Northern Powergrid's response to Ofgem's Industry Code Governance: Initial consultation on implementing the Competition and Markets Authority's recommendations

KEY POINTS

Strategic direction of the industry codes is vital to support the significant change programme that is required to deliver a smart, flexible energy system. The strategic direction from Ofgem needs to encompass all commercial and technical areas but code governance itself should distinguish between these areas to reflect differing needs. The need for efficiency in making these changes is higher than ever with the draw on resources created by Brexit and the existing code administrator routes could be used to enact some of the changes.

- We understand the merits of applying the **new governance regime to those codes that manage the commercial trading arrangements** between parties and the industry systems that support those trading arrangements.

  - We see the **merits in competitively tendering code management and code support services** and we have participated in such commercial processes in support of the Distribution Connection and Use of System Agreement.

  - However, we do not believe it is appropriate to introduce third party code managers for the electricity network technical codes (i.e. the Grid Code and Distribution Code). It is important to **retain the link between management and delivery**.

  - A phased approach may be a practical step to implement the changes on a prioritised basis.

- If there are delays to licensing of codes due to other governmental priorities there should still be alternative ways to **improve code and coordination via the code administration code of practice (CACoP)** to drive desired outcomes for significant projects.

- We **strongly support the proposals on the development of the strategic direction**, perhaps starting with the inclusion of the key projects from Ofgem's forward work plan together with additional detail on target outcomes.

- **When Ofgem establishes the consultative board it will need to be appropriately resourced.**

  - Acquiring the necessary resources for the consultative board will need prioritising in order to support better overall management of code-code change activity for priority projects.

  - Secretariat and project management resources will be required in addition to senior industry stakeholders.

1.   Introduction

1.   Northern Powergrid welcomes the opportunity to response to Ofgem's consultation on implementing the Competition and Market Authority's (CMA's) remedies on industry code governance, we also appreciate the additional context provided at Ofgem's stakeholder workshop on 12 January 2017.

2.   The well-attended and active participation in the workshop was valuable and effectively communicated a wide range of stakeholder views. We realise there are challenges for Ofgem in developing appropriate solutions and we are keen to support Ofgem in its further work in this area.

3.   We note the following key changes that Ofgem plans to put in place:

   • Licensing of code managers and delivery bodies: Ofgem will design a new regulatory regime for code management and system delivery, considering a role for competition in driving benefits for consumers;

   • Setting a strategic direction for code development: Ofgem will introduce a new tool to provide industry with a coherent vision for change. This will set the parameters of the new arrangements, making sure effort and resources are focused on the industry changes that benefit customers most; and

   • Establishing and running a consultative board: This new body will coordinate and prioritise cross-code change that benefits consumers. It will develop and help maintain a joint industry plan in line with the strategic direction.

2.   Detailed responses to the consultation questions

4.   Set out below are our responses to the individual consultation questions separated by chapter.

Chapter 2: Scope of the new arrangements

Question 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?

5.   No, not entirely. We understand the merits of applying the new regime to the codes that support detailed operational process arrangements between parties and commercial trading arrangements, especially where there are clear adverse effects on competition. However, we do not perceive the same concerns, issues and risks in respect of the Grid Code (GC) and Distribution Code (DC). Changes to these technical network codes do not seem to present the same types of issues as those for the commercial and operational/central system codes. We are not aware of any parties presenting change proposals on the networks codes that raised

subsequent concerns regarding the management of such proposals. Therefore, we are not aware of an identified need to change the governance of these network codes. We are not opposed to change *per se* but the need for (and cost of) change must be weighed against the benefits (for which a compelling case has not been forwarded). Having said this, if there are legitimate concerns we would be keen to help look at the issues and consider potential improvements.

6.   It may be that a phased approach is appropriate with the changes delivering the estimated highest value placed into the new regime first. We would not class the technical network codes in this category.

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

7.   No, we do not believe so.

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

8.   Further to our answer to question 1 we think the emphasis should be on those codes that control industry trading systems and core trading relationships between parties. These are the codes where we can see the benefit in making changes and where we have observed others stating examples from these areas too.

Chapter 3: Licensing and Competition

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

9.   A single licence for end-to-end delivery of code changes seems to be a logical approach. We think there are merits in avoiding additional responsibility boundaries/ hand-offs unless there are clear benefits identified.

Question 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?

10. Yes, we agree with the approach of reviewing the licence requirements of National Grid Electricity Transmission (NGET) in respect of the GC and strengthening if necessary rather than holding a tender to identify an appropriate code manager. The same logic should be applied to the management of the DC; administered by the Energy Networks Association on behalf of the distribution network operators (DNOs). The consultation discusses code management and code delivery and it is obviously important to consider the means of delivery of any change as part of the consideration of any modification; if only to ensure that the views of those parties who would actually deliver and implement are taken into account as a modification is developed and considered.

11. We agree with Ofgem's view (at paragraph 3.6) that the link between management and delivery is important and as a first principle should be the responsibility of a single body for each code. For the technical codes i.e. the DC and GC the delivery naturally falls to the DNOs and NGET respectively. It is important to consider the means of delivery of any change as part of the consideration of any modification if only to ensure that the views of those parties who would actually deliver and implement a change are fully taken into account as a modification is developed and considered. Therefore, it seems reasonable that the code management and delivery remains the responsibility of the DNOs and NGET rather than competitively appointing a new code manager for the DC and GC who may then need to contract with the DNOs/NGET to deliver the changes. Such an arrangement could introduce conflict between the DNOs' or NGET's licences and their interface with a competitively appointed code manager.

12. At paragraph 3.12 the consultation seeks views on the relative pros and cons of strengthening NGET's licence regarding code administration as opposed to introducing competition for the role and we have some view in respect of the GC:

   • Pros: It would retain the linkage between code management, code change delivery and solution implementation. It would also help to ensure that the NGET delivery expertise is factored into change assessment. Provides retention of access to the technical knowledge of NGET staff who would be involved in the implementation of any solution. Avoids the need for a code manager to employ standalone, scarce and expensive technical expertise. Strengthening the licence provides a vehicle for creating improvements if required.
   • Cons: Legacy NGET thinking may inhibit the consideration of innovative ideas. Competition may create the opportunity to reduce the NGET code management costs.

13. This does not mean that there is no case for change in respect of the GC and DC. Rather the joint work by the ENA's group on transmission system operator and distribution system operator interfaces should explore and work with Ofgem to understand how efficient 'whole system' industry change may be delivered. The GC and DC need to be managed in close cooperation to ensure that strategic aims are being met.

Question 3: What are your views on the merits and drawbacks of the four identified models for competitively licensing code management where applicable?

14. We strongly support competitively appointing code managers in pursuit of optimum cost and service. Whilst we have no strong preferences on the optimum procurement model, model 3 seems to offer the optimal balance of pros and cons as per table 2 of the consultation. Permissive models 1 and 2 appear inefficient due to a two-step process with the initial qualification stage potentially too low a hurdle to add value to the process.

15. For models 1 and 2 there would also seem to be a risk of tying up Ofgem resources in vetting numerous applicants and granting licences without having upfront visibility on how many companies might submit an application just to get on a code governance 'long list' pool i.e. in case they decide to bid for a code manager role in the future.

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

16. Model 3 (and perhaps model 1) would seem to be the most appropriate for the commercial trading codes so that the parties affected by the codes can have the confidence of Ofgem leading a tendering process (linked to Ofgem's target outcomes) rather than another separate body.

17. However, there may be a need for a variation on model 3(a 'model 3a') for those codes that also manage industry systems. This could be a modified model 3, whereby a small number of topic experts are added to Ofgem's tender evaluation team, perhaps recruited from the current experts on the relevant code's panels.

Chapter 4: Strategic Decision

Question 1: Do you agree with the purpose of the strategic direction?

18. Yes, we understand the need for and agree with the purpose of the strategic direction.

Question 2: Do you have any views on how the strategic direction should be developed and implemented?

19. We note the intention to develop iteratively the initial strategic direction and a useful starting point may be to set out the key strategies driving the existing priorities in Ofgem's forward plan. Ofgem could then consult on potentially desirable further changes resulting from those priorities.

20. We believe that options for more fundamental changes should be consulted on separately in line with the approach taken with the call for evidence on a smart, flexible energy system. There may be merits in splitting Ofgem's ongoing aims and outcomes between short- and medium-term priorities.

Question 3: How much detail do you consider should be included in the strategic direction?

21. We think that the detail should focus on target outcomes. The detail should be included for short-term priorities. For medium-term priorities the level of detail may be less important and should avoid being overly prescriptive on the mechanisms for delivery. A draft plan could be consulted on with parties and especially code managers being consulted on the options for delivery of the priorities.

Question 4: Which specific projects do you consider should be included in the initial strategic direction?

22. We propose that Ofgem should prioritise those areas that are more likely to be 'code change intensive'. It is these areas where there is the most value in ensuring that industry change is being developed and implemented at an appropriate pace.

23. As such we propose that the subjects most in need of initial strategic direction are as follows:

- Faster switching and the smart meter programme

- Half-hourly settlement
- Network charges (as set out in the call for evidence on a smart, flexible energy system)

Chapter 5: Consultative Board

Question 1: What do you see as the core role and functions of the consultative board?

24. We agree with Ofgem that the consultative board's key role would be the coordination and facilitation of the delivery of cross-code strategic changes. When Ofgem sets up and runs the consultative board it will need new resources and capabilities if it is to provide sufficient value in respect of maximising the delivery of beneficial changes:

- Senior stakeholders
- Appropriate secretariat support for better management of code change activity with
  - Sufficient technical knowledge of codes; and
  - Programme and project management

25. We have highlighted the need for the consultative board to have access to programme and project managers due to the need to deliver beneficial changes through better overall management, project prioritisation, cross-code coordination, sequencing of deliverables and risk mitigation.

Chapter 6: Moving to new arrangements

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

26. This is not easy to determine at this stage. However any negative impacts could be minimised through appropriate phasing and timing. Please see our answer to question 3 in chapter 6 below.

Question 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.

27. Ofgem taking powers to initiate and prioritise strategically important modification proposals, together with the ability to 'call-in' and take control of such modification proposals would appear to make the current SCR powers obsolete; especially when the wider regime of new arrangements have also been applied appropriately to the relevant codes.

28. We note that Ofgem does not expect to remove the SCR process as a facility to drive change before the licensing arrangements are in place and we agree that this is logical. It may also be appropriate to 'test' how the new arrangements are working in practice in respect of significant changes prior to switching off the SCR facility.

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

29. A phased approach to the implementation of the competitive process may be appropriate with the changes delivering the estimated highest value placed into the new regime first. It may also be appropriate to consider newer codes like the Smart Energy Code to be reviewed last.

30. Timing may also be important in order to minimise contractual change risk especially if a particular code is in the middle of delivering something like a major IT project.