

Laura Nell
Ofgem
9 Millbank
Westminster
London
SW1P 3GE

Mr Chris Bennett
Director of Regulation

www.nationalgrid.com

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Dear Laura,

Thank you for the opportunity to respond to your consultation on the implementation of the CMA recommendations in respect of industry code governance. This response is provided on behalf of National Grid Electricity Transmission plc ('NGET') and National Grid Gas Transmission ('NGGT'). NGET owns the electricity transmission system in England and Wales and is the National Electricity Transmission System Operator (NETSO). It is responsible for administering the electricity Connection and Use of System Code (CUSEC), the Grid Code and the System Operator – Transmission Owner Code (STC). NGGT owns and operates the gas Transmission System and, in association with the gas Distribution Network Operators, also jointly provides for the administration of the Uniform Network Code (UNC) Governance arrangements through the Joint Office of Gas Transporters (JO).

We are supportive of the remedies outlined in the consultation. We believe that enhancing and standardising the delivery of market change through codes, whilst bringing the consumer to the heart of any strategic code direction, is paramount. We consider that further clarity needs to be provided on the role, composition and objective of the Consultative Board, how the Strategic Direction will be developed (and by whom) and how this interacts with policy-setting by Government. In establishing any new entities, it is essential that the role and functions of are clearly set out and distinguished from those of other existing bodies.

As the System Operator (SO) for both Gas and Electricity Transmission Networks in Great Britain, our unique experience, expertise and whole-system view puts us in a strong position to enable consumer benefits from the transformation of the energy system into one that is smart and more flexible. Your recent consultation on the future role of the Electricity System Operator (ESO) highlights the role the ESO can play, as a leading industry voice, to actively engage in identifying and proposing changes to code arrangements, as well as interacting with stakeholders to bring forward pro-competitive proposals to industry codes. We are firmly of the view that we should be engaged to further develop and clearly delineate the roles of you and the SO in developing and implementing the Strategic Direction and other aspects of the proposed reforms.

From an NGGT perspective we would reflect that a number of Code Manager and Code Delivery functions are currently delivered by distinct entities (the Joint Office of Gas Transporters providing UNC administration services as described above) and Xoserve (providing 'Delivery Body' services in

respect of central systems). On this basis, we are keen to better understand the full implications of the proposed 'licensing and competition' regime.

We discuss below some key issues we feel are critical to ensuring that industry codes facilitate the longer-term development of the market. In order to help support further understanding on these topics it would be helpful if you could provide further guidance on these as it develops and implements these reforms.

We note that the electricity codes are often considered by a number of market participants to be a barrier to entry and overly complex; we would therefore be interested in whether you consider that current arrangements are sufficiently robust for the future energy system. Reforming the electricity codes could have some advantages, such as simplicity in benchmarking performance of Code Managers, but the different funding arrangements currently in place for different Code Administrators would need to be considered alongside the consideration of the amalgamation of some codes. Finally, in developing these reforms to introduce competition for Code Manager and Code Delivery roles, we would expect that new structures or organisations are not introduced unnecessarily, at the expense of the consumer.

We consider industry codes as the operational framework for the market. They are integral to implementing the Strategic Direction which should be set in line with established policy decisions made by Government. This position contributes to our thinking and has informed our answers to your questions which are below.

Yours sincerely,

Mr Chris Bennett
Director UK Regulation.

Scope of the New Arrangements

1. Do you agree that the codes and functions we have identified (i.e. the codes within the scope of the CACoP and their associated central system delivery functions) should be within scope of the new regime?

We believe that the codes captured in the consultation document are the key codes for the respective fuels and therefore they should all be in scope of the new arrangements. However, we also acknowledge that for codes such as the iGT UNC, SPAA and SEC, if there is a significant increase in administration/delivery cost (from 'commercial' services provision perspective), these costs may be disproportionate.

2. Are there any other codes or systems that should be within scope and if so please give your reasons?

We are happy with the codes and systems in scope.

As a point to note in respect of gas systems, unlike other UK Link systems (which are owned and operated by the incumbent delivery body Xoserve), the Gemini system is 100% owned by National Grid NTS (and is currently operated by Xoserve on its behalf).

3. Are there any other factors you think we should consider when making this decision?

In our view the four factors identified (2.4) cover the key elements. However, whilst being supportive of the increased licence obligation to deliver a 'Code Manager' role, introducing such a wholesale change to the way the codes are managed would mean the requirement to increase staffing amounts and capabilities. This would result in an increase in costs however it is not clear in the consultation document how these increase in costs would be addressed. We note that funding arrangements is recognised as a future task (presumably for consideration by the Licencing and Competition Work stream) and we would like to highlight the importance of ensuring sufficient and robust funding arrangements for any new roles and activities in order for these to be delivered successfully.

Licencing and Competition

1. What are your views on our proposed approach of including the code manager and delivery body function in a single licence?

In our view where codes are currently administered by a licensee, as is the case for the 'NETSO' codes highlighted in the consultation, it would be in the best interests of consumers and the industry for existing governance arrangements to continue. This would minimise cost and disruption whilst new arrangements are being put in place elsewhere. Where these codes are proposed to be subject to a tender process we support the move to independent licences. For those codes whose governance arrangements are subject to change, there may be different skill sets required for undertaking the Code Management and Code Delivery roles meaning that different parties may be best placed to undertake these roles. It may therefore be prudent to license parties separately.

Separate licences for the 'Code Manager' and 'Code Delivery' will allow for a more accurate tendering process where interested parties can bid based on their expertise, specialism and background. It is important to ensure that when implementing any licences for the codes, each code has the same incentive and ability to deliver against the Strategic Direction.

Where there are separate licences, there will need to be clear separation of responsibilities and accountabilities (eg between the Transmission System Operator and the 'Code Managers') in respect of the implementation of regulatory obligations. Further, additional clarity is required in terms of the change the 'Code Manager' would be expected to progress as compared to that expected to be initiated by National Grid or other code parties. For instance, as part of the implementation of EU Network Codes in respect of gas, necessary changes to non-Code contractual arrangements (for example, Interconnection Agreements) were delivered by National Grid.

2. What are your views on strengthening the licence of NGET to include new code management requirements rather than holding a tender to identify an appropriate code manager?

We are supportive of this approach. NGET holds the technical, commercial and analytical expertise capability across the System Operator (SO), for the codes that we administer. Retaining this role within the NGET SO would therefore enable this expertise to continue to be used and minimise cost and disruption to the industry and consumers.

3. What are your views on the identified merits and drawbacks of the four competitive tendering models for competitively licencing code management where applicable?

We agree with the stated pros and cons within the consultation document and is supportive that the administration of any tendering process should be managed and owned by you to ensure that the consumer interests are always at the forefront of decisions.

For any code which will retain the existing framework where the Code Administrator transitions to the 'Code Manager' we feel it would be prudent to maintain a permissive approach if licencing is mandated. However, for codes that will be tendered as part of the new licencing regime, we feel that a sole licencing approach would be the most cost efficient process because under the permissive licences the implication is that a number of organisations would have licence obligations 'switched off' if they are unsuccessful in the tender process. When the time came to re-tender it seems prudent that you would have to re-evaluate their suitability again which negates any benefits a permissive licence obligation could provide.

4. What are your views regarding which model(s) may be appropriate for different codes, or types of codes?

We feel that it is important not to ring-fence all codes into one tendering model. For codes that do not have Central Systems a lighter touch can be used akin to that in Model 1 as it would allow more opportunity for small codes/businesses to be actively involved in the tendering process. For codes that support large scale Central Systems and have significant commercial and system security drivers e.g. UNC, BSC and CUSC, a more complex and detailed tendering model akin to Model 3 may be more prudent to ensure that the 'Code Managers' and Delivery Bodies can effectively take on the role of developing and managing any large-scale changes.

Strategic Direction

1. Do we agree with the purpose of the Strategic Direction?

We believe that the Strategic Direction can be an important tool to implement change in a more efficient and focused manner, therefore we are supportive of this approach. Given our unique, whole-system view and the proposed extension of our electricity role as set out in your consultation on the future role of the electricity SO, we think we have a key role to play in developing the Strategic

Direction and enabling the smart, flexible energy systems of the future. We would welcome the opportunity for further discussions about the respective roles of Ofgem and the SO's¹ in developing the Strategic Direction.

As the purpose of the Strategic Direction evolves, it would be beneficial to have further clarity on the following questions:

1. What frequency does Ofgem intend to review/restate the Strategic Direction? This will need to be sufficiently frequent to take into account changing market and technological developments, without causing unnecessary uncertainty by changing too often.
2. When Code Modifications have no link to the Strategic Direction (raised by industry as part of standard Governance processes) how will these modifications be progressed? Will they be prioritised in line with required changes to meet the Strategic Direction?
3. With the UK increasingly interconnected with the EU stakeholders, how wide does engagement need to be to decide on the GB priorities?
4. Are timelines to be provided within the Strategic Direction for Codes Panels and 'Code Managers'?

2. Do you have any views on how the Strategic Direction should be developed and implemented?

We believe it is important that the Strategic Direction is developed taking into account factors such as policy decisions, investment drivers and technological developments. We analyse and publish a large amount of information on potential developments in the energy market, much of it developed with the industry through a thorough stakeholder engagement process. This includes our annual Future Energy Scenarios (FES), a holistic view of the UK's changing energy landscapes. Additionally, the Electricity Ten Year Statement (ETYS) and the Gas Ten Year Statements (GTYS) illustrate potential future developments to the transmission systems, and the System Operability Framework (SOF) provides a view on how the changing energy landscapes described in FES could affect future system operability. We welcome the chance to discuss with you how these insights could help shape the Strategic Direction.

Regime changes progressed under current arrangements may not always have the consumer benefits as a primary consideration, thus consumer interests should carry greater weight in regime development. The Strategic Direction should also recognise that Gas and Electricity markets may have different challenges and therefore may need different areas of focus or different high level solutions.

Furthermore, when developing the Strategic Direction it is important that industry is consulted to ensure support at all stages of implementation. In order to achieve this it is important that pre-engagement with industry is carried out not only to inform, but also to enrich and increase the quality of the direction.

However, further clarity is required on how the Strategic Direction will be delivered, where the Consultative Board sits in the delivery of the Strategic Direction and how these will both interact with the Panels and relevant codes. We note in the consultation document that you see the implementation of Electricity EU Network codes in GB as a project likely to benefit from the introduction of the Strategic Direction and Consultative Board. Considering that the deadline from implementing the EU Network codes is approaching (Requirements for Generators Spring 2018), we would welcome any

¹ The scope of the SO refers to both Gas and Electricity SO's.

thoughts/seek to understand if you may have thoughts on accelerating the introduction of the Strategic Direction to meet this requirement.

We welcome the opportunity to work with you to shape the Strategic Direction to enable consumer benefits from the transformation to smarter, more flexible energy systems.

3. How much detail do you consider should be included in the Strategic Direction?

We believe that sufficient detail is required in the Strategic Direction in order to enable the Consultative Board to compile a joint industry plan. It is also important that the level of detail is sufficient to allow industry parties to conclude if any proposals they are considering are consistent with the Strategic Direction. To ensure industry buy in, it is important the Strategic Direction affords enough flexibility in implementation so that codes and industry have the ability to deliver innovative solutions that are in the best interests of the consumer.

4. Which specific projects do you consider should be included in the initial Strategic Direction?

NGET feels that Electricity codes are currently undergoing an unprecedented level of change, so in line with the code Forward Workplans NGET feels it is important to focus on areas which our stakeholders highlight as the biggest concerns:

1. Implementation of the Electricity EU Network codes;
2. A review of the Charging Arrangements: Embedded Benefits, facilitation of Storage and Flexibility;
3. Faster, more reliable switching;
4. A move toward half-hourly settlement for profile classes 1-4 and;
5. Extending Competition in Electricity Transmission (ECIT Project).

We believe that the existing code Forward Workplan co-ordinated by the existing Code Administrators would appear to provide a useful starting point regarding the expected material changes to market arrangements.

Consultative Board

1. What do you see as the core role and functions of the Consultative Board?

We believe that the Consultative Board is an important body in facilitating, co-ordinating and providing accountability for delivering the strategic direction, cross-code development and championing the consumer through the relevant code panels. As part of this it is important that it maps out the priorities of how the Strategic Direction will go from inception to implementation.

It is important that the Consultative Board has the correct industry participation, powers and support to ensure its success. We believe it is important for the board to consist of those parties who will be tasked with delivering any strategic direction/wider industry changes, and that the scope needs to be clearly defined to avoid any duplication of activities with other industry bodies. This should include the requirement to ensure efficient and effective cross-code co-ordination of any widespread industry change.

Finally, the interaction between the Panels and the Consultative Board needs to be considered and clarified including how any disputes between industry bodies are resolved.

Moving to new arrangements

1. What are the main impacts of the proposed new arrangements on existing projects?

Creating the 'Code Manager' and 'Code Delivery' Bodies will change the way the codes are managed, delivered and the roles in which they fulfil which can create a risk to the delivery of projects currently in flight. Transitional arrangements need to be put in place for current change projects being developed to avoid the risk of aborted costs being incurred as a result of conflicting priorities.

Also, it is not clear how 'business as usual' systems enhancements (i.e. those not driven by a contractual change) are treated and if they would be prioritised by the Consultative Board or the Code manager (where appropriate).

2. Would Ofgem's enhanced powers over strategically important modification proposals mean that our Significant Code Review (SCR) powers will be obsolete, and will the new powers form an effective substitute? Please explain your reasoning

We believe that through CGR3 you introduced the enhanced ability to run and control the direction of SCRs and the changes associated with the SCRs. SCRs provide a freeze on the codes to ensure that changes are made on a holistic basis to avoid a wider range of individual modifications causing confusion and a sub-optimal outcome.

It is not yet clear how the Strategic Direction and Consultative Board will control wide-scale change to the extent that it will also control the ability for individual parties under Open Governance² being able to raise modifications in parallel to the delivery of the Strategic Direction.

If the process for delivering the Strategic Direction can be made clearer by providing you with the ability to initiate and steer proposals of significance, then it can be used as a suitable avenue for change to the extent that the SCR process may no longer be required.

3. What are your views on staggering the implementation of competitive applications for licences?

It is important when implementing any wholesale change into industry to ensure any adverse impacts are managed, and where possible, negated. With such a wholesale change to the code arrangements, it will have an impact on the development of change and industry engagement as industry gets to grips with new governance structures and accountabilities for codes in relation to Code Management and Delivery.

As a result, in our view anything that will negate this risk is a positive step so is fully support of staggering competitive tenders in order to ensure the industry workload is manageable. For example, staggering implementation (perhaps prioritising smaller codes) would enable the tendering process to be trialled and if necessary refined before the 'larger' codes are transitioned to this process.

However, it is important through the passing of time for the tendering process to align so that all codes are tendered at the same time to ensure transparency and the most cost efficient process for the consumer. Furthermore, we are concerned that the current diversity of funding mechanisms for Code Administrators means that it is hard to benchmark against each other. Therefore we feel it is

² 'Open Governance' is the term for Code Governance that allow parties the ability to raise and develop Code change proposals.

important that there is a consistent funding mechanism in place for all 'Code Managers' and 'Code Delivery' Bodies so they can be truly benchmarked against each other. This should then support the case for the consolidation of 'Code Managers' and eventual reduction in the quantity of industry codes, which based on feedback, should assist with the participation levels of smaller and independent parties.