is it appropriate that all panel members are required to be impartial,

i.e. not to represent the interests of their company?
Yes, for the larger commercial codes a requirement for impartiality is entirely reasonable for panel members with voting rights; we believe that panel members should represent the best interests of the code itself. However, for the technical codes and smaller codes we do not believe that impartiality is required and may even be counter-productive. For the technical codes we believe that the parties most directly affected should be directly connected to the decision making process.
Question 11: Should DCUSA and SPAA voting be undertaken by panel, rather than all parties?
We are unfamiliar with the arrangements in SPAA, but as party voting has been part of DCUSA arrangements since its creation and was introduced as a mechanism to engage with parties in the decision process any decision to change this should be carefully considered. If the primary driver is for consistency with other code's arrangements and if Ofgem sees no issues with panel voting in other codes we would be supportive in the interests of consistency. However, if Ofgem also opts for an independent DCUSA panel chair and more direct oversight of charging methodologies the constituency of the DCUSA panel may need to be considered again so that a suite of changes make sense altogether.
Question 12: Should code administrators provide a chair for workgroups?
Yes, if this is required for consistency across the larger commercial codes. However, this may not be proportionate for smaller or technical codes; indeed for smaller codes and technical codes it may unnecessarily increase industry costs. Having the code administrator sitting as the chair of working groups may have benefits beyond independence as industry specialists who take the role of working group chair from time-to-time could instead focus their time on providing informed opinion and expertise. The code administrators should be asked if this would require additional skill sets for its staff and whether different staff would need to be employed at additional cost. In general, we support improved code management arrangements that deliver clear additional benefits with proportionate increases in code costs.
Question 13: Would including a consumer impacts section on each change proposal form help to ensure consumer interests are discussed and published?
Yes, this would highlight to the proposers of changes that they need to take a clear view of the effect on consumers of any particular change.
Question 14: Do you agree with the housekeeping changes we have proposed?
Yes, in respect of the promotion of efficiency of the administration of the codes. We have no comment regarding the proposed housekeeping change for the BSC, CUSC and STC.

Chapter 5

Question 1: Should all 'material' charging modifications proceed through pre-
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modification processes and demonstrate some initial evidence against the relevant charging objectives prior to being formally raised?

Yes, we think pre-modification processes can add value by creating better developed change proposals. However, we think that the pre-modification process should be carried out for Use of System Methodologies as they are quite complex, but not for the much more simple connection charging methodology. The pre-modification process could be carried out by something similar to the existing Distribution Charging Methodology Forum (DCMF) Methodology Issues Group (MIG) that already looks at use of system charges and carries out pre-assessment work. In addition, we believe that a Methodology Issues Group should be brought under formal DCUSA governance i.e. to form a DCUSA MIG in a similar way to the existing DCUSA Standing Issues Group (SIG). In addition, arrangements should be put in place to ensure that all use of system charging changes are submitted to the proposed DCUSA MIG. Arrangements should also prevent bypassing through submission direct to the panel since there would be a risk of creating two routes i.e. via a pre-modification assessment or straight to the Panel without prior assessment.

Question 2: Could the current pre-modifications processes for charging code changes be applied more effectively in line with CACoP Principles 5 and 6?

Aligning assessment to CACoP principles 5 and 6 is logical; however, we are not sure if this would improve the effectiveness of the pre-modification process itself as we are not aware of any specific deficiencies in existing pre-assessment arrangements. We are fully supportive of a formal pre-assessment process for use of system changes.

Question 3: Should panels develop forward workplans for charging modifications in line with agreed priority area(s) to provide a more robust approach to managing modifications?

This could be very beneficial in assisting the development of more manageable arrangements for charging methodologies. However, agreeing the priorities is unlikely to be simple given previous attempts to prioritise distribution use of system charging methodology changes, particularly where individual stakeholder may be wedded to specific proposals that they regard as urgent. In addition, having a programme of work that is too rigid could reduce accessibility and flexibility and act against the interest of parties.

Question 4: Do you agree that charging modifications which are ‘not material’ (in line with self-governance criteria) should be progressed through the self-governance route?

Yes, in principle, however agreeing any materiality criteria may be challenging and we believe that changes that affect charges for mass-market customers are not appropriate for self-governance. Charging methodology changes affecting mass-market customers should be decided upon by the Authority to ensure appropriate scrutiny has taken place on the appropriate balance of interests of different consumer groups and in the interests of general consumer protection.

Question 5: Do you agree that bringing all current charging methodologies forums under DCUSA governance could help to improve stakeholder engagement and increase the consistency of processes for charging modifications?

No, we do not agree with bringing all current charging methodology forums under DCUSA governance and we think that there would be benefits in only bringing one charging group under DCUSA. We see clear benefits in bringing the DCMF Methodology Issues Group (MIG) into formal DCUSA arrangements. Our thinking is set out below:

- MIG - we believe that a Methodology Issues Group with membership made up from experts from multiple different DCUSA parties (and other stakeholder contributors) should be brought under formal DCUSA governance in a similar way to the existing DCUSA Standing Issues Group (SIG). The MIG would formally look at use of system charging issues and the SIG would continue to look at non-charging issues.
- DCMF - This should remain as a more informal stakeholder forum that encourages parties to discuss market developments and raise market issues that may be aided by use of system charging changes. Where a solution may be found in a potential methodology change this could be considered up to a level of detail sufficient to produce a formal documented 'issue' for consideration by the MIG.
- COG - The DNO Commercial Operations Group (COG) is an ENA group that does not discuss use of system charges, the COG reports to the ENA's Electricity regulation Group (ERG). The COG can draw on the support of a DNO only Distribution Charging Methodology subgroup (the COG DCM Sub-group) as required, to address any charging matters at high level. This provides the only forum where Ofgem can discuss use of system charging methodologies and potential new developments with DNOs to help crystallise thinking prior to wider stakeholder discussions. This group is able to informally consider the pros and cons in the initial stages of an idea prior to wider consideration with other stakeholders. We see no reason to bring the COG DCM sub-group under DCUSA governance.

Question 6: Do you agree that having a panel sponsor would help the DCUSA Panel better understand the origins of charging modifications and the DCUSA Panel would be more accountable for, and engaged with, efficiently progressing them?

Yes, it may better help the panel understand the origins of charging modifications. However, we think improved engagement by parties and efficient progression would be better achieved through more formal arrangements and specifically by bringing the Methodology Issues Group (MIG) under formal DCUSA governance.

Question 7: Please set out any other proposals you may have for improving the governance for charging methodologies under open governance arrangements.

Prioritisation of use of system charging methodologies may be better achieved by agreeing a prioritisation hierarchy; such as (highest priority first):

- To reflect changes in legislation (to bring codes into alignment with new law);
- To comply with licence changes, so that code provisions are not out step with obligations on parties;

- Changes to deliver aspects of any Ofgem strategic steer;
- Changes to deliver Ofgem priority programmes such as Half-hourly settlement for mass-market customers
- Urgent changes proposed by parties (where agreed as urgent by the code panel);
- Non-urgent changes proposed by parties; and
- Housekeeping changes.