Code Governance Review (Phase 3):
Final Proposals

Decision

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Overview:

In 2010, Ofgem's Code Governance Review implemented measures to improve the governance arrangements in three of the main codes which underpin the gas and electricity industry arrangements. In 2013, the second phase of our Code Governance Review extended many of the outcomes to the remaining industry codes.

Our code governance reforms were aimed at reducing unnecessary barriers and red tape. They were also aimed at ensuring significant code change could be delivered more effectively.

In May 2015, we issued an open letter noting that we continue to have concerns that the code governance arrangements may not be operating in the best interests of consumers and that it was timely to review the code governance reforms that we had implemented. In October 2015, we published our Initial Proposals for further reform, taking into account the responses to our May letter.

This document sets out our Final Proposals for further reform. It takes account of the responses that we received to our May letter and our Initial Proposals and also feedback from our July industry workshop and our December code administrators' workshop.

Context

The gas and electricity industry in Great Britain is facing significant change in the coming years. This change includes the:

- roll out of gas and electricity smart meters to over 53 million domestic and non-domestic premises by 2020

- low carbon transition which will lead to increasing levels of intermittent electricity generation and new low carbon technologies, with potentially a greater role for flexibility in the system including demand side response (DSR)

- EU Third Energy Package, which has introduced and is introducing new legislation, known as European Network Codes (ENCs), governing the design, operation and planning of the European energy sector.

These issues are already driving change to the detailed rules that underpin the operation of the industry and further changes to the rules are needed. These rules are set out in a number of industry codes, which include governance arrangements that define how the codes may be changed.

We have previously reviewed the industry code governance arrangements and introduced reforms to improve them. However, in the context of the anticipated scale of change required in the coming years, we continue to have concerns that the arrangements may not be operating in the best interests of consumers. We consider it is timely to review the reforms we have implemented and potentially introduce further reform to the arrangements.

Associated documents

Code Governance Review (Phase 3) Final Proposals – consultation on licence modifications
https://www.ofgem.gov.uk/publications-and-updates/code-governance-review-phase-3-final-proposals-consultation-licence-modifications

Code Governance Review (Phase 3) Final Proposals – consultation on surveys and metrics
https://www.ofgem.gov.uk/publications-and-updates/code-governance-review-phase-3-final-proposals-consultation-code-administration-reporting-metrics-and-performance-surveys

Code Governance Review (Phase 3): Initial Proposals (2015)
https://www.ofgem.gov.uk/publications-and-updates/code-governance-review-phase-3-initial-proposals

Open Letter on Further Review of Code Governance dated 15 May 2015
https://www.ofgem.gov.uk/publications-and-updates/open-letter-further-review-industry-code-governance

Licence modifications to implement Code Governance Review (Phase 2) Final Proposals
https://www.ofgem.gov.uk/publications-and-updates/modification-gas-and-electricity-licences-implement-code-governance-review-phase-2-final-proposals

Code Governance Review (Phase 2) – Final Proposals (2013)
https://www.ofgem.gov.uk/publications-and-updates/code-governance-review-phase-2-final-proposals

Licence modifications implementing the Code Governance Review Final Proposals (2010)
https://www.ofgem.gov.uk/publications-and-updates/licence-modifications-implementing-code-governance-review-final-proposals

Code Governance Review – Final Proposals (2010)
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=297&refer=Licensing/IndCodes/CGR

Code Administration Code of Practice
https://www.ofgem.gov.uk/publications-and-updates/code-administration-code-practice-version-4

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Executive Summary

In this document we set out our Final Proposals for the third phase of our Code Governance Review (CGR3). These proposals build on reforms we have already introduced to improve code governance based on the arrangements and institutions currently in place.

In June 2014 the Competition and Markets Authority (CMA) launched its Energy Market Investigation following a market investigation reference from Ofgem. In March 2016 the CMA published its provisional decision on remedies. That document sets out that the aim of the CMA's proposed remedies in relation to code governance is to recalibrate the role of Ofgem and code administrators while maintaining industry involvement, for the purpose of driving forward code changes that affect competition and consumers' interests. The CMA has set out its view that this should in turn facilitate longer term development of the code governance framework under the supervision of Ofgem. The CMA's proposed remedies to achieve this aim include increasing Ofgem's ability to engage more proactively with the code regime, focusing on strategic level input, and a recommendation to DECC to make the provision of code administration and delivery services activities that are licensed by Ofgem.

We consider that the changes we are proposing here will make important incremental improvements while this new regime is developed and implemented: indeed we believe the changes we outline in this document will help code administrators and the wider industry prepare for the more fundamental changes proposed by the CMA. We also consider that these proposals are in line with our commitment to Better Regulation principles and to reducing regulatory burdens on industry while maintaining effective consumer protection.

Significant Code Review (SCR) process – Chapter 2

Our Final Proposals are in line with our Initial Proposals. Our Final Proposals provide three options that could be followed under an SCR process. We will retain the ability to follow the current SCR process, under which we direct a licensee(s) to raise modification proposals at the end of the SCR. In addition, we are introducing the ability for us to raise a modification proposal(s) at the end of an SCR. Under these two options the modifications would follow the standard industry process. The third option would enable Ofgem to lead an end-to-end process to develop code modification(s). We consider that these changes will provide additional flexibility in how the Authority may choose to lead an SCR and enhance the existing SCR process.

Self-governance process - Chapter 3

Our Final Proposals on the self-governance process require industry to assess whether a modification requires Authority consent, i.e. why it **is** material, rather than why it is **not** material, which is the current situation. We also expect code administrators to work together to produce guidance that can be applied across

codes to help proposers assess whether their change should follow a self-governance path.

Code administration - Chapter 4

In the area of code administration we have identified a number of changes that we consider would make code administration and related arrangements more effective, in particular in supporting smaller parties and in driving consistency across the code change processes. These changes include the development of forward work plans by the code administrators and increased cross-code coordination, through the development of a modification proposals register and the use of an agreed process for modification proposals that may affect more than one code. We have also put forward changes to the way that the code administrators report on metrics, and have today published a separate consultation on our detailed proposals for these metrics and surveys. In December 2015, we held a workshop with the code administrators to discuss how they could take forward a number of our proposals, and we welcome the work that has been done to date in these areas. We will work with the code administrators and the industry to implement the changes we have identified.

Charging methodologies – Chapter 5

We have set out our Final Proposals for a number of ways in which we expect to see improvements to the governance of charging methodologies, which should lead to increased participation in governance processes over time. Several of our proposals for the charging methodologies relate to self-governance and code administration. In particular, greater use of pre-modification processes (charging forums) by more participants should assist in the development of charging issues into well-defined formal charging modifications. In addition, we anticipate that increased use of the self-governance route for charging modifications (where appropriate) would create a more effective balance to the decision-making framework that applies industry's and our resources more efficiently. Finally, our final proposals in relation to the DCUSA charging methodology arrangements, including bringing the charging forum into DCUSA governance and panel members sponsoring charging forums, will benefit the DCUSA change process by improving accessibility of information for all interested parties, by supporting effective panel decisions and recommendations in relation to charging issues and assist the panel in developing effective forward work plans.

Implementation

Alongside this document, we are consulting on licence changes to give effect to some of our Final Proposals. We are also consulting on issues related to implementing new code administration reporting metrics and performance surveys. In addition, we expect code administrators, panels and the wider industry to work cooperatively to deliver other changes we have identified.

1. Introduction

Chapter Summary

This chapter provides background on Ofgem's Code Governance Review (CGR) and sets out the purpose and content of this Final Proposals document. It also sets out our objectives in undertaking this third phase to the CGR and the scope of our work.

Background

1.1.   The industry codes are, broadly speaking, the regulated contractual arrangements that underpin the operation of the electricity and gas industry arrangements. They each include governance arrangements which define how the codes may change. We have previously reviewed the code governance arrangements and implemented reforms. This document concludes our review of those reforms, and details our Final Proposals for further reforms under this latest phase of our Code Governance Review (CGR3).

Previous Code Governance Reviews

1.2.   We launched our Code Governance Review (CGR) in November 2007, in light of the evolving nature of the industry and strategic challenges likely to impact the code arrangements. The first phase of CGR concluded in 2010 and focused on three of the main industry codes (the Balancing and Settlement Code (BSC), the Connection and Use of System Code (CUSC) and the Uniform Network Code (UNC)).

1.3.   In our CGR Final Proposals, we identified a number of deficiencies with the arrangements and introduced a range of reforms in two main areas. First, seeking to reduce unnecessary barriers and red tape in the existing industry code governance arrangements. And second, aimed at ensuring that significant code change could be delivered more effectively. We recognised that the code governance arrangements worked well in delivering incremental change to industry codes, but that they had not been effective in supporting larger scale and more complex change. In 2013, we concluded the second phase of CGR (CGR2), extending our key reforms to cover all of the industry codes.

1.4.   The governance reforms we introduced under CGR and CGR2 covered four main areas: introduction of the **Significant Code Review (SCR) process,** enabling Ofgem to lead a holistic review that may result in complex and/or cross code change; enhancements to the **role of the code administrators,** including the introduction of the Code Administration Code of Practice (CACoP) and the Critical Friend role; establishment of **self-governance arrangements** for modifications; and the inclusion of certain **charging methodologies** within industry codes.

Code Governance Review (Phase 3)

Objectives and Scope

1.5.   In this third phase of our review of code governance, we are reviewing the effectiveness of the key measures we introduced under our previous CGRs. Our objective has been to identify further reforms, seeking to ensure that the governance arrangements of all industry codes deliver both non-material self-governance changes and more complex changes in an efficient and timely way. Further, we are seeking to ensure the governance arrangements promote transparency and accessibility for all industry participants. These further reforms are intended to facilitate best practice becoming business as usual, whilst avoiding unnecessary regulatory burdens.

1.6.   The scope of our review covers the four broad areas considered previously: the SCR process; self-governance; code administration; and the governance arrangements for charging methodologies.

1.7.   The scope of the review is based on continued concerns that the code governance arrangements may not be operating in the best interests of consumers, particularly given that the electricity and gas industry in Great Britain is facing significant change in the coming years. These changes include the roll-out of gas and electricity smart meters and the low carbon transition, which will lead to increasing levels of intermittent electricity generation and new low carbon technologies. In the context of the anticipated scale of change required in the coming years, we continue to have concerns that the arrangements may not be operating in the best interests of consumers.

Process to date

1.8.   In May 2015, we issued an open letter to which we received 36 responses. In July 2015, we held a workshop to inform our thinking and provide a further opportunity to seek views on the issues discussed in our open letter. The views provided in responses to our consultation and at our industry workshop supported our view that it is timely to review the governance reforms we have already made and to explore further code governance reforms.

1.9.   In October 2015, we published our Initial Proposals setting out our proposals for further reforms in respect of code governance. These proposals took into account the views provided in response to our May open letter and at the July workshop.

1.10. We received 32 responses to our Initial Proposals consultation, all of which are available in full on our website. In December 2015, we held a workshop[1] for code administrators to provide a further opportunity to understand their views and to discuss ways in which they could take forward some of our proposals.

Related work under the Market Investigation Reference

1.11. Industry code governance is one of the areas also being considered by the Competition and Markets Authority (CMA) as part of its ongoing Market Investigation Reference (MIR). In its provisional findings, the MIR identified code governance as having an Adverse Effect on Competition (AEC) and proposed possible remedies.[2]

1.12. We set out in our response to the CMA's provisional findings that we strongly agree with its conclusion that the current code governance regime, including the limited incentives that incumbent organisations have to promote and deliver change that could benefit consumers, gives rise to an AEC. We also set out that we believe there are changes to the industry governance regime that can address these issues, building on the options set out in the CMA's notice of possible remedies. We noted that a reformed set of institutions would be central to ensuring that the regulatory regime is able to respond to the innovation and change the industry is going to see in the coming years.

1.13. On 17 March 2016 the CMA published a consultation on its provisional draft decision on the MIR. In respect of code governance, the consultation sets out that the aim of the CMA's proposed remedies is to recalibrate the role of Ofgem and code administrators while maintaining industry involvement, for the purpose of driving forward code changes that affect competition and consumers' interests. The CMA has set out its view that this should in turn facilitate longer term development of the code governance framework under the supervision of Ofgem. The CMA's proposed remedies to achieve this aim include increasing Ofgem's ability to engage more proactively with the code regime, focusing on strategic level input, and a recommendation to DECC to make the provision of code administration and delivery services activities that are licensed by Ofgem. We are fully committed to developing remedies that can improve market outcomes for energy consumers, including on code governance reforms beyond the scope of the reforms from our CGR3.

1.14. The reforms proposed by the CMA and those from our CGR3 build on reforms we have already introduced, and seek to improve code governance to enable the consideration of the long-term development of codes within the broader regulatory framework. A number of respondents to our Initial Proposals set out their views on more fundamental reform, which goes beyond the scope of our CGR3 process. We

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[1] https://www.ofgem.gov.uk/publications-and-updates/code-administrators-workshop-02-december-2015
[2] https://www.gov.uk/cma-cases/energy-market-investigation

recognise that more fundamental reform is needed and therefore welcome the CMA's provisional decisions in respect of the recalibration of the roles and incentives of Ofgem and code administrators; however, we still consider that there would be benefits to making the changes proposed in this document in the meantime, and consider these to be consistent and are moving in the same direction as the CMA's proposed remedies.

Content of this document

1.15.   In the following four chapters of this document, we set out our proposals in each of the four broad areas covered by the scope of our review:

- **Chapter 2**: contains our proposals in respect of the **SCR process**;

- **Chapter 3:** contains our proposals in respect of the **self-governance process**;

- **Chapter 4:** contains our proposals relating to **code administration**; and

- **Chapter 5:** sets out our proposals in respect of the **governance arrangements for charging methodologies.**

1.16.   Within each chapter, we summarise our Initial Proposals and the responses to them. We then set out our Final Proposals for each of the areas. With respect to the SCR process, we propose potential enhancements aimed at making the process more effective; for the self-governance process, we propose ways to ensure it is used effectively across all the codes; for code administration, we set out a range of measures aimed at increasing transparency, accessibility and consistency; and for the code governance arrangements for charging methodologies, we set out proposals that build on its effective introduction into the governance arrangements.

1.17.   We also set out the ways in which we expect our Final Proposals to be taken forward. We consider that there are three routes for implementation:

- **Ofgem to take forward:** this is the route for changes that we consider require licence changes, and other changes we will lead on. We have therefore today also published a consultation document that sets out the required licence changes to implement some of our Final Proposals, as well as a consultation on options for implementing our final proposals on code administration reporting metrics and performance surveys (discussed in Chapter 4 of this document).

- **Industry participants to take forward:** this is the route where we expect the changes to be made by certain industry players. This is particularly the case where it is considered that improvements could be made through behavioural changes by certain players, for example through website changes. We also note the areas where changes are already being made.

- **Cross-industry working groups:** for some of our proposals, we do not consider that regulatory (e.g. licence) changes are the appropriate method for implementation. However, we recognise that there may be the need for a number of parties (including Ofgem) to be involved in taking forward such changes (which may include developing appropriate code change, if necessary). As mentioned above, we have already held one workshop with the code administrators and we set out the areas that are being taken forward in this way.

Next steps

1.18. Our accompanying consultation document sets out our proposed licence changes necessary to implement some of our Final Proposals contained in this document. Subject to the responses received to that document, as a next step we expect to publish the Statutory Notices on the licence changes, followed by a direction to make the changes if appropriate. We currently expect to complete the licence change process in summer 2016.

1.19. The separate accompanying consultation document we have published today sets out our proposed way forward in respect of the metrics to be reported by the code administrators and the survey to be undertaken in respect of the performance of the code administrators.

1.20. A number of our Final Proposals set out in this document will require code administrators, code panels and industry more widely taking forward developments in the code governance process. We welcome the progress that has been made to date in these areas and would welcome the opportunity to continue to engage with the relevant industry parties, as appropriate.

2. Significant Code Reviews

Chapter Summary

This chapter discusses the Significant Code Review (SCR) process under which Ofgem can lead a review to deliver complex code change. It summarises our Initial Proposals and the responses that we have received to them. It then sets out our Final Proposals for reform to the SCR process, to enable Ofgem to lead a collaborative, end-to-end SCR process, including the development of code change.

2.1.   The SCR process was introduced under CGR to provide a mechanism that was able to deliver effective and efficient complex change to the industry codes, through Ofgem leading holistic reviews. We also published high-level guidance on the process that we would follow when conducting an SCR, for example giving notice to industry of our intention to undertake an SCR, and consulting through written documents and workshops.

2.2.   To date we have conducted three SCRs, each of which has resulted in code modifications: the Electricity Balancing SCR; the Electricity Transmission Charging SCR; and the Gas Security of Supply SCR. In addition, on 17 November 2015 we launched the Switching SCR[3] and in December 2015 we announced that we intended to launch an SCR on mandatory half hourly electricity settlement in early 2016.[4]

Initial Proposals

2.3.   In our Initial Proposals, we recognised that the SCR process in its current form could still result in inefficiencies and duplication, if the industry decides at the end of the Ofgem-led industry consultation process within the SCR to undertake its own process which may revisit some of the work already undertaken.

2.4.   In the SCRs that we have undertaken, we considered it may have been helpful to have had the ability for Ofgem to run an end-to-end process and/or to have an explicit ability to direct timetables, in order to drive forward the implementation of our SCR conclusions. Our experience from the SCRs that we have conducted to date also indicated that providing a mechanism for Ofgem to lead the drafting of code modification text alongside consultation with industry may provide a way of working through issues, for example where there is significant industry disagreement.

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[3] On 21 January 2016, DECC published a command paper containing draft legislation which would provide Ofgem with additional powers to help it manage and deliver reform of energy supplier switching. If such powers were provided, we would expect to use those rather than an SCR.
[4] https://www.ofgem.gov.uk/sites/default/files/docs/final_open_letter_on_hhs.pdf

2.5.   We noted in our Initial Proposals that it is important that detailed implementation issues arising from the drafting of legal text can be properly considered in forming policy conclusions under an SCR. We recognised that, in some cases, implementation issues may only become apparent during legal text drafting and that such issues could potentially influence the outcome of policy conclusions. This supported our view that it would be appropriate to enable Ofgem to have the ability to draft code modifications as part of an SCR.

2.6.   We therefore considered that the SCR process should provide for a collaborative, Ofgem-led, end-to-end approach. We considered that effectively incorporating what is currently the industry-led phase (of developing detailed code change) within the Ofgem-led process would facilitate a more efficient end-to-end process and avoid potential duplication under two separate processes. To ensure this process is effective, we considered that this would require Ofgem to be able to draft code modification legal text as part of our SCR. We recognised the need for effective engagement and collaborative working with industry, and considered this would be essential under an Ofgem led end-to-end process, in order that we could take into account stakeholder views and draw on industry expertise to develop appropriate code modifications.

2.7.   We proposed that this Ofgem-led process would be an additional tool that we may use for delivering change under an SCR – we would also retain the ability to issue a Direction to a licensee to raise a code change/develop legal text. We also considered that there are benefits in clarifying the ability for Ofgem to direct timetables for the development of code modifications, in cases where the SCR process relies on a direction to a licensee(s) to raise changes under the normal industry change processes.

2.8.   In our original CGR proposals, we were concerned that the effectiveness of the SCR process and the ability for it to arrive at coherent and well-thought through policy positions could be undermined by industry participants using the modification process to delay or otherwise frustrate the process of developing code modification text.[5] We set out in our Initial Proposals that a 'backstop measure' for Ofgem to draft code modification text would provide an effective means of overcoming such risks.

2.9.   In our Initial Proposals, we set out that, were we to implement the option of Ofgem developing code modifications, we would expect to develop code modification legal text with close involvement from code administrators, code owners, affected licensees and code parties. This would be done through working groups established by Ofgem as part of the Ofgem-led SCR process and could be designed effectively to mirror the working arrangements used by code panels as part of the established code modification process.

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[5] https://www.ofgem.gov.uk/sites/default/files/docs/2008/12/majpol_selfgov_condoc_191208_0.pdf

Responses to our Initial Proposals

2.10.   The majority of respondents to our Initial Proposals responded to the questions that we raised in respect of our proposals for SCRs. Of those that responded, a small majority supported our proposal for Ofgem to have the ability to lead an end-to-end SCR process, including the development of code change and legal text. One respondent who supported the proposal considered that it would help in more complex SCRs that affect multiple codes, whilst another respondent considered that it would ensure cross-code issues are co-ordinated and led. Another respondent welcomed the more integrated approach in co-ordinating industry changes across multiple codes. Another respondent commented that there was a need for Ofgem leadership in this area. In supporting this proposal, a number of respondents highlighted the requirement for a full consultation process to be undertaken.

2.11.   Respondents that did not support the proposal gave varying reasons: the changes would not have a material impact on the delivery timescales; a better resolution would be to determine the steps that should take place under the SCR process versus the ones that generally happen under the code change process and remove any duplication e.g. leave a full Impact Assessment to the code change section; it was not clear what criteria Ofgem would use to decide which option to use, which would create uncertainty; the industry-led process has more checks and balances; the proposal removes the process by which industry can effectively input into an SCR; it was not clear that a lack of overall lead from Ofgem has led to the length of SCRs; and the current process gives Ofgem sufficient powers to lead larger scale industry change. One respondent saw merit in the proposals, but did not consider Ofgem to be the right body to lead the end-to-end process.

2.12.   Of those that responded, a larger majority supported, in principle, our proposal 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 and also our proposal that Ofgem should be able to raise a modification under the standard process.

2.13.   In providing support for our proposals, a number of respondents qualified their support in various areas. In respect of Ofgem setting timetables, respondents noted that the timetable would need to be consulted on with industry before being set and that any such timetable would need to allow for flexibility. Those respondents that did not support Ofgem setting a timetable were mainly concerned with how that timetable would be set. One respondent suggested that the approaches already in place under the CUSC and DCUSA could be extended to other codes, which could avoid the need for Ofgem to take additional powers.

2.14.   Respondents also raised a more general concern with Ofgem's role in respect of it being able to raise a modification proposal under the standard SCR process and also if it were to lead an end-to-end process. One respondent raised the question of Ofgem's impartiality when approving a modification proposal that it had raised.

Another respondent highlighted that there would still need to be a role for panels in respect of voting. Several respondents questioned what the appeals process would be in this situation.

2.15.   Respondents also noted that there was a requirement for more robust project and programme management, and that it would be helpful to have a steer from Ofgem earlier in the process.

2.16.   Several respondents made specific comments on the illustrative licence drafting included in Appendix 3 to our Initial Proposals. Some respondents also requested sight of the licence drafting ahead of our Statutory Consultation on the licence modifications.

Our Final Proposals

2.17. We welcome the views of respondents regarding our proposals to reform the SCR process. We agree with those respondents that considered that Ofgem leading an end-to-end process would be particularly beneficial in situations involving complex SCRs that affect multiple codes. The ability for Ofgem to lead the process may reduce the possibility which may occur in complex situations under the current process. For example, where a Direction (in the form of either a high-level binding principle or detailed binding conclusions) is issued by Ofgem but the detail is then developed under the jurisdiction of the various affected code panels. This may therefore result in variations in the final solution (i.e. modification proposal), both in content and timing, that is presented to Ofgem for approval.

2.18. Some respondents that did not support our proposals expressed the view that the current process already gives Ofgem sufficient powers in this area. Whilst we recognise the powers that Ofgem already has, we consider that our proposals are about ensuring that there is a process in place that is as effective as possible in delivering complex modifications to the industry codes. In this respect, we would also note that the CMA's proposed remedy will see Ofgem taking a more strategic role in code development through the production of strategic work plans. We consider that our proposals in respect of the SCR process are consistent with the CMA's proposed remedies.

2.19. We note that one respondent saw merit in the proposals, but did not consider Ofgem to be the right body to lead the end-to-end process; however, we do not consider that there is currently an alternative body with the appropriate expertise and incentives to lead such a process. We therefore consider that Ofgem is currently the most appropriate body to lead this work. However, we note that the CMA has proposed a role for Ofgem to lead on code changes with oversight of licensed code administrators. The CMA considers that there is scope to expand the role of code administrators to take on project management responsibilities that do not sit naturally with Ofgem as the economic regulator. In this regard we would also note the CMA's expectation that over time our involvement would increasingly take the form of

influencing the activities of licensed code bodies and industry through the design of appropriate incentives and obligations in the regulatory framework.

2.20.   Some respondents considered that our proposals would mean that the SCR process would still result in inefficiencies and duplication. One respondent considered that it was not clear that a lack of overall Ofgem lead had resulted in the length of the SCRs that had been undertaken. Given the likelihood of the complexity of the issues that are to be addressed through an SCR, we recognise these risks and the timescales that may be required. However, we consider that, by Ofgem leading an end-to-end process, the steps of which would be clearly set out at the outset, these risks should be significantly reduced. Further, under the Ofgem-led process, consideration would be given throughout to both the relevant objectives of the code(s) and also Ofgem's statutory duties and objectives; thereby reducing the possibility that a final modification proposal was presented that had not been assessed against all the relevant requirements. We also consider that, by reducing the possibility of inefficiencies and duplication, particularly in respect of analysis and consultation, overall timescales could potentially be reduced. In addition, this process would enable assessment across all codes and parties as to what resources are necessary, what issues need to be resolved, and whether there are any cross-code issues at all stages of the process.

2.21.   We recognise the concerns raised by respondents regarding the need for effective engagement and collaboration with industry throughout this process and the need to draw upon industry experience in order to develop appropriate code modifications. A number of respondents, whilst supporting the proposal for Ofgem to be able to set a timetable, highlighted the need for such a timetable to be consulted on and for the timetable to allow for flexibility and revision. In this area, we recognise the benefits of an approach where modifications are subject to a standard timetable unless agreed otherwise by the relevant panel and the Authority, and therefore all parties at the outset of the modification process have a clear understanding of the timeframe involved, and why it may be subject to amendment.

2.22.   There would be effective engagement and collaboration with industry, including code panels, throughout the process, whether that be an Ofgem-led end-to-end process or an SCR that follows the existing process. We fully recognise the importance of full industry engagement and the valuable input and insights that all parties can provide in reaching the most appropriate solution to a complex issue. We have therefore updated our SCR guidance to illustrate how such engagement and collaboration will take effect under the new processes as set out in these Final Proposals. Importantly, we set out how the new processes will provide the opportunity for all parties to undertake analysis, and consider the implementation solutions in detail. This will be done via industry meetings and industry-wide consultations. In developing our approach to conducting an SCR, we would, as with any policy development we undertake, have careful regard to our duties in respect of better regulation including transparency and accountability. In addition, the Authority has specific duties in respect of consumers, and therefore this process would ensure the effects on them are considered throughout.

2.23. A number of respondents also raised concerns regarding Ofgem's impartiality when approving a modification proposal that it had raised. One noted that it was important that the relevant code panel retained its role in respect of voting on a modification proposal. Respondents also questioned what the appeals process would be in this situation.

2.24. As set out above, the Authority has specific duties with which it must comply. In particular, when making its final decision on a modification proposal, it must consider whether the modification better facilitates the relevant objectives of the code and whether its decision complies with the Authority's statutory duties. This requirement applies irrespective of whether Ofgem has raised the modification proposal. As was commented on by a respondent, it would be a less than ideal situation if the Authority decided that a modification proposal failed to facilitate the relevant objectives/duties at this late stage. Therefore, it is vital that all possible solutions are considered, fully consulted on, and concerns raised are fully addressed as part of the process. Nevertheless, in accordance with its duties, the Authority would be highly receptive to any representations made by the panel, and would take these into account in deciding whether to approve any modification proposal.

2.25. We recognise the comments that have been made regarding the appeals process. However, as set out above, we would expect any modification proposal that came to the Authority for a decision having followed the SCR process to have been fully consulted on and to provide an appropriate solution that is compliant with both the relevant objectives of the code and the Authority's statutory duties. In this situation, there are still routes for challenging the Authority's decision. Where the Authority goes against the panel's decision, an appeal can be brought to the CMA. In other circumstances, a decision of the Authority is subject to judicial review.

2.26. We note the CMA considers that its proposed remedy for Ofgem to have a back stop executive call-in power, together with its proposed remedy for Ofgem to take powers to initiate and prioritise strategically important modification proposals, would form an effective substitute to Ofgem's current SCR powers. The CMA has noted that additional legislative measures would need to be implemented in order to permit Ofgem to make code changes directly through the proposed call in power, and has recommended DECC enact legislation to grant the power for Ofgem to modify codes in certain exceptional circumstances. We recognise these proposed remedies may in time result in us revisiting the need for the SCR process, but consider it is appropriate to retain it at this time, and to proceed with our proposed enhancements under CGR3, which we consider are consistent with the direction of travel of the CMA's proposed remedies.

2.27. Several respondents provided specific comments on the illustrative licence drafting included as Appendix 3 to our Initial Proposals. Other respondents, particularly those directly affected, requested that the licence drafting relevant to them was shared with them prior to publication. We welcome the comments on the illustrative licence drafting and these, together with how we have responded to them, are set out in our separate consultation that we have also published today. In that

document, we have included legal drafting for all the licence changes that would be required to implement our Final Proposals set out in this document.

2.28. Our **Final Proposals** are for the implementation of reforms to the SCR process as set out in our Initial Proposals (in addition to retaining the existing options).

2.29. The current SCR process together with our Final Proposals is illustrated in Figure 2.1. We have simplified the diagram that we included in our Initial Proposals document to show that, in essence, there are three main options, which are:

1. **Ofgem directs licensee(s) to raise modification proposal(s)**. At the end of the SCR process we would issue a direction to the relevant licensee(s). Our direction may set out high level principles (with the detail to be developed by industry) or more specific, detailed conclusions to be given effect through code change(s). The modification(s) would follow the standard industry code modification processes.[6]

2. **Ofgem raises modification proposal(s)**. At the end of the SCR process we would raise a modification(s) under the relevant code(s), and the modification(s) would follow the standard industry code modification processes.

3. **Ofgem leads an end-to-end process to develop code modification(s).** The standard industry process would not apply; Ofgem would lead consultation and engagement needed to develop the appropriate code change(s). We would expect close involvement of the industry; for example, we may establish and lead workgroups similar to the approach under the standard code modification processes (but led by us).

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[6] Including, for example, establishing workgroups to develop and assess proposed change, and providing for alternatives to be raised if appropriate.

Figure 2.1 Diagram illustrating the proposed SCR process
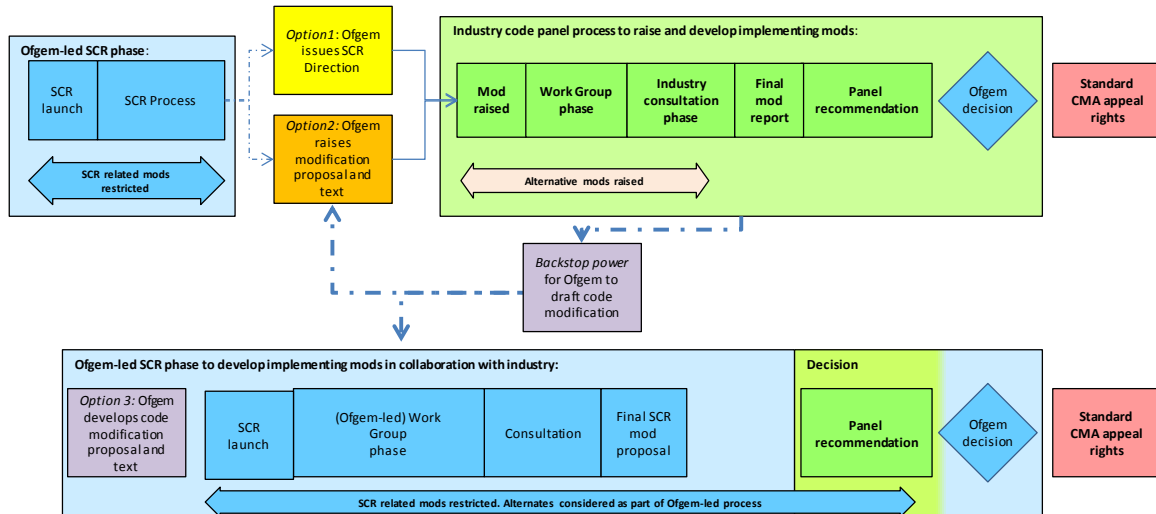
2.30. The consultation on the legal text to implement these Final Proposals is set out in an accompanying document (Code Governance Review (Phase 3) Final Proposals – consultation on licence modifications).[7] The draft legal text provides for the maximum of flexibility in respect of the SCR process and enables the process to move between the options, where applicable. An updated draft of our guidance document is included in Appendix 1.

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[7] https://www.ofgem.gov.uk/publications-and-updates/code-governance-review-phase-3-final-proposals-consultation-licence-modifications

3. Self-Governance

Chapter Summary

This chapter discusses the self-governance code change process under which industry can make decisions on changes that do not have a material impact on consumers and competition. We set out the responses to our Initial Proposals and also out the work that has been undertaken to date by the code administrators in this area. There is broad support for the use of self-governance and we set out our Final Proposals on options which may encourage greater use of this approach.

3.1.   We introduced a self-governance route for code modifications through CGR and CGR2 to ensure that our (and industry) resources are focused on those issues that have a significant and material impact on consumers and in respect of our wider statutory duties.

3.2.   The self-governance process has generally worked well, and industry parties have welcomed its introduction. There have been benefits in increasing the efficiency of the code processes and ensuring that greater resources are appropriately focused on more material changes. However, it has also been recognised that there may be greater scope for further use of the self-governance process.

Positive identification against self-governance criteria

Initial Proposals

3.3.   Currently, when raising a modification, the industry and panels must assess whether a modification meets the self-governance criteria – i.e. why it is not material. In our Initial Proposals, we set out an alternative approach, which would require the industry to assess whether a modification requires an Authority decision – i.e. why it is material. We considered that this would be a marginal change to the existing process, and would continue to require an assessment of the materiality of a proposal. We noted that it may help with behavioural change, by requiring a positive identification of those matters which are material and therefore clearly demonstrating what is driving the need for the Authority (rather than the industry) to make a decision. We also considered that it may help avoid any potential undue caution that parties may have towards self-governance that can arise based on the current approach (of having to identify why a proposal is *not* material).

Responses to our Initial Proposals

3.4.   Nearly all respondents to our Initial Proposals commented on this issue. Of those that did, the large majority agreed 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. Comments in support of this change included that it would ensure all modification proposals are considered for self-governance and that self-governance would be the status quo. One respondent, although supportive, considered that the change may lead to an increase in volumes of trivial or vexatious proposals. Another respondent commented that targets should not be set for the volume of modifications to follow the self-governance process.

3.5.   Those respondents who did not support the change considered that it would not make a difference, with one noting that only changes to the criteria would make a difference. Another respondent considered that it would not provide an incentive to increase self-governance, whilst another noted that, if the proposal is believed to better facilitate the relevant objective regarding enhancing competition, then it is not likely to be self-governance. One respondent noted that self-governance should be only for housekeeping and administrative changes and that panels should not be making decisions which have material and/or commercial impacts.

3.6.   Of those respondents who supported the change, several made specific comments regarding the process. One highlighted that it was important for parties to have confidence that the self-governance process leads to robust decisions. Others commented that it may not be clear when the proposal is first raised if it should progress via self-governance and that the panel decision should be capable of review. Another respondent considered that Ofgem should highlight if a modification proposal is not material.

3.7.   Some respondents suggested that robust rules were needed on which party identifies why Authority consent is required, whilst another respondent considered that each panel member should have the power to veto self-governance for a modification. It was also raised that under the CUSC, the CUSC panel has to seek confirmation from the Authority that the self-governance criteria have been met, which negates the benefit of self-governance.

3.8.   Some respondents also made comments on the criteria, with one party proposing changes to them. Another respondent noted that panels must consider the impact on individual parties. It was also commented that modifications which have a material impact on domestic customers or those where code parties are highly likely to be split by party type should go to Ofgem for decision.

 Final Proposals

3.9.   We welcome the comments from respondents who support our Initial Proposal to require a positive identification of why Authority consent is needed (rather than why it is not), which could then result in additional modifications being developed under self-governance. We note that respondents who did not support our proposal did so on the basis that they considered it would not make a difference, rather than not being supportive of the self-governance process itself.

3.10.   We recognise that it may not be clear when a modification proposal is first raised as to whether it meets the criteria and therefore should follow the self-governance route. We therefore consider that it is appropriate for this question to be revisited as the modification progresses.[8]

3.11.   In respect of the comments made regarding the process for self-governance, we note the following. We would expect the proposer of the modification to initially set out whether the self-governance route should be followed; based on our Final Proposals, we would expect this to be amended, such that the requirement is for whether an Authority's decision is required. The relevant code panel then determines whether the modification meets (or in the future does not meet) the self-governance criteria. On receipt of a self-governance statement[9] (i.e. confirmation from a code panel that a modification proposal should follow the self-governance process), we can direct that the Authority's decision is required, i.e. that the modification should not follow the self-governance route. The Authority can also separately determine that the Authority's decision is not required, i.e. that a modification proposal should follow the self-governance route. We also note that modifications that follow the self-governance route can be appealed to us, with the criteria for appeal including that the appealing party is likely to be unfairly prejudiced by the implementation or non-implementation of that modification proposal.[10]

3.12.   We note that the CMA, whilst welcoming the use of the self-governance arrangements and noting that there is scope to expand its use, highlighted that some modification decisions that appeared to it to be fundamental to ensuring effective competition and meeting the needs of customers had not involved the Authority. For the avoidance of doubt, our proposals mean that modification proposals that **are** material should not follow the self-governance route, but should come to the Authority for a decision.

3.13.   We note the comments that were made by some parties in respect of the criteria that modification proposals are required to meet in order to follow the self-governance process. We consider that the current criteria are appropriate in respect of assessing whether a modification should be self-governance. As set out in our Initial Proposals, we think it would be helpful for guidance in respect of the materiality criteria to be developed; this is discussed further in the next section.

3.14.   We consider that our proposal may help with behavioural change and may help avoid any potential undue caution that parties may have towards self-governance.

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[8] For example, in respect of P326 (Introduction of a non-Working Day adjustment to the Credit Cover Percentage calculation), the BSC panel reconsidered the issue of self-governance when the Workgroup's Assessment Report was presented to it on 10 March 2016.
[9] It should be noted that not all codes require a self-governance statement to be issued.
[10] Our guidance on self-governance decision appeals can be found at:
https://www.ofgem.gov.uk/sites/default/files/docs/2013/10/ofgem_guidance_-_self-governance_modification_appeals_process.pdf

3.15.   Our **Final Proposals** are, therefore, that modifications should be assessed as to whether they require an Authority decision – i.e. **why they are material**.

3.16.   We note that for some codes (MRA and SPAA) the default position is already one of self-governance.[11] In respect of the Grid Code and the Distribution Code, there are currently no provisions in respect of self-governance for modification proposals. We noted in our Initial Proposals that a modification proposal has been raised in respect of the Grid Code (GC0086: Grid Code Open Governance)[12] which is looking at introducing open governance processes to that code, including a self-governance route for Grid Code modifications. We consider that this modification process is the appropriate forum for this to be taken forward.[13] In respect of the Distribution Code, we expect the relevant parties to consider (and if appropriate consult with users on) whether similar governance changes may be appropriate for the Distribution Code governance arrangements.

3.17.   As set out in our Initial Proposals, we expect the code administrators for each of the other codes (BSC, CUSC, DCUSA, iGT UNC, STC and UNC) to take forward the change in respect of the self-governance process, and work with industry to develop the changes, as necessary, to achieve this.

Guidance on the materiality criteria

Initial Proposals

3.18.   In our Initial Proposals, we considered that there is merit in the current approach, which enables the industry to come to a view on a case-by-case basis on what constitutes materiality in relation to particular proposals. However, we recognised that further, high-level guidance on the criteria the industry should consider may be helpful. We set out that panels and code administrators are well placed to develop such guidance, which could be based on experience already gained from the use of the self-governance process to date. Whilst guidance could be developed for individual codes, we noted that it may be more consistent with the principles of CACoP if the code panels coordinate their approach and develop a single, agreed guidance.

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[11] For SEC, we note that there is no default position, rather that the panel assesses the modification proposal to consider which path it should follow.
[12] All documents regarding GC0086 can be found on the National Grid website here: http://www2.nationalgrid.com/UK/Industry-information/Electricity-codes/Grid-code/Modifications/GC0086/
[13] On 17 March 2016, we received the final modification report on GC0086 (see link at footnote 12 above).

Responses to our Initial Proposals

3.19. The majority of respondents who responded to this question were in favour of guidance on materiality being developed, with some commenting that this should be consistently applied across all codes. One respondent commented that it would improve the confidence of panels to make self-governance decisions, while others referred to the greater clarity on the materiality criteria that would be provided by such guidance.

3.20. A small number of respondents had concerns that the guidance could be difficult to develop. One respondent commented that Ofgem must make its own assessment of whether a proposed modification is material and it is therefore inappropriate for Ofgem to delegate this responsibility to code panels.

3.21. Most respondents, however, agreed that panel and code administrators are best placed to develop self-governance materiality guidance. There was support for the guidance to be developed under CACoP and then to use this as common guidance created for all codes. One respondent, who supported the guidance being developed as part of CACoP, felt this should only be a high-level set of principles and noted its view that a materiality assessment has a significant contextual element and may mean different things in different codes.

3.22. Of those who supported the panels and code administrators developing the guidance, a number called for the Authority to set out principles to be followed or to give advice on the level of materiality required in the guidance. Others suggested that Ofgem should approve any guidance that is produced.

3.23. Some respondents, including a number of code administrators, commented that Ofgem is best placed to lead on the production of the guidance. Reasons for this focused on Ofgem's ability to give a cross-code perspective and our role as final arbitrator on whether a proposal is self-governance.

Code administrators' work to date

3.24. At our December workshop, we and the code administrators discussed how and at what stage a code administrator can best help a proposer decide whether its modification is appropriate for self-governance.

3.25. There was some agreement that guidance on materiality may be helpful for panels and code users. However, code administrators voiced concerns that they are not the appropriate party to draft this guidance; rather, that it should be led by Ofgem with input from code administrators.

Final Proposals

3.26.   We agree with the majority of respondents that it would be useful for guidance on materiality to be produced and that introducing guidance on the self-governance process will support panels in the decisions they make and help ensure the basis of these decisions is clearer to industry.

3.27.   With our Final Proposal that modifications should be assessed as to whether they require Authority consent – i.e. why they are material – guidance on materiality will help a proposer come to a decision on the modification path the change should follow.

3.28.   Self-governance decisions are changes that are unlikely to have a material effect on, for example, competition and consumers and can, therefore, be determined by the relevant code panel without reference to the Authority for decision. The code administrators and panels have experience in assessing the materiality of a modification since the self-governance provisions were introduced under CGR and CGR2. We therefore consider it appropriate that the code administrators, with appropriate panel, industry and Ofgem input, develop guidance to support their users and code panel to make this decision. We note that the CMA considered that there is scope to expand the efficient usage of the self-governance scheme and that, to this end, we could publish additional guidance on how to interpret the key materiality criterion. Our view is that the code administrators as part of their increased role, which is discussed further in the following chapter, are best placed to develop this guidance.

3.29.   As set out above, we note that, during the progression of a modification that is identified as self-governance, both code panels and the Authority are able to alter the path the modification will follow to require an Authority decision (and vice-versa). This would be done if it became apparent that the impact of the change is material (again, and vice versa). There are also appeal provisions in place in respect of self-governance changes that provide a further safeguard for parties. We consider that these provisions mean that appropriate safeguards remain in place to ensure that industry can be confident that a change is following the correct modification path.

3.30.   Our **Final Proposal** is that code administrators are well placed to lead work to support us in developing guidance on materiality criteria and the self-governance process, with input from industry. We expect code administrators to work together to produce guidance that can be applied across codes to help proposers assess whether their change should follow a self-governance path. We expect the code administrators to seek input from each panel and agreement from Ofgem on appropriate guidance, and to consult with the wider industry if appropriate.

4. Code Administration

Chapter Summary

This chapter discusses a range of issues related to code administration. It summarises our Initial Proposals and responses to them. It also sets out the work that has been undertaken to date by the code administrators in these areas. It then sets out our Final Proposals to make the code administration and related arrangements more effective, in particular in supporting smaller parties and in driving greater consistency across the code change processes.

Code administration

4.1.   This chapter discusses a range of issues which we have grouped together as generally related to our theme of 'code administration'. These are discussed below under the following headings:

- Guidance on Critical Friend

- Visibility of CACoP and Critical Friend role

- Self-governance and review of CACoP

- Surveys

- Managing code change and cross-code coordination

- Standardisation of modification process and template

- Identifying consumer impacts

- Code administration coordination

- Independence and panel voting

- Other issues

4.2.   The CMA's proposals are for code bodies to take an expanded role to deliver code modifications. We consider that our proposals set out in this chapter should result in both code administrators and code panels being more involved in the modifications process. We consider these changes are consistent with the remedies the CMA has proposed to address its concerns relating to the current industry code governance limiting innovation and pro-competitive change. In particular, the changes outlined in this document should help code administrators to increasingly focus on the service they are delivering to their users: this should help organisations prepare for

the licensed regime through which there will be more accountability over the quality of service delivered to their users.

4.3.   We also note that the CMA considers that there are some reforms that could be implemented in the short term before the introduction of the licensing regime for code administrators. Further, that these reforms should be taken forward by us as part of CGR3. We consider that our Final Proposals set out in this chapter will provide incremental reform and will help to ensure an efficient transition to a licensing regime.

Guidance on Critical Friend role

Initial Proposals

4.4.   In our Initial Proposals, we noted that Principle 1 of the CACoP sets out guidance on how code administrators should achieve their role of Critical Friend, and we noted that making the present guidance mandatory may strengthen the Critical Friend role; however, we also considered there is a risk that it may stifle innovation. In particular, we noted under CGR that we expected the examples provided in this guidance to be refined over time in light of operational practice.

4.5.   We also noted in our Initial Proposals, however, that there have been no changes to the guidance under Principle 1 since CACoP was introduced in 2010. Whilst this may be because the guidance is appropriate, it may also indicate there is further work the industry and code administrators could do to learn from best practice across the codes, and ensure this is reflected in updated guidance. We considered that this may be an alternative to mandating the detailed scope of the Critical Friend role, and would be consistent with our aims when including this as guidance under CACoP in 2010. We indicated that code administrators should work together to update the existing guidance as necessary and take steps to adopt best practice across all the codes.

Responses to our Initial Proposals

4.6.   The majority of respondents to our Initial Proposals who commented, supported updating the guidance on the Critical Friend role in CACoP. Some respondents saw this as an opportunity to extend consistent best practice in code administration across all codes. This included sharing examples of good practice between code administrators.

4.7.   A respondent considered that the role of the code administrator as a Critical Friend needs to be clearly set out and described in more detail. This would include amending the description of Principle 1 to cover support outside the modification process. Another respondent was concerned that further guidance could constrain innovation and instead 'ensuring best practice' implies active review and monitoring of code administrator's performance, which would be more effective at driving behaviour and performance.

4.8.   Another respondent questioned the degree to which Ofgem is judging or evaluating code administrators against CACoP and stated there would be benefit in focusing on specific outcomes, for example the quality of conference call facilities.

4.9.   One respondent set out its view that contractual arrangements work best at ensuring code administrators deliver a good service to industry by setting out what is expected: this incentivises code administrators to provide a good service and a degree of competitive tendering is best at delivering the outcomes set out in CACoP. This respondent also commented that in circumstances where a specific entity or group are required to have in place code administration arrangements there is no clear route for the other code parties to be involved in the management of the services provided.

4.10. The view of another respondent was that there is no evidence that helpful support from code administrators is lacking, with smaller parties choosing not to engage. For this reason, before any changes to the role of a code administrator are made, this respondent's view was that they should be trialled and assessed for their effectiveness before they are rolled out across codes. Trialling of changes was also supported by a second respondent.

4.11. One respondent proposed that the CACoP should apply to the Green Deal Arrangements Agreement (GDAA).

Code administrators' work to date

4.12. At our December workshop, a code administrator provided slides on what a code user should expect from their code administrator. It was discussed whether these slides could form the basis of high-level guidance on the code administrator role of the Critical Friend.

4.13. One code administrator agreed to compile a 'Top 5' list of activities that code administrators should carry out to a high standard that users can access. It was agreed to circulate this amongst code administrators to allow them to consider whether this guidance was appropriate for all codes.

4.14. Following the December workshop, the 'Top 5' list was circulated and a minor amendment made to reflect that code administrators will be impartial and support smaller parties and all change proposals.

Final Proposals

4.15. We are grateful for comments from respondents, and note that the majority supported guidance on the role of the Critical Friend for code administrators.

4.16.   We welcome the 'Critical Friend – Top 5' guidance that code administrators have produced and consider this guidance will be helpful to all code users. In particular, by having agreement on a list of 'Items and Content' all code administrators will adhere to, this allows users to expect a consistent service across codes. We consider the level of detail contained in the 'Critical Friend – Top 5' is appropriate, as it allows code administrators to meet the requirements but allows flexibility and innovation in how this is done.

4.17.   We note the comments from a small number of respondents on how the performance of code administrators is assessed by Ofgem. We discuss the role of metrics and surveys in the assessment of the services provided by code administrators in the section below.

4.18.   As we are not mandating any changes to the Critical Friend role, and instead the code administrators have agreed a list of five key services users can expect them to provide in performing their existing role, we do not agree that there is a requirement to trial this guidance.

4.19.   We note the comment by one respondent that the CACoP should apply to the GDAA. We recognise the benefits of code administrators following the principles contained in the CACoP and that the GDAA code administrator is able to follow these.

4.20.   We also note that one respondent raised concerns that there is no direct route for it to propose changes to code administration services. We would expect code administrators to respond to the feedback they receive from industry parties via the surveys and metrics and to amend the CACoP as appropriate. This is discussed further in the section below.

4.21.   Our **Final Proposals** are therefore that the code administrators should continue to share best practice in line with the 'Critical Friend – Top 5'. We have added this to our website and support its roll out across all code websites to improve the visibility of this role.

Visibility of CACoP and Critical Friend role

Initial Proposals

4.22.   In our Initial Proposals, we considered that the visibility of the CACoP needs to be increased to ensure that code users are aware of what should be available to them. We proposed that this could be achieved by having clear hyperlinks available on all code websites to a dedicated CACoP webpage. This page should include detailed descriptions of the services that the individual codes provide to users in order to meet each CACoP principle. This should help to raise the profile of the document as well as, through greater transparency, to make the code administrators more accountable to their users for how they work.

4.23. Given the low level of awareness of the existence of the Critical Friend role amongst smaller parties in particular, we also considered that the visibility of this role needs to be improved to help increase engagement and ensure all parties are able to make most effective use of the services the code administrators can offer. We set out that we will take steps to make this role more visible on our website so that affected parties can see what the role entails and what administrators can do to support them.

4.24. We considered that code administrators should also make this role more visible on their websites. We suggested that this could be done by each code website having a page that is dedicated entirely to this role. This could include a description of the role and have a clear and obvious link to it on the home page of each website. To make this page more useful and transparent, our view was that each code administrator should detail exactly what it is doing by reference to the CACoP guidance in order to meet the Critical Friend principle and what services it is providing to users. We did not consider that this would be an onerous task and considered that, by clearly signposting this information, it would increase users' awareness and transparency, and may facilitate greater consistency of approach across the codes.

Responses to our Initial Proposals

Visibility of CACoP

4.25. Most respondents supported achieving greater visibility of the CACoP through clear links available on all code websites. Respondents considered that this initiative was considered relatively easy to achieve. There was general agreement that both Ofgem's and each code administrator's websites should include easy access to the CACoP. One respondent commented that more active engagement techniques were required from the code administrators. Another respondent suggested having a single website for all code administrators.

4.26. Some respondents considered that, as the CACoP is already published, there would be limited benefits of the proposed approach and noted that greater visibility did not necessarily improve outcomes. There was also a question on how this would be administered and funded.

Visibility of Critical Friend role

4.27. On the Critical Friend role being better advertised, the response was positive with most respondents agreeing that there would be benefits. It was thought that advertising could include promotion of the role by both the code administrators and by Ofgem.

4.28. Some respondents thought the proposal could even introduce competition between code administrators to drive improvements. It was suggested by several

respondents that advertising the Critical Friend role could be through a central Ofgem web page containing links to the various code administrators.

4.29. The code administrators' websites were identified as being in need of improvement through better signposting to guidance and the identification of key contacts.

Code administrators' work to date

4.30. As set out in the previous section, the code administrators have developed a 'Top 5' list of activities that they should carry out in their role as Critical Friend.

Final Proposals

4.31. We welcome the 'Critical Friend - Top 5' being published on the websites of all the code administrators.

4.32. We support the view that the visibility of the CACoP needs to be increased and that it would be beneficial to all users of the codes to have a better understanding of how the individual code administrators meet each of the CACoP principles, as supported by the respondents to the Initial Proposals. This can be achieved by having clear links available on all code websites to a dedicated CACoP page. This page should include detailed descriptions of the services that the individual codes provide to users in order to meet each CACoP principle. We consider that this should increase awareness, in order to help raise the profile of the document and to improve transparency to make the code administrators more accountable to their users for how they work.

4.33. We consider the creation of a dedicated CACoP page could be achieved through little cost and that value would be added to code parties by improving awareness and accountability, which would easily offset this small cost. A single webpage would also provide for a consistent approach between codes to improve the signposting of information.

4.34. Our **Final Proposal** is for the 'Critical Friend – Top 5' to remain highly visible on each code administrator's website. Our **Final Proposal** is also for each of the code websites to have a dedicated CACoP page which provides information as to how the code administrator meets each of the CACoP Principles. We expect each of the code administrators to take this forward.

Self-governance and review of CACoP

Initial Proposals

4.35.   Principle 4 of the CACoP sets out that the document must be periodically reviewed, with any changes proposed following such a review required to be approved by the Authority. In our Initial Proposals, we considered that the CACoP review process could be streamlined and that one way of doing this would be to introduce a self-governance process into the review so that minor, non-material changes can be made without the need for Authority consent. We also considered that it may be appropriate for the CACoP to be reviewed less frequently than on an annual basis (although retaining the ability for change to be brought forward at any time, should it be required).

Responses to our Initial Proposals

4.36.   A large number of respondents commented on these issues. Of those that did, a small majority supported the proposal to introduce a self-governance process to the review of CACoP for minor, immaterial changes.

4.37.   A number of respondents did not agree with our proposal. One respondent felt that, as CACoP sets minimum standards in code administration, it was not appropriate for code administrators to set these standards themselves. Respondents also commented that Ofgem, as a body that looks across codes, should be central to any review and in a position to assess the cost benefit analysis of any change. Concerns around the process that any self-governance changes would follow were also raised.

4.38.   We also asked for views on how frequently the CACoP should be reviewed. Some respondents suggested review periods of two or three years; however, the majority of respondents agreed that an annual review was appropriate. It was also highlighted that there should be flexibility to allow for ad hoc reviews.

4.39.   A small number of respondents felt that the period of the review was not important. Instead, reviews should be carried out when requested by a panel, code administrator or Ofgem. It was also considered that the results of the surveys could be a trigger.

Code administrators' work to date

4.40.   The code administrators have been working on a review process under Principle 4 of CACoP. This was put on hold following discussion at our December workshop to allow the process to reflect our Final Proposals.

Final Proposals

4.41. The CACoP contains a set of principles for code administrators to follow; beneath the principles is guidance, which should assist the code administrators in meeting the principles.

4.42. The annual reviews that have so far taken place have resulted in mainly minor changes to the detailed guidance points, which have had no significant effect on the substance of the best practice principles or how these are applied by the different code administrators. The proposal to introduce a new Principle 13[14] was not the result of the annual review process but was instead developed following concerns raised by the BSC panel.[15]

4.43. Since publishing our Initial Proposals, we have given further thought to the CACoP review process and taken into account the responses to our consultation. In particular, we consider the key point is not necessarily around the process for reviewing CACoP, but rather that the CACoP sets out the principles of best practice and that code administrators' behaviour should adhere to these principles. We consider that an effective review should focus on how well that is happening, and not necessarily on the detailed drafting of the CACoP itself.

4.44. In light of this, we consider there may be a more effective way to meet the objective of keeping CACoP and best practice under review than introducing a self-governance change process. As we set out in 2010, the outcome of the metrics reported on annually by the code administrators under CACoP Principle 12[16] and the surveys that we propose are undertaken (see below) could lead to improvements being identified and, therefore, potentially more substantial changes being proposed. We consider that the proposals we are making in respect of the development of the reporting metrics and surveys will strengthen this ability. In responses, the majority view was that it is appropriate that CACoP is reviewed annually. By taking into account the outcomes, as appropriate, to both the reporting metrics and the surveys, we consider that the effect is an annual review of CACoP.

4.45. We note that a number of respondents considered that there should continue to be a role for Ofgem in the review of CACoP, as Ofgem looks across all codes. Also, given that CACoP sets out the minimum standards in code administration, concerns emerged that it was not therefore appropriate for code administrators to set these standards themselves. Given that the principles and underlying guidance within CACoP are now firmly established, our view as noted above is that the focus should be on reviewing how effectively code administrators adhere to these principles, rather than

[14] Principle 13: Code Administrators will ensure cross Code coordination to progress changes efficiently where modifications impact multiple Codes.
[15] https://www.elexon.co.uk/wp-content/uploads/2014/10/12_236_07_CACoP_Principle_13_PUBLIC.pdf
[16] Principle 12: The Code Administrators will report annually on agreed metrics.

focusing on the detailed drafting of the CACoP document itself per se. In the event that housekeeping changes to CACoP are identified, we encourage code administrators to establish a process to record these changes so they can be submitted for Authority approval at an appropriate time, ideally alongside any more substantive changes that may be identified.

4.46. Our **Final Proposals** are therefore that a self-governance process for CACoP changes should not be introduced at this time. Further, that the key input into any developments of CACoP should be reflective of the outputs from the metrics and surveys. We expect code administrators to work together to establish a proportionate, transparent review process in light of these Final Proposals.

Surveys

Initial Proposals

4.47. In our Initial Proposals, we considered that it is important to have effective, fit for purpose reporting metrics that help achieve the principles underpinning the CACoP and that the current metrics may need to be reviewed to ensure this. We considered that quantitative metrics are useful, not so much for cross-code comparison, but to track progress within an individual code. As such, we considered that code administrators should continue to report on the quantitative metrics, but that such metrics need to be improved to make them clear as to exactly what each code should be reporting on to maintain consistency.

4.48. We set out that the qualitative results should then be useful when comparing current practice across codes. In order to improve the usefulness of such results, we proposed that a qualitative survey should be sent out periodically by one body to all code users covering all codes, which could be led by an industry body or Ofgem. A report could then be produced to compare across all codes. This report could also contain a section for each code mapping the quantitative metrics across the years that they have been reported on.

Responses to our Initial Proposals

4.49. The majority of respondents supported the view that a single body should lead a single qualitative survey covering all codes. However, there was no agreement on which body this should be. Among those who did make a suggestion, it was fairly evenly split between an independent party either commissioned by the code administrators or by Ofgem. There was one suggestion that such an independent party should be paid for by the codes.

4.50. Most respondents agreed that the current quantitative metrics need improving, while one respondent said they were not aware what the current metrics were. Some respondents suggested that several of the current metrics are not a reflection on the

performance of the code administrator; rather they just give context about how the code is running. Some suggestions were given as to how these metrics can be improved, for example, omitting the metric which measures Ofgem performance[17] and including more detailed guidance on how each metric should be reported to ensure a more consistent approach across the board. One respondent suggested measuring the types of parties who respond to each consultation as a measure of engagement.

4.51.   One respondent suggested that Ofgem should publish all these reports. Two respondents wanted more information regarding how any changes to the current system would be funded.

Code administrators' work to date

4.52.   We have been working with code administrators to review the current metrics, both at the December Workshop and in informal consultations. We have received some useful feedback as to what they think the best metrics are to measure their performance.

Final Proposals

4.53.   We agree with the view that a single body should lead a single **qualitative survey**. This would not only cut down on the number of surveys that parties need to complete but a single survey would also allow for direct comparisons between code administrators.

4.54.   Although the code administrators currently fulfil this role individually, we do not consider this should be taken forward directly by them collectively. This may slow down decision making when attempting to agree on the content of a single survey. Instead, we agree with a number of respondents that it should be undertaken by an independent (to code administrators) third party. Our view is that currently Ofgem is best placed to take this task forward.

4.55.   This approach will enable not only independence from the code administrators, but also allow us to bring in parties who are experts in the field of surveys. We also note the CMA provisional remedies, which proposes licensed code bodies whose performance is monitored by Ofgem. Ensuring consistent customer surveys which comply with best practice are the kinds of initiatives which could help assess the quality of service being given by code administrators to their users.

4.56.   As set out in the previous section, we consider that the output from this survey should provide a useful tool in considering whether the Principles set out in the CACoP

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[17] Average time between a proposal being submitted for decision and a decision being published.

need to be amended, in order to better reflect the expectations of the service that the code administrators should be providing.

4.57.   Our **Final Proposal** for the **qualitative survey** is that Ofgem should commission an independent third party to undertake a cross-code survey and that the final report should be published on the Ofgem website. We consider that the code administrators should fund this survey (given they all individually already fund user surveys) and alongside these Final Proposals we are consulting on potential options for allocating the costs across the various code bodies.

4.58.   We agree that the **quantitative metrics** need improving and require greater visibility if the results are to be helpful to the industry. We consider it necessary to amend the questions to improve clarity and ensure that all code administrators are reporting on the same data in the same manner. We do not think that such a data collection exercise can necessarily be used to compare code administrators; rather, the data should show a snapshot of the current workings of each code and its progression over time.

4.59.   Alongside these Final Proposals, we are consulting on exactly what data should be collected. We expect that, following the outcome of the consultation, code administrators will submit to us their data for the first quarter of 2016. We will then expect results to be submitted by the end of the month following each quarter (i.e. submit data by the end of July for Q2, by the end of October for Q3, etc.).

4.60.   Our **Final Proposal** for the **quantitative data metrics** is that Ofgem should prescribe the exact data to be collected and that code administrators should fill out such data collection forms on a quarterly basis and submit their results to Ofgem to be published on our website. Subject to our separate consultation, we expect to implement this through approving an appropriate change to CACoP Principle 12.

Managing code change and cross-code coordination

Initial Proposals

4.61.   We proposed that all panels develop a forward work plan, in consultation with the industry and Ofgem, which takes into account, for example, Ofgem's published Forward Work Plan and ongoing significant major Ofgem and/or government priorities. In developing forward work plans, we expected coordination across codes to ensure consistency.

4.62.   In addition, we considered that panels could take a more proactive approach to managing 'major' industry change, including cross-code change and potentially also establishing arrangements to ensure oversight of end-to-end delivery of central systems changes, where appropriate. For example, the codes could provide for the panel to be able to put in place appropriate project management and/or assurance

arrangements to provide for greater oversight and to coordinate major change. We noted that this is consistent with the approach now being adopted to manage the end stages of Project Nexus.

4.63. We also noted the approach to managing code change and cross-code coordination that we and industry are adopting to implement the electricity European Network Codes (ENCs). The industry has established the Joint European Stakeholder Group, made up of industry representatives as well as representation from DECC and Ofgem. We noted similar groups to these could be set up to work on other policy initiatives to ensure robust and focused analysis and effective use of resource.

4.64. The approaches we suggested aimed to provide for a more strategic approach for panels in managing code change and cross-code coordination, while retaining the benefits of open governance by enabling parties to continue to raise modifications as per the existing arrangements. We noted that whilst this extension of their role would be something that could be taken forward by each panel, there would be benefit to industry participants in ensuring that there is a coherent and coordinated approach across all codes. Initially, we considered a group should be set up to look at how such an approach could be taken forward in a consistent manner.

Responses to our Initial Proposals

4.65. A number of respondents commented on the management of code change and general cross-code co-ordination. These responses in principle supported greater co-ordination, with there being recognition that stronger cross-code working and shared engagement by code administrators was required. The consistency of links and use of standardised templates were all highlighted as suggested improvements.

4.66. The views we received were that forward work plans should be kept high level to allow for a general overview and not become a disproportionate burden to the code administrators. One respondent thought that current efforts could be enhanced but should also remain proportionate.

Code administrators' work to date

4.67. At the December workshop, two ways of enhancing cross-code coordination were discussed. These related to a tool to register all live modifications across all industry codes and a joint working process to cover modification proposals that could affect more than one code. Subsequently, code administrators have been developing the live modification register, which would act as a 'one stop shop' for all interested parties to view all modification proposals.

4.68. Code administrators have also developed a joined-up process for modifications that may impact more than one code. This includes an identification process for cross-code impacts, establishing arrangements for oversight of the process and the

associated approach to be taken. It also deals with the setting up of workgroups, how joint consultations are undertaken and how these are reported and communicated.

Final Proposals

4.69.   We support the development of a live code modification register as a tool to register all code modifications and determine potential cross-code coordination opportunities which will cut across, and assist in, forward work planning. Such a register should enable all interested parties to view in one place all modifications across all codes. We consider that such a tool should be simple to use and linked to the relevant part of each code administrator's website. We would expect that such a tool would include information such as the proposing organisation, codes impacted and the status of the modification.

4.70.   We welcome the development of a process for identifying modifications that involve more than one code and for a subsequent, efficient joint modification process to be adopted. We consider that this will reduce duplication across codes and enable the effects of the modification proposal to be considered across all codes and affected parties simultaneously. We welcome the work that has been undertaken and expect this to be promoted and followed by the code administrators.

4.71.   We continue, along with the CMA, to consider that the development of forward work plans at a high level will enable code administrators to manage change at a strategic level. We note the CMA's view that we could provide significant incremental value by developing, in collaboration with the relevant code bodies, a series of documents that set out the changes needed to deliver the strategic direction for each code. In preparation for this remedy, we consider that the code administrators, with input from code panels and industry should work to develop their own forward work plans.

4.72.   As set out in our Initial Proposals, we continue to support that each code could provide for the panel to be able to put in place appropriate project management and/or assurance arrangements to provide for greater oversight and to coordinate major change. We would also note the expectations of the CMA to expand the role of code administrators to take on project management responsibilities; appropriate obligations in relation to this could be included as part of the proposed new licensing arrangement.

4.73.   Our **Final Proposals** are for: (i) code administrators to continue to develop and implement the modifications register; (ii) code administrators to publish on their websites, and to use, the joint process for cross-code modifications; (iii) code administrators to monitor the performance of the process when modifications follow it; (iv) individual code administrators, with support from their respective code panels, to initiate work to explore how to develop an effective forward work plan, going forward (and subject to the CMA's final decision) these will also take into account the work

taken forward by Ofgem to develop a strategic view; and (v) for each panel to consider and to establish project management and assurance provisions.

Standardisation of modification process and template

Initial Proposals

4.74.   We noted that the CACoP currently sets out a modification process, although this is currently not standardised across all codes. A more standardised modification process would mean that users will know how to raise a modification in all codes just by knowing one process. We considered that such a process could be decided by the code administrators working together, with our input, and could be published in the CACoP. Another way to aid engagement would be to standardise the modification templates across all codes. We proposed that there should be a standard template for each step of the process (i.e. for raising a modification, progressing it through workgroups, sending it out to consultation and producing the final modification report). We considered that, when producing such templates, thought should be given to having a clear front page which outlines the proposal, solution, recommendations, and any other useful information. Such a template could be produced by the code administrators with input from Ofgem and industry participants and included in the CACoP.

Responses to our Initial Proposals

4.75.   There was strong overall majority support for the proposal from respondents. One respondent considered that this proposal may specifically help smaller parties. There was some acknowledgment that there have been previous attempts to standardise the modification process and templates towards a more aligned approach. There were a number of comments from those who favoured the existing modification forms that appear in certain codes, with the CUSC, UNC and BSC all mentioned. Despite the support for consistency, there was recognition that the codes themselves were all different and that this needed consideration, in particular in respect of the style and layout of templates and the ability to include specific criteria.

4.76.   One respondent thought that the template could be split in two, comprising both a generic part that was general to all codes and a part specific to a particular code. From those who did not support the proposal, the differing governance and role of administrators was cited, and there were concerns regarding the potential to increase burdens during a period of significant change.

4.77.   Determining the best and insofar as is practicable, templates to use as the baseline was considered by one respondent to be a significant piece of work that should be completed with industry consultation. As such, the possible costs involved were identified with the call for an impact assessment from one respondent.

Code administrators' work to date

4.78. Following the December workshop, the code administrators have developed a standardised modification template. The template actually consists of four separate documents: Stage 1 - Modification Proposal; Stage 2 - Workgroup Report; Stage 3 - Draft Modification Report; Stage 4 - Final Modification Report. There are four documents as they are colour coded according to the stage of the process that the modification proposal is at. However, the intention is that the document is developed in a consistent manner as the modification proposal goes through the process.

Final Proposals

4.79. We welcome the development of a standard template to be used across all codes. This should assist those who work across more than one code. We recognise that there are differences between codes, but consider that the processes and templates should be as similar as possible. We recognise that there will be a period of familiarisation for users of the new templates but consider there to be longer term benefits. We also consider that the development and use of a standard template should help to ensure that the differences in the modification processes across codes should reduce.

4.80. In respect of the template itself, as noted above the code administrators have developed a standard template following our December workshop. The code administrators have developed a separate, colour-coded template for each of the main stages of the modification process (e.g. for initial proposal, workgroup report etc.). We note this results in four templates, rather than a single template to apply throughout the modification process (which is the approach currently adopted under some of the codes). We recognise the benefits of the colour coding of the templates providing a very clear understanding of the progress of the modification proposal. That said, our view is that each template for each document should be as similar as possible, this would then be increasingly populated as the modification proposal goes through the modification process.

4.81. Our **Final Proposal** is for a standard modification template to be used across all codes. We expect all code administrators to adopt this standard template. We expect the use of this template to reduce the differences in the overall modification process across codes.

Identifying consumer impacts

Initial Proposals

4.82. We considered that including a consumer impacts section on every change proposal form would help to ensure that consumer impacts are considered through the entire modification process; we therefore proposed that such a section should be

included in each form. If possible, we noted that this should be filled in by the proposer when a modification is raised. However, if such impacts are not known, this should be filled in as soon as possible and reviewed at every stage of the process (i.e. workgroups, consultations and panel discussions). As such, consideration of consumer impacts should be included in the Terms of Reference for each of the workgroups. We did not envisage this section on the change proposal form to be used to decide whether or not the impacts are beneficial; rather, it would be to consider issues such as how it affects consumers, what type of consumers and an approximation of how many would be potentially affected. If it were considered that a modification would not have any impact on consumers, we would expect a note explaining why this is thought to be the case and revisited as above if new information comes to light.

4.83. We considered that these changes could be taken forward by the relevant industry party and that it may also be helpful to set out in CACoP how consumer impacts should be considered.

Responses to our Initial Proposals

4.84. There was strong support for the introduction of a consumer impacts section with few objections, although some respondents raised points which they considered highlighted the need for further consideration.

4.85. In supporting the proposal, one respondent thought it would improve transparency and clarity, while another suggested it would encourage active discussion and regular and closer ties between code administrators and consumer representatives.

4.86. One respondent thought that direct consumer impacts would be difficult to identify. A further view was that consumer interests are already considered through the assessment of the relevant code objectives.

4.87. One respondent thought the consumer impact should not substitute the wider Ofgem assessment, whilst another identified the issue of parity with other impacts.

4.88. The provision of guidance on making an assessment of the consumer impact was also mentioned.

Code administrators' work to date

4.89. The code administrators have included a section that will cover consumer impacts within the standardised modification template.

Final Proposals

4.90.   We welcome the support for the inclusion of a consumer impacts section in the modification template. We recognise the concerns raised regarding the potential difficulties in identifying these impacts. However, we consider that, by including the section in the template, it will mean that at all stages of the modification process the question should be asked as to what the impacts of the proposal could be on consumers. This should assist consumer representatives seeking clarity on the potential impacts on consumer. We agree this would not substitute the wider Ofgem assessment, but it should be more efficient and helpful in highlighting throughout the modification process the expected consumer impacts, so that industry and we can take full account of these in assessing the modification and coming to a decision.

4.91.   Our **Final Proposal** is for a consumer impacts section to be included in every modification proposal template. We expect industry to follow the process and for consumer impacts to be continually assessed through each modification proposal process.

Code administration coordination

4.92.   In the previous sections of this chapter, we have set out our Final Proposals for a number of areas in respect of code administration. In order for our Final Proposals to be implemented in a coordinated and standardised manner, all code administrators will need to work together.

4.93.   At the code administrators' workshop the question of needing a 'lead' code administrator was touched on in some of the areas discussed. We agree that it would be helpful for one code administrator to lead the coordination of input from all code administrators and that this is a role that the host CACoP code administrator[18] could helpfully take on. We do not consider that this would be an onerous task, and would note that it would not be for this lead code administrator to undertake all of the tasks, but purely to ensure that our Final Proposals, and any further initiatives, were being taken forward in a coordinated manner across all codes. We also recognise that there will be a role for Ofgem to engage with the industry in the implementation of our Final Proposals in these areas.

4.94.   Our **Final Proposals** are therefore for a 'lead' code administrator to coordinate across all codes the implementation of our Final Proposals and lead on cross code coordination on an enduring basis; we consider that this role should be held on an annual basis by the host CACoP code administrator.

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[18] The code administrator responsible for coordinating the annual review of the CACoP. This role is rotated on an annual basis.

Independence and panel voting

Initial Proposals

4.95. **Independent panel chairs**: we proposed that each code panel has an independent chair. As per the arrangements we introduced under CGR, it would be for the licensee(s), having particular regard to the views of the relevant panel, to ensure that they have discharged the requirement that the panel chair be independent. As with the existing codes that have this approach, we proposed that the Authority should have a right of veto over any candidate put forward by the licensee.

4.96. **Independent panel members**: we proposed, for modification business at the very least, that panel members should act independently (i.e. voting members must act impartially and not represent the interests of their employer and/or constituency). This should also mean that panel members provide reasons as to why the modification proposal better facilitates the relevant objectives of the code. We did not expect such panel members to be independent of the energy industry, but they must act in an independent manner and there must be controls in place to achieve this. We also proposed that the DCUSA and SPAA voting should be undertaken by panel.

4.97. **Independent workgroup chairs**: We considered that workgroups should be chaired independently, and we proposed that this could be achieved through code administrator chairs. We recognised that in some cases, the code administrator function is carried out by the System Operator and not a separate code administrator entity. We considered that the representative of the licensee, acting in the capacity as code administrator rather than representing National Grid Electricity Transmission (NGET) as the System Operator, could provide an appropriate degree of independent chairing. We noted that there may be some instances where the code administrator might have a direct interest in the modification, in which case it may be appropriate for an alternative chair to be in place.

4.98. We noted that, were these proposals to be implemented, they would require changes to the current requirements of the panel or workgroup in respect of some of the codes. We set out that we would expect the relevant party to take forward such changes, which in the case of independent panel chairs would require an appropriate licence change, as was the case for implementation in the CUSC and the UNC.

Responses to our Initial Proposals

4.99. The majority of respondents responded to one or more questions in this section of our Initial Proposals. The main points from the responses are highlighted below.

4.100. **Independent panel chairs:** A majority of respondents supported code panels having an independent chair. Some of these respondents sought clarity from us on whether independence means impartiality rather than a chair appointed from outside

of industry. Some respondents highlighted the different governance arrangements under certain codes (DCUSA, MRA, SPAA) and queried whether our reference to code panels relates exclusively to where those bodies conduct modifications business. Some of the respondents who were not supportive were concerned that independence here means fully independent of industry and there would be costs involved in appointing an independent panel chair in those circumstances; others were concerned about the potential loss of expertise if the panel chair appointed is fully independent of industry. One respondent suggested that one way to keep the costs of appointment low could be through a single independent chair appointment made for multiple panels where appropriate, e.g. NGET, as licensee for all the codes it owns, appoints a single chair.

4.101. **Independent panel members:** Most respondents agreed that panel members should act impartially. Some of these respondents, however, interpreted impartiality as independent of their employer only. They considered that panel members appointed by a constituency of parties could represent all those parties' interests collectively (and therefore could still be 'impartial'). One respondent distinguished between panel members for commercial codes (who should act impartially of all interests) and those for technical codes (who should not act impartially but represent the interests of those appointing them to facilitate their engagement in code modification processes). Some respondents wanted to review the current composition of panels should panel members currently appointed to represent a constituency of interests be expected to act fully impartially of all interests. One respondent considered that having paid panel members who perform only the role of panel members, rather than electing or appointing paid employees from industry to panels, would ensure full impartiality.

4.102. **DCUSA and SPAA voting:** There was a split in respondents' views on voting by DCUSA and SPAA panels on code modifications instead of by code parties. Some of the respondents supportive of panel voting highlighted that this would be consistent with other codes' voting arrangements. However, they also highlighted that the current constituency-based composition of these panels may need to be revisited as a result. A number of respondents who did not support DCUSA and SPAA panel voting considered that party voting on DCUSA and SPAA modifications provides these parties with direct participation in the modifications process, which would otherwise be lost. Some of these respondents questioned how transparent the panel voting would be and whether panels would provide reasons for their decisions. One respondent considered the current situation where no customer representatives (with voting rights) participate on the DCUSA panel or in workgroups as unacceptable.

4.103. **Independent workgroup chairs:** A large majority of respondents supported independent workgroup chairs, with many also supporting code administrators to perform this role. Those in support highlighted the benefits: industry expertise would be focused in the workgroup membership rather than in the workgroup chair role; more stakeholder engagement by smaller parties where there is an independent chair; greater accountability of an independent chair to code panels and stakeholders on the quality of the delivery of modification assessments; and an independent workgroup chair would be more focused on efficiently delivering assessment of a code change based on its urgency and in line with the timetable set by the panel. Some

respondents, though supportive, also noted that code administrators need the right expertise or skills to manage workgroup meetings; questioned whether code administrators would require increased resources to undertake the workgroup chair role and, if so, who would pay; and noted that code administrators could not be fully impartial if code changes affect them.

Final Proposals

4.104. In our Initial Proposals, we highlighted the important role of independence in code governance processes. The presence of panel chairs and members who are elected or appointed but who **act** independently (i.e. impartially) can provide for more effective code governance, for example in respect of consideration of the code's relevant objectives. Further, they can help provide more effective oversight of code administrators, thereby increasing code administrators' accountability to code participants. Independent workgroup chairs can increase the robustness of industry assessments by providing a more focused approach to delivery of those assessments. They can also help ensure that smaller participants and consumer representatives are more confident about and can trust the code processes and better engage with them as a result.

4.105. Some respondents questioned the meaning of independence in this context. We consider that independence need not mean fully independent of industry so long as the code panel/workgroup chair and panel members undertake their duties in accordance with the code requirements (which, in some cases, expect them to **act** with impartiality or independence from those who have appointed them[19]) and the panel objectives and **are seen to do so**. We consider that it would be helpful for all the codes to ensure that panel/workgroup chairs and panel members act independently (i.e. impartially). However, we consider that how effectively these chairs and members deliver positive code governance outcomes in practice is key, and achieving this does not necessarily need specific requirements in the licence or code as to who carries out these roles or who appoints them. Below we set out our Final Proposals for each of the areas considered.

4.106. **Independent panel chairs**: in setting out our views below, we consider that these views apply to code panels regardless of the type of business they are carrying out in line with the relevant code requirements. In our view, panel chairs should **act** independently (i.e. impartially) however they are appointed. Panel chairs have a specific role to play in relation to code governance processes: building trust and providing confidence to all code parties and interested stakeholders that panel business is carried out in a sound manner; ensuring effective oversight of code processes on behalf of stakeholders, working with appointed panel members; ensuring

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[19] For example, the CUSC Section 8.3.4 and the DCUSA Section 1B Clause 6.16.1 sets out that panel members should act impartially/independently when acting in that capacity.

that all panel members are treated fairly and equally in the conduct of business; and efficiently and effectively managing panel meetings.

4.107. We consider that licensees with the relevant responsibility in their licences (BSC, CUSC, UNC) should continue to fulfil the requirement to appoint an independent panel chair, with the Authority having an approval role in relation to the candidate put forward. For other codes where there is no such licence requirement, we do not propose to add such a requirement. We agree with a number of respondents that to add such a requirement could be a significant change, particularly in the context of the CMA's ongoing work which encompasses code governance, and therefore may not be proportionate for all codes at this time. We also note that some respondents raised the question of cost in respect of the appointment of panel chairs that are independent of industry. However, we consider that an independent chair would, at most, result in a small incremental cost. It is for those appointing panel chairs to consider how, and by whom, the duties and role of the panel chair described above are best achieved when considering potential candidates for appointment and how an appropriate degree of independence may be achieved. We note that some respondents consider industry expertise in the panel chair role is important for technical codes. In those cases, it is for the relevant licensee(s) as code owner(s) to identify who is best suited to undertake the duties and role to deliver the most effective outcomes for all interested parties, regardless of their level of technical expertise.

4.108. Our **Final Proposals** are therefore not to add a licence requirement for appointing panel chairs where this does not already exist. We note that, where licences and codes currently provides for an appointment, subject to Authority approval, this arrangement will continue. For the other codes, we expect careful consideration to be given during the appointment process as to whether potential candidates are suited based on their ability to act independently (i.e. impartially) to deliver effectively the duties and role of panel chair.

4.109. **Independent panel members**: panel members, are expected, among other things, to provide clear reasons against the code objectives when voting on modification recommendations/decisions. Similar to panel chairs, panel members have a role in building trust and confidence in the governance arrangements among stakeholders, in particular, those with less resource to engage. Therefore, how panel members **act** determines whether they are performing their duties effectively as panel members in line with code requirements.[20] We note that some respondents interpreted independence when applied to panel members as meaning independent of the member's employer but not of the constituency interests that elected/appointed him/her (in those codes where this approach applies). We consider that panel members should aim to meet the code requirements, including assessing code modifications and providing reasons against the objectives, regardless of who they represent. We acknowledge that acting 'impartially' is, of itself, not incompatible with

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[20] As with panel chairs, some codes state explicitly that panel members must act impartially/independently when carrying out their role (BSC Section B2.8.1 and DCUSA Section 1B Clause 6.16.1).

election/appointment by specific interests, so long as the outcomes achieved meet code requirements and result in thorough, robust and effective decisions and recommendations by panels. We therefore do not intend to mandate a change to those codes where panel members are appointed to represent constituencies of code parties. However, we do expect all panel members to act impartially in fulfilling their role. Continued transparency in decision making should result in appropriate industry oversight of this, and panel chairs may also have a role in holding panel members to account in how they fulfil their role. We note that one respondent's view is to pay dedicated panel members so they do not 'represent' any interests. However, we consider that this approach would not necessarily improve panel recommendations and decisions on modifications.

4.110. The quality of panel members' recommendations and decisions, clearly reasoned against the code objectives, is paramount. This should be a key focus of panel members' responsibilities to code parties and wider stakeholders, whether the code requires them to act impartially or to represent the wider interests of those who appoint them. There are controls in place in some codes to ensure that panel members place their duty to carry out their responsibilities above those of their employers. In the case of technical codes, while panel members bring a level of expertise to their role which may arise through their employment, they still need to provide clear justification for the outcome of their votes as panel members against the code objectives. In this regard, we would note the CMA's view that the analysis supporting recommendations from code panels should be sufficient for Ofgem to take a decision.

4.111. Our **Final Proposal** is that we will not mandate a change to those codes where panel members are appointed to represent constituencies of code parties. We expect panel members to provide clear reasons for their views on code modifications, assessed against the code objectives, in order that the Authority can understand how a voting decision was reached. By doing so, panel members will help build trust and engagement with parties who have an interest in the codes to deliver effective code processes.

4.112. **DCUSA and SPAA voting:** for all codes, there is a licence requirement that final reports on code modifications detail clear reasons, set out against the relevant code objectives, as to why a particular recommendation or decision has been made.[21] Whether the recommendation or decision comes from a panel vote (with the panel or panel members providing reasons) or from a party vote, a clear statement of the outcome is necessary, as it should assist the Authority in reaching its decision, or may assist parties in deciding whether to appeal a modification decision. In respect of the DCUSA and SPAA, party voting is the equivalent of panel voting under other codes.[22]

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[21] In respect of DCUSA, the relevant licence requirement is in the electricity distribution licence (Standard Licence Condition (SLC) 22.10(c)). In respect of the SPAA, it is in the gas supplier licence (SLC 30.9(a)).
[22] We note that under the SEC the change process includes both a party vote and change board vote. However, as this process has only recently gone live no vote has yet been undertaken.

Under SPAA, we note that parties attending the relevant SPAA Change Board vote on change proposals against the relevant objectives and then provide decisions (or recommendations to the Authority as the case may be) on the proposals.

4.113. In May 2015, we made a decision on party voting practices under DCUSA.[23] We noted in our decision that we would keep under review a possible change to panel voting under DCUSA if there was a strong case for it. Since our decision on that modification proposal, we are aware of one example under DCUSA where a split vote in one party category resulted in a recommendation affected by that vote but where not all parties in that category provided reasons for their vote against the code objectives. This suggests that there is still a risk with the current arrangements that where parties vote, reasons against the objectives are not provided or can be unclear and the Authority may then need to undertake further consultation to understand parties' views on a modification prior to making a decision.[24] This underlines our concerns about the need for an effective voting mechanism and the importance of providing a clear rationale for any recommendation and how this can best be achieved.

4.114. In light of the split views provided in responses on the benefits of panel voting under DCUSA and SPAA compared with current party voting, and the potential need to revisit current panel composition as a result, we do not intend to mandate change at this time. However, we expect industry to review whether the current governance arrangements under both codes achieve the appropriate outcome, namely that the voting mechanism is fit for purpose and that modification decisions and recommendations are accompanied by clear reasons against the code objectives, and, if not, to consider further changes that achieve clarity on the reasons for the outcomes of party votes on modifications.

4.115. We note the concerns of one respondent about lack of customer representation and voting rights on DCUSA panel and workgroups. We welcome and encourage greater customer representation on workgroups to provide customers' expertise during the workgroup assessment. The outcome of modification votes is based on whether the code relevant objectives are better facilitated. By assessing the consumer impact (in line with our Final Proposal above (paragraph 4.91)) with input and engagement from customer representatives, we expect workgroup assessment and DCUSA party votes to reflect outcomes that will benefit consumers. As part of the review we have proposed, industry should consider whether the current DCUSA

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[23] DCUSA proposal DCP214 (Voting) was approved by the Authority on 22 May 2015. Our decision letter is here: https://www.ofgem.gov.uk/publications-and-updates/distribution-connection-and-use-system-agreement-dcusa-dcp214-voting

[24] DCP228 (Revenue Matching in the CDCM) is a recent example of where the vote in one party category (Supplier) was split and therefore the recommendation to reject in the Supplier category skewed the entire party vote on this modification. One Supplier party provided no reasons why it voted to reject. We undertook a further consultation on DCP228 before making our decision: https://www.ofgem.gov.uk/publications-and-updates/consultation-proposal-amend-arrangements-scaling-under-common-distribution-charging-methodology-dcp228

arrangements provide for effective consumer representation to inform decisions and recommendations within the code arrangements. In making our decisions, we must always consider our principal objective to protect consumers (and our wider statutory duties), and will take full account of all consumer views and impacts in reaching a decision, irrespective of which parties have participated in voting on a proposed change.

4.116. Our **Final Proposals** are therefore not to mandate change to the panel voting arrangements under DCUSA and SPAA governance at this time. However, as noted, we expect industry to review whether party voting is achieving the necessary outcomes that ensure that modification recommendations and decisions are accompanied by clear reasons against the code objectives.

4.117. **Independent workgroup chairs**: we welcome that there was clear majority support in responses for independent (i.e. impartial) workgroup chairs and for code administrators to fulfil this role. As with panel chairs, workgroup chairs are expected to fulfil a specific role: building trust and confidence amongst workgroup members and wider stakeholders that workgroup assessment is carried out effectively; ensuring that meetings are run efficiently in line with panel instructions on timetable; and ensuring that workgroup members are treated equally and fairly during workgroup discussions. These were the benefits of an independent workgroup chair highlighted in some responses. As a consequence, an independent chair should encourage wider participation from stakeholders with the relevant expertise in workgroup assessment and from others with an interest in modifications with the outcome of improved workgroup recommendations.

4.118. We note specific concerns raised by some respondents about code administrators' expertise and the possible cost of code administrators acting as workgroup chairs. In our view, the expertise should lie in workgroup membership with the workgroup chair acting as an effective meeting and process manager, carrying out this role in a resource-efficient manner. As the workgroup chair role is also about building trust and confidence amongst code parties and other stakeholders, a code administrator chairing a workgroup should declare any conflict of interest and an alternative chair should be appointed. For example, a proposer or proposer representative should not take up the workgroup chair role.

4.119. Our **Final Proposals** are for existing governance arrangements to provide for workgroup chairs that are independent (i.e. impartial). Code administrators should carry out this role unless there is a clear conflict of interest, for example, the code administrator is affected by the outcome of the modification under discussion. An appropriate replacement should take the workgroup chair role in that case. The workgroup chair's role is to facilitate an effective process with workgroup members providing expertise. We expect all code administrators to undertake the workgroup chair role in a resource-efficient manner.

Other issues

Initial Proposals

4.120. In our Initial Proposals we also set out that we had identified two relatively minor or 'housekeeping' issues that we proposed to address as part of this review.

4.121. The first issue related to the code objective, contained in some form in the majority of the codes and licence conditions, which refers to efficiency in code administration. For example, BSC objective (d) is "promoting efficiency in the implementation and administration of the balancing and settlement arrangements described in paragraph 2"[25] and DCUSA objective (d) in the licence is "the promotion of efficiency in the implementation and administration of the DCUSA arrangements".[26] This type of objective supports progression of housekeeping modifications and modifications related to code administration. Currently, there is no similar code administration efficiency objective in the CUSC (both the main code objectives and the charging objectives), the DCUSA charging objectives, the Distribution Code objectives and the Grid Code objectives. We proposed including such an objective for these codes.

4.122. The second issue related to the applicable objectives of the BSC, CUSC and STC. The licence condition for each of these codes indicates that the 'applicable objectives' in relation to proposed modifications to the modification procedures themselves are those provisions in the relevant licence condition which set out what the modification procedures should contain (for example, in relation to the BSC, paragraph 4 of SLC C3 of the electricity transmission licence). This approach does not apply to other codes, and we noted that, in practice, industry assesses all modifications against the same set of applicable objectives for that code, whether they seek to modify the modification procedures or other parts of the code. We considered this is appropriate, and proposed amending the definition of applicable objectives for the BSC, CUSC and STC to remove reference to the licence provision relating to the scope of the modification procedures.

Responses to our Initial Proposals

4.123. Just over half of respondents commented on these proposals, all of whom agreed with them.

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[25] SLC C3.3(d) of the electricity transmission licence.
[26] SLC 22.2(d) of the electricity distribution licence.

Final Proposals

4.124. Our **Final Proposals** are to implement the changes as set out in our Initial Proposals. In addition to these housekeeping changes, we are also proposing to make a small number of other minor typographical changes. The details of these changes and the draft legal text required to implement all of these minor housekeeping changes is set out in the accompanying document: Code Governance Review (Phase 3) Final Proposals - consultation on licence modifications.

5. Charging methodologies

Chapter Summary

This chapter discusses a broad range of issues related to the governance of charging methodologies. It summarises respondents' views to our Initial Proposals and sets out our Final Proposals on ways that the existing modification processes in respect of charging methodologies can be made more robust with the aim of delivering more effective and efficient outcomes.

Pre-modification process

Initial Proposals

5.1.   In our Initial Proposals, we considered that there could be benefits in all 'material'[27] charging modifications going through a pre-modifications process prior to being formally raised. The benefit of this approach would be that there is some initial evidence against the relevant charging objectives for proceeding formally with a charging modification. Early discussion through a pre-modification process with other industry participants can give early sight of an issue to interested stakeholders, help in the development of a charging modification with wider input before its formal submission, and thereby improve the efficiency and timeliness of the formal process as a result. Charging modifications which cannot demonstrate some early assessment could be sent back by the relevant panel to be developed further prior to returning to the formal process.

5.2.   We considered that the proposal form for each charging modification should record what pre-modification assessment was undertaken, any outcomes of that assessment, and how the modification formally raised as a result may better facilitate the relevant charging objectives of the code. It would not dilute the principle of proposer ownership which applies from when a modification is formally raised. Instead, it would enhance this principle, as the proposer can show it has used the pre-modifications process to debate the issue and has established some robust evidence for taking forward a modification.

5.3.   We also noted that the CACoP provides (Principle 5) for active support, by code administrators, of access to the use of pre-modification processes so that industry can be encouraged to debate and develop solutions. Also, the CACoP provides (Principle 6)

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[27] In this context, 'material' can be determined in line with any guidance developed in respect of the use of the self-governance route and whether Authority consent is required for a modification – see paragraph 5.22 below.

for proposer ownership to apply to modifications that are formally raised so that the proposer can retain control of its solution.

5.4.   We did not see a conflict in the practical application of these two principles. Instead, for charging modifications, they should complement one another to ensure:

- a proposer of a potential modification has confidence in the pre-modifications process (the charging methodologies forums) to debate and develop its idea, and then

- the proposer is able, if appropriate, to formally raise a proposal, which has been robustly developed and over which it retains ownership.

Responses to our Initial Proposals

5.5.   A majority of respondents supported the use of pre-modification processes for 'material' charging modifications except in certain circumstances, e.g. urgent modifications. Some of these respondents saw the benefit of discussing ideas or issues through a pre-modifications process prior to submission of charging modifications into the formal process. One respondent highlighted a recent UNC modification,[28] which aims to embed use of a pre-modification process into UNC governance to improve the overall efficiency of the modifications process.

5.6.   Other respondents did not support a mandatory pre-modification process for 'material' charging modifications, which they saw as running counter to open governance and the principle of proposer ownership. Some respondents wanted greater clarity about what is 'material'. Some respondents also highlighted that existing pre-modification processes for charging issues already work well for the relevant codes and saw no benefit in a 'mandated' step for charging modifications. Some respondents also identified a mandatory pre-modifications process as a resource issue for small parties and noted that the current pre-modifications processes are not accessible to some parties.

Final Proposals

5.7.   We welcome the strong support for the use of pre-modification processes (charging forums), which can help produce well-developed modification proposals for submission to the formal process. We also note the views of those respondents who

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[28] UNC 566S (UNC Modification Stakeholder Engagement and Guidelines) gives more guidance to proposers about the process to be followed for all new UNC proposals, allowing more scrutiny by the UNC code administrator (Joint Office) as a Critical Friend and the UNC panel at the time a proposal is raised. If a proposal is under-developed, the panel may send it to a pre-modification process for discussion. UNC566S was implemented on 12 February 2016.

considered that the use of pre-modification processes should not be mandatory, and that flexible use should be made of these forums, for example, so that urgent modifications can be raised directly to the formal process. We agree that proposer ownership should be retained for all proposals. However, our view is that more effective use of charging forums can be made where issues are raised which need clearer definition, so that this results in a well-developed modification spending less time in the formal process. Potential proposers of charging modifications could therefore find the pre-modification process provides a more effective avenue for defining an issue as a modification prior to formal submission.

5.8.   The role of code administrators as Critical Friends to code parties is important in delivering effective governance in this area. In each code incorporating charging methodologies (CUSC, UNC, and DCUSA),[29] the code administrator is able to reject a proposal at the outset on the grounds that it insufficiently defines the issue or defect it seeks to address or that the proposed solution is not well-defined. However, the code administrator, as a Critical Friend, can also play a positive role in providing assistance to smaller parties and others in drafting modification proposals before they are formally raised. The code administrator could, in carrying out this part of its role, refer the proposer to a charging forum where appropriate. The panel may also have a role in directing proposals to a pre-modification process. Further, the Authority may informally have concerns around a proposal before it is formally submitted, which could result in a referral to, or further discussion at, a charging forum. The recent modification to the UNC suggests there is scope to define referrals to charging forums in codes through the introduction of appropriate guidance.

5.9.   Our **Final Proposals** are therefore not to mandate the pre-modification process for 'material' charging modifications. However, code parties, code administrators (as Critical Friends) and code panels should make more effective use of the existing pre-modification processes to enable well-defined charging modification proposals to be developed and then raised in the formal process. The operation of a more effective process should not impact either proposer ownership or the progress of timely urgent modifications. We expect that the recent introduction of guidance on when to refer matters to pre-modification processes in the UNC should be explored for the other codes which incorporate charging methodologies. In particular, that the relevant code administrators should work with industry/relevant charging forums as appropriate to consider this for the other codes, and develop appropriate code modifications where relevant. We consider that this should result in the current processes delivering more effective and timely changes that benefit consumers and competition.

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[29] We would also note that there is a charging methodology in the SEC and, therefore, going forward, the issues discussed in this chapter and our Final Proposals will also apply in principle to the SEC.

Development of a forward work plan by panels for charging modifications

Initial Proposals

5.10. In our Initial Proposals, we considered that a more strategic approach to how panels plan and manage modification processes could be particularly beneficial for charging modifications. In particular, that certain charging 'priority' area(s) could be agreed each year and charging modifications that deliver in the priority area(s) would be the subject of a panel forward work plan. There would be an expectation, therefore, that, except for more complex modifications, these charging modifications would be developed and ready for decision for implementation on the specific date.

5.11. We noted that this approach would concentrate both industry and Ofgem resource over a specific period of time, but an effective plan and timetabling of modifications could provide more focus and efficient use of resources. We considered that panels, working alongside industry, code administrators and ourselves, are well placed to develop and execute effective forward work plans that deliver in significant priority areas with timely and real benefits for, amongst other things, consumers and competition. We considered that it would be appropriate for these plans to include charging modifications and that the existing processes are capable of being adapted to achieve these aims.

Responses to our Initial Proposals

5.12. There was majority support from respondents for panels to develop forward work plans with assistance from code administrators and Ofgem. Those in support noted that development of a forward work plan would help industry, panels and Ofgem to better plan the use of their collective resources. Some respondents also saw benefits if there was forward planning for all modifications, not just charging modifications. One respondent suggested that these plans are developed across all codes and then amalgamated. One respondent highlighted the annual review of charging methodologies, as obligated by licence, as an appropriate opportunity for code panels to initiate and then deliver a strategic forward work plan. Industry workgroups would work to the priorities in the work plan to deliver relevant charging modifications.

5.13. A number of concerns were raised about adopting a more active planning approach. Some respondents disagreed with mandating a forward work plan. They also questioned whether parties would be allowed to raise modifications outside of the agreed priorities and work plan which they saw as stifling open governance and proposer ownership. Some respondents sought clarity on who would decide on plan priorities. Other respondents did not consider that panels were best placed to decide priorities when industry (through workgroups) is responsible for resourcing the modifications process and that workgroups would need to be involved in planning. One

respondent considered that panels are reactive and so their role may need reassessment if it is to become a more pro-active one.

Final Proposals

5.14. We welcome the support of respondents for panels to develop work plans aided by industry and Ofgem for changes to charging methodologies and other code change where appropriate. We consider that this approach would assist in better planning and use of resources by industry, code administrators and Ofgem in order to deliver effective, efficient and timely outcomes for consumers and competition. As set out in the previous chapter, we consider that code panels would be assisted by code administrators in developing their strategic plans by identifying priorities from a variety of sources. For example, input could be provided from industry directly and through charging forums where industry can raise issues and have these better defined for inclusion in the forward work plan. Ofgem's published Forward Work Plan together with, in the future, the strategic work plan that the CMA has proposed Ofgem should develop should also highlight broader initiatives on charging for inclusion in a work plan.

5.15. We note some concerns about whether this approach would allow for the raising of non-priority charging modifications outside of the work plan. We do not consider that a work plan is inconsistent with flexibility in the modifications process that allows, for example, progress of less 'material' modifications at the same time. We are not proposing at this time to mandate that code panels develop forward work plans though industry may wish to consider if any code change may be required to support effective delivery of plans. We expect effective communication between code administrators and code panels so that panels can more proactively identify and deliver modifications to an appropriate plan. We will monitor progress on how effectively this is delivered on an ongoing basis.

5.16. Our **Final Proposals** are for individual code administrators, with support from their respective code panels, to initiate work to explore how to develop an effective forward work plan for charging methodology changes for their code (and subject to the CMA's final decision), which would incorporate input from Ofgem, in respect of developing a strategic view, and industry as appropriate. We consider that the existing code processes are sufficiently robust to allow code administrators to begin taking a pro-active approach to planning by undertaking this work. Where cross-code coordination across charging methodologies is appropriate, we would expect the individual code administrators to consider how to work together effectively in a coordinated fashion. We see a number of potential benefits to this approach involving the efficient delivery of code changes on behalf of consumers.

Use of the self-governance route for charging modifications

Initial Proposals

5.17. In our Initial Proposals, we put forward our view that the proposals that we set out in respect of self-governance for other modifications could also apply to charging modifications. We noted that we would keep a definition of 'material changes' in relation to charges under review. We noted that guidance or an initial assessment of why Authority consent is needed for a modification, including for a charging modification, could enable some charging modifications to proceed through the self-governance route too, freeing up resources for consideration of 'material' modifications in line with established priorities.

Responses to our Initial Proposals

5.18. There was strong support from respondents that use of the self-governance route for charging modifications is appropriate in principle. Some respondents were strongly in favour, indicating that all charging modifications could potentially follow this route with the Authority 'calling-in' individual charging modifications with a 'material' impact. A number of respondents, while supportive, sought clarity on the definition of 'material' in line with the self-governance criteria. Those respondents not in favour considered that all charging modifications are 'material' to some extent and so unsuited to the self-governance route. Some of these respondents also noted that charging modifications with 'mass market' impact should always be considered 'material' and therefore not follow the self-governance route. One respondent noted that self-governance may not be appropriate as the licence requires the charging methodologies to be approved by the Authority.

Final Proposals

5.19. We welcome the support of most respondents for use of the self-governance route for non-material charging modifications. We consider that there are charging modifications which can follow this route when judged against the existing self-governance criteria.[30] If there are charging modifications that do meet the relevant criteria, then there is scope for panels/parties (as appropriate to the code concerned) to decide on these changes, freeing up resources to concentrate on 'material' modifications.

5.20. In Chapter 3 of this document, we set out our further thinking on the use of the self-governance route and the need for code panels to positively assess modification

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[30] CMP248 (Enabling capital contributions for transmission connection assets during commercial operation) is a recent example of a charging modification which, it was agreed, met the self-governance criteria. The CUSC modifications panel made its decision on CMP248 on 29 January 2016.

proposals for their materiality. We have also highlighted there the further work on producing guidance on defining 'material' that we expect to be undertaken. This work should help to address some respondents' concerns about the definition of 'material'. We note the concerns of some respondents that 'mass market' impact charging modifications will always be material. However, a positive identification of materiality, coupled with the Authority's ability to 'call-in' a modification where the self-governance route is no longer appropriate, can act as effective checks and balances to the use of the self-governance route. In practice, when a modification is identified as being self-governance, the Authority could direct that a charging modification should not follow the self-governance route, i.e. the Authority will decide on the modification. The Authority could also make its own separate determination that the charging modification does meet the self-governance criteria and should follow the self-governance route.

5.21.   We note that the licence requires the Authority to approve charging methodologies. The licence also provides for the change process for the methodology to be set out in the relevant code and for changes to these methodologies to be managed through open governance under the relevant code. We consider that for charging methodology changes, like other code changes, this includes the use of a self-governance route for non-material changes, with a role for the Authority to step in and actively make decisions if we consider it appropriate to do so. This should ensure licensees continue to have in place an appropriately approved methodology.

5.22.   Our **Final Proposal** is for the principle we set out in Chapter 3 – that a modification should be assessed as to whether it requires Authority consent, i.e. why **it is** material – to extend to charging modifications. In reaching that assessment, code panels should have regard to the existing self-governance criteria and also to any guidance produced on materiality.

Specific proposals for DCUSA charging

Initial Proposals

Information about pre-modifications processes to be less fragmented

5.23.   In our Initial Proposals, we considered that it may be appropriate that information about the various charging methodologies forums (DCMF, DCMF MIG and COG)[31] should be brought under DCUSA governance and administered by a single party to provide a 'one-stop shop' for information about charging issues (and non-charging issues) and to improve the consistency of processes. We noted that ensuring that all relevant documentation is managed through a single website should provide

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[31] The DCMF is the Distribution Charging Methodologies Forum. The DCMF MIG is the DCMF Methodologies Issues Group. The COG is the Commercial Operations Group.

ease of access for interested stakeholders and could help to address concerns about the lack of engagement by some affected parties. It could also assist in ensuring that a more effective 'joined up' pre-modifications process develops for DCUSA.

Each charging methodologies forum (DCMF, DCMF MIG and COG) to have a DCUSA panel sponsor

5.24.   In our Initial Proposals, we noted that currently there is no formal connection between the DCUSA panel which oversees the process for formal charging modifications and the pre-modifications processes through which these modifications should be initially developed. We considered that by having a panel sponsor who reports back to the panel each month on the issues discussed at the DCMF, the DCMF MIG and the COG, the panel would better understand the origins of charging modifications and the panel would be more accountable for, and engaged with, efficiently progressing them. Together with the panel playing a more direct role in managing forward planning for charging modifications, our view was that this approach should develop and maintain a firm link between the DCUSA panel which is responsible for DCUSA governance and the charging methodologies forums tasked with initially assessing charging issues and potential modifications.[32] Panel members could take up a 'sponsor' role on the various charging methodologies forums without any significant change to existing arrangements, e.g. the forum's Terms of Reference may in certain cases be amended to facilitate this.

Responses to our Initial Proposals

Information about pre-modifications processes to be less fragmented

5.25.   There was strong majority support for bringing DCUSA pre-modification forums (specifically the DCMF and DCMF MIG) under DCUSA governance and publishing related information on the DCUSA website. Some respondents in support did not consider bringing the COG under DCUSA governance as appropriate as it is an ENA-run group paid for by DNOs and not by the wider industry. Some respondents supported our proposal but queried whether bringing all pre-modification information into one place would necessarily improve stakeholder engagement. These same respondents considered that charging methodologies are complex and wanted simpler methodologies to assist all parties to understand them.

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[32] Parallels can be drawn with the BSC, where individual BSC Panel members sponsor and attend panel sub-committees.

Each charging methodologies forum (DCMF, DCMF MIG and COG) to have a DCUSA panel sponsor

5.26.   There was a split in views on this proposal. Those in favour considered that having a panel sponsor increases accountability and panel knowledge of charging issues under discussion. One respondent suggested the panel sponsor could attend as an observer only, to develop knowledge about charging issues but not take part in discussions. Those respondents against the proposal highlighted that panel members may lack knowledge and so their sponsor role would be of limited use. Other respondents suggested possible alternatives to the panel sponsor role, e.g. for the chair of the pre-modifications forum to attend the panel and report, or increased resourcing of the pre-modifications process to increase knowledge instead.

Final Proposals

Information about pre-modifications processes to be less fragmented

5.27.   We welcome the strong support from respondents for bringing the DCMF and DCMF MIG under DCUSA governance[33] and also to publish related information from these charging forums in a 'one-stop shop' on the DCUSA website. We consider that it should improve both (i) the transparency of discussions on charging methodologies and potential modifications, and (ii) access to relevant papers for users who may wish to use these forums to discuss issues or attend them for information. One simple and cost-effective way to facilitate publication is for the DCUSA website to carry links to the relevant information currently published on the ENA website so that it is more immediately accessible to stakeholders. As a next step, we would encourage the relevant parties to explore how to bring the DCMF and DCMF MIG under DCUSA governance to align with the DCUSA Standing Issues Group (SIG) which currently falls under DCUSA governance.

5.28.   While we recognise that there are different funding arrangements for the COG and that the DNOs are the main participants, the COG Terms of Reference make clear that the DCUSA and relevant charging methodologies (the CDCM and the EDCM) are within scope of COG discussions.[34] Therefore, we consider that, as a minimum, a link to published papers from the COG on the DCUSA website would also increase transparency and improve users' knowledge and understanding of the DNOs' thinking in these specific areas. We would also encourage DNOs to consider how best in future to ensure that COG and related forum papers can be made accessible to all parties

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[33] Currently, DCMF and DCMF MIG papers appear on the Energy Networks Association (ENA) website only: http://www.energynetworks.org/electricity/regulation/distribution-charging/distribution-charging-working-groups.html.
[34] COG and COG Connections Charging Methodology Forum (CCMF) papers also only appear on the ENA website: http://www.energynetworks.org/electricity/regulation/working-groups.html.

who wish to engage on charging issues through this forum and its suitability for inclusion under DCUSA governance.

5.29. We note that there were some concerns about how holding information about these charging forums in one place would necessarily improve stakeholder engagement. We consider this to be one element of a more pro-active Critical Friend role for the DCUSA code administrator to assist stakeholders, in particular small parties and consumer representatives, with accessing resources and understanding more about the charging methodologies. We note that there are concerns about the complexity of the charging methodologies which may create a barrier to engagement. We recognise that by their nature, charging methodologies can be complex. One simple step towards addressing this problem is to allow parties to find the right information in one place as a way to increase understanding of the methodologies. However, we also recognise that code administrators will not in all cases themselves have detailed, technical understanding of the charging methodologies. As noted under our first Code Governance Review[35], we therefore expect relevant licensees to play an active role. We note this could include, for example, assisting parties to understand the charging methodologies and the impacts on parties' charges, providing guidance and plain English explanations as appropriate.

5.30. Our **Final Proposals** are that all relevant papers for the DCMF, the DCMF MIG and the COG currently published on the ENA website should be accessible on the DCUSA website through appropriate document links which are prominent and visible to those parties who access the DCUSA website. This would act as a first step towards providing greater access to understanding what these charging forums do, so that all parties, but particularly those who currently do not engage, can make more effective use of them. We will continue to monitor progress so that DCUSA governance is strengthened as appropriate.

Each charging methodologies forum (DCMF, DCMF MIG and COG) to have a DCUSA panel sponsor

5.31. We note that respondents' views were split on our proposal. We consider that DCUSA panel members could benefit from carrying out a sponsor role for each of the charging forums by building increased knowledge of charging issues. This in turn would increase their accountability for the progress of those charging issues when they become charging modifications. We note some alternatives to panel sponsors were suggested. One suggestion was that the chairs of the charging forums report directly to the DCUSA panel on a regular basis, as the code administrator currently does for the DCUSA SIG. Another suggestion was to increase resourcing for the charging forums. While the latter suggestion would increase costs without clarity on who would pay, the former is potentially viable and low-cost and could complement

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[35] See Chapter 3, paragraph 3.12 of our March 2010 Code Governance Review Final Proposals:
https://www.ofgem.gov.uk/sites/default/files/docs/2010/03/cgr_finalproposals_310310_0.pdf

panel sponsorship. We consider that panel sponsorship provides a more direct opportunity to DCUSA panel members to participate in, and increase their knowledge of, charging issues, which would ultimately benefit panel decision-making on how charging modifications progress.

5.32. We consider that panel sponsorship is one way in which there can be increased understanding of the work of charging forums and the issues discussed there which may, over time, become charging modifications. We note that panel sponsorship will address concerns about panel members' lack of knowledge – which they should build up over a period of time – and ensure that panel members are generally more accountable for their role in respect of modifications business where charging modifications are concerned. We note that panel sponsorship could be complemented by charging forum chairs attending and reporting to DCUSA panel periodically on their business. This would also build panel members' knowledge about charging issues and help in how they plan for future charging modifications.

5.33. Our **Final Proposal** is therefore that appropriate mechanisms are explored by the DCUSA panel under current DCUSA governance arrangements to allocate panel members as panel sponsors to each of the existing charging forums (DCMF, DCMF MIG and COG).

Appendices

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Appendix 1 – Updated draft SCR Guidance

This Appendix sets out draft, indicative guidance on the SCR process. Subject to us making the proposed licence modifications we are currently consulting on, we currently expect this guidance will replace our existing published SCR guidance.

Introduction

The Significant Code Review (SCR) process provides a tool for Ofgem to initiate wide ranging and holistic change and to implement reform to a code based issue. This guidance sets out the steps in our process for launching and conducting SCRs and replaces the existing guidance in light of the revised process to result from the Code Governance Review (Phase 3) (CGR3).

This document is intended to provide guidance to interested parties on how an SCR would be conducted. It is intended to illustrate the steps and stages we would expect to follow when undertaking the SCR process. However, there may be instances where the process may need to deviate from that set out in this guidance.

Drivers for an SCR

We would consider whether to launch an SCR in response to various events including, for example, developments in EU law, a Government-led policy, or an internal work stream, in addition to stakeholder-made representations or code modifications that are proposed by industry.

An SCR may be appropriate where the solution to the issues raised would be given effect through code changes. We would consider whether the issues are significant in relation to our principal objective and/or our statutory duties and functions, or the result of obligations arising under EU law. In particular, we would consider if the issue may have significant impact on gas and electricity consumers or competition, and/or may be likely to have significant impact on the environment, sustainable development or security of supply and where the area of work is likely to create cross-code or cross code-licence issues.

The SCR process

Forward Work Programme

We produce an annual Forward Work Programme, which details our main themes and priorities for the coming year.[36] The Programme provides information on the work to be undertaken to support the main themes and priorities as well as financial data and information on our planned deliverables and performance indicators for the year

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[36] https://www.ofgem.gov.uk/about-us/corporate-policy-planning-and-reporting/corporate-strategy-and-planning

ahead. Where possible, we would expect that any SCRs that we were considering undertaking would be highlighted in our Forward Work Programme.

Consulting on undertaking an SCR

We would consult before deciding on whether to undertake an SCR. We would expect the consultation to set out our views on the need for an SCR; the proposed scope and scale of the work including, where possible, an estimate of the time and cost implications; and the reasons why we consider that an SCR is the most appropriate mechanism to take forward the area of work. We would also expect to consult on which of the SCR process options (as set out in the diagram at the end of this document) we would expect to follow.

Launching an SCR

We will consider the responses to the consultation before deciding on whether or not to launch an SCR. Reasons for us not to proceed may include (but would not be limited to):   other priorities being identified; that the work could be progressed through other code governance processes; or deciding the area of work may be unsuitable for an SCR as the solution lies outside of the industry codes. We would publish any decision not to proceed with an SCR and the reasons for it.

If we were to proceed, we would publish a statement on our website (the launch statement), and would also aim to highlight this to the code panels that we expect to have an interest in the SCR. The statement is likely to include (taking into account the responses to our consultation): the scope of the SCR; the process option to be followed; the reasons for launching and for carrying out the SCR rather than an alternative action; and, where possible, an initial estimate of the time and cost implications for both Ofgem and industry. It should be recognised that the information set out in this statement may change as the SCR process is followed.

Once an SCR has been launched, new modification proposals, which cover similar ground to the SCR may not proceed through the standard industry modification process. Only urgent proposals or those specifically exempted by us will be allowed to proceed through the code modification process.

Criteria for choosing the SCR process options

As a result of CGR3, there are now different process options that an SCR can follow (plus the ability to move between certain options). These are set out in the diagram at the end of this document and can be described as follows:

1. **Ofgem directs licensee(s) to raise modification proposal(s)**. At the end of the SCR process we would issue a direction to the relevant licensee(s). Our direction may set out high level principles (with the detail to be developed by industry) or more specific, detailed conclusions to be

given effect through code change(s). The modification(s) would follow the standard industry code modification processes.[37]

2. **Ofgem raises modification proposal(s)**. At the end of the SCR process we would raise a modification(s) under the relevant code(s), and the modification(s) would follow the standard industry code modification processes.

3. **Ofgem leads an end-to-end process to develop code modification(s).** The standard industry process would not apply; Ofgem would lead consultation and engagement needed to develop the appropriate code change(s). We would expect close involvement of the industry; for example, we may establish and lead workgroups similar to the approach under the standard code modification processes (but led by us).

As noted above, we would first expect to consult on which of these options we would follow prior to launching the SCR; however, the process option chosen initially may change as the SCR progresses. This could include taking over the drafting of the modification proposal(s) if we have previously directed a licensee to raise a modification(s).

The criteria that we would expect to consider when making a decision on which option to follow are likely to include:

- Whether the issues affect a single or multiple codes, and whether a higher level of co-ordination is required as a result of there being complex cross-code issues.

- Incentives for industry to participate in particular issues and whether these may be misaligned with outcomes in the best interests of consumers.

- Timing and implementation issues that could potentially influence the outcome of policy conclusions or facilitate a more efficient end-to-end process and avoid potential duplication under two separate processes.

Setting the Timetable

As noted above, we would expect to include an indication of the time we anticipate it will take to complete the SCR process. Such a timetable will, inevitably, be subject to change and will be determined as a result of consultation with all interested parties.

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[37] Including, for example, establishing workgroups to develop and assess proposed change, and providing for alternatives to be raised if appropriate.

Depending on which option the SCR follows, we may at a later stage also consider the benefits of directing the timetables for the development of code modifications, in cases where the SCR process relies on a direction to a licensee (or to licensees) to raise changes under the normal industry change processes. Again, we would expect to consult prior to directing such a timetable.

Communication and Consultation

We would expect all communications in respect of the SCR to be fully inclusive and seek to ensure that all parties that may be affected are fully aware of developments as the SCR progresses.

Depending on the scale and length of the SCR we would expect to undertake a number of written consultations setting out the issues and our thinking on how to tackle those issues through code changes.[38] We may also undertake consultations on specific aspects of complex issues, to allow interested stakeholders to provide views.

Regardless of the SCR process being followed, including where we develop code modifications, we expect there to be close involvement from code administrators, code owners, affected licensees and code parties. This will enable all parties to undertake analysis and to consider all possible implementation solutions in detail.

This could also be achieved through working groups established by Ofgem and which could be designed effectively to mirror the working arrangements used by code panels as part of the established code modification process.

If the chosen option of the SCR is an Ofgem led end-to-end process, we would expect that all realistic/viable options for achieving the required outcomes would be the subject of consultation prior to the conclusion of the SCR process.

Completion of the SCR phase

The steps that we would expect to take at the completion of the SCR phase are dependent on which of the options has been followed.

- Under the option for us to direct a licensee to raise code modification(s): at the end of the SCR phase we would expect to issue an SCR conclusions document. If we consider that code changes are required, we would expect to issue SCR Direction(s) to the relevant licensee(s), within our SCR conclusions document (or in a separately published document within 28 days of our conclusions). The SCR Direction(s) will set out the code matters to be addressed by the licensee(s) that should form the basis of modification proposal(s).

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[38] We would also consider whether we should undertake an Impact Assessment in line with our statutory duties under section 5A of the Energy Act.

- Under the option for us to raise modification proposal(s): at the end of the SCR phase we would expect to issue an SCR conclusions document. We would expect to raise any modification(s) following publication of our SCR conclusions document. This modification proposal(s) would then follow the standard industry process.
- Under the option where we lead an end-end process: we would expect that a modification proposal would have been developed and been presented to the relevant Panel(s) during the SCR process. The SCR process would end when the Authority makes a decision on any modification proposal.

An SCR process could be completed without a modification proposal being taken forward if, for example, it were felt that the issue being addressed could be better resolved through alternative measures.
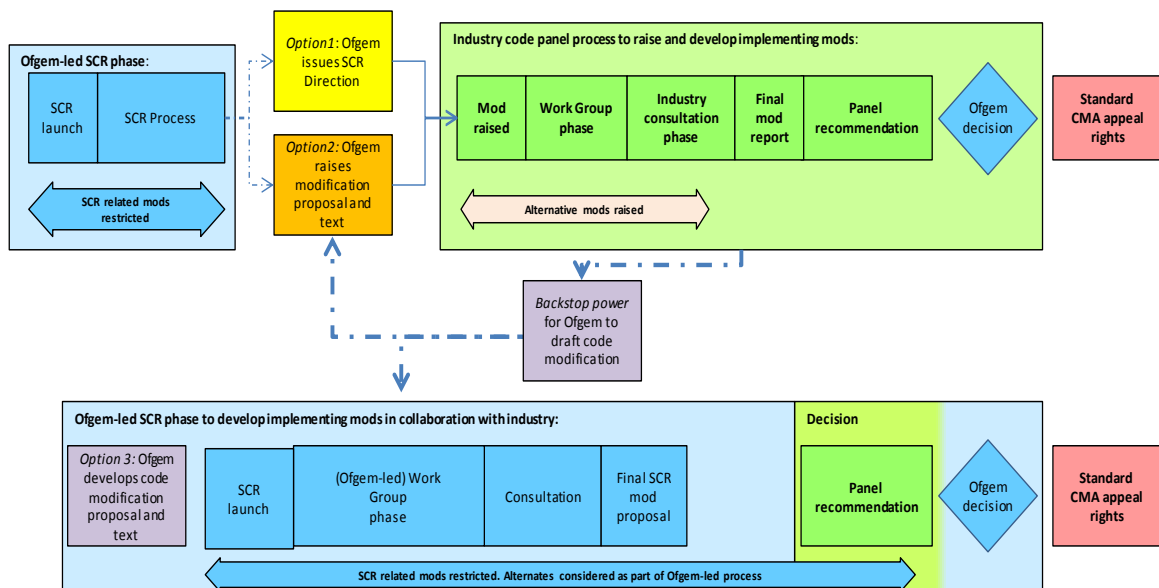
Appendix 2 - Glossary

B

BSC

Balancing and Settlement Code.

C

CACoP

Code Administration Code of Practice.

CGR

Code Governance Review.

CGR2

Code Governance Review phase 2.

CGR3

Code Governance Review phase 3.

Code Governance Review

Ofgem led review of industry code governance, the first phase of which concluded in 2010.

CUSC

Connection and Use of System Code.

D

DCUSA

Distribution Connection and Use of System Agreement.

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.

I

iGT UNC

Independent Gas Transporters' Uniform Network Code.

M

MRA

Master Registration Agreement.

S

SCR

Significant Code Review.

SLC

Standard Licence Condition.

SPAA

Supply Point Administration Agreement.

STC

System Operator – Transmission Owner Code.

U

UNC

Uniform Network Code.

Appendix 3 - Feedback Questionnaire

1.1. 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?

1.2. Please send your comments to:

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