

Modification Report
Use of Principles of Governance in Applying Section Y of Network Code
Modification Reference Number 0714

Version 2.0

This Modification Report is made pursuant to Rule 8.9 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

To introduce the Principles of Good Governance within the Modification Rules as currently included within Network Code

2. Transco's Opinion

Transco recognises that the intent of this Proposal is to provide further clarity as to the appropriate criteria against which changes to Section Y of the Network Code should be considered.

However, the Panel are required to consider each Modification Proposal on its own merits, and with regard to better facilitating the achievement of the code relevant objectives, which are set out in Transco's GT Licence. Transco believes that the addition of further criteria and principles on which Modification Proposals to Section Y will be evaluated will add complexity and potential conflict to the process. Equally, in considering Proposals against a separate set of Principles, the primary requirement to better facilitate the achievement of the code relevant objectives (which are derived from the Licence) may be lost or diluted.

If it were established that the code relevant objectives need to be amended or supplemented, this should be taken forward via changes to the GT Licence rather than the Network Code.

Transco notes that the Panel may require assistance in evaluating Modification Proposals to amend Section Y of the Network Code. Transco therefore suggests that the Principles of Governance could be incorporated into the Terms of Reference for the Panel. This might afford some guidance as to how best to assess such Proposals, whilst also ensuring that the obligation to better facilitate the code relevant objectives takes precedence when considering the process to be applied to a Proposal.

Transco also questions the means by which these Principles of Governance might be enforced. If, as it is suggested, they do not form part of the Network Code and are not an Ancillary Agreement, it is apparent that no party or person has any means by which to enforce compliance with them. Transco therefore does not support implementation of this Proposal.

3. Extent to which the proposed modification would better facilitate the relevant objectives

The proposer makes no specific reference as to how this Proposal would better facilitate the relevant objectives.

In relation to whether or not the Proposal better facilitates the code relevant objectives, Transco considers that the addition of the Principles of Governance against which a Proposal should be assessed adds unnecessary complexity to the governance regime and therefore would not better facilitate achievement of the code relevant objectives. More fundamentally, we are also concerned that the relevant code objectives are derived from the Licence, and the addition of any further, different criteria could detract from the hierarchy of the Licence.

**4. The implications for Transco of implementing the Modification Proposal , including
a) implications for the operation of the System:**

Transco does not anticipate any such implications.

b) development and capital cost and operating cost implications:

Transco does not envisage additional capital or operational costs as a result of this Proposal.

c) extent to which it is appropriate for Transco to recover the costs, and proposal for the most appropriate way for Transco to recover the costs:

No significant additional costs are anticipated.

d) analysis of the consequences (if any) this proposal would have on price regulation:

Implementation of this Proposal would not be expected to impact price regulation.

5. The consequence of implementing the Modification Proposal on the level of contractual risk to Transco under the Network Code as modified by the Modification Proposal

It is not anticipated that there will be a change to the level of contractual risk to Transco as a consequence of this Proposal.

6. The development implications and other implications for computer systems of Transco and related computer systems of Users

No such implications are anticipated.

7. The implications of implementing the Modification Proposal for Users

- Users may find the Principles of Governance add clarity when raising Modification Proposals for Section Y.
- Users may find the additional criteria against which they must justify Modification Proposals to Section Y confusing and onerous, and there is potential for conflict with Transco's Licence obligations.

8. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non-Network Code Party

No such implications are anticipated.

9. Consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party of implementing the Modification Proposal

Transco is not aware of any such consequences.

10. Analysis of any advantages or disadvantages of implementation of the Modification Proposal
Advantages

The Proposer states that "each of the proposals [0712: Additional Information in Modification Proposals and Modification Reports, 0713: Ability for Users to Vary their Modification Proposals, 0714: Use of Principles of Governance in Applying Section Y of the Network Code and 0715: Modification Panel Approval of the treatment of Representations in Final Modification Reports] presents a reasoned identification of the issues being addressed together with a revised method, which instils greater transparency, consistency, efficiency and collection and collation of information upon which any Modification Proposal may be judged against the relevant objectives of the licensed parties concerned".

Disadvantages

- Transco believes there is a risk that implementation of this Proposal may make the governance process overly complex in that there will be criteria, in addition to the code relevant objectives, against which a Proposal has to be assessed. These new criteria also have the potential to conflict with Transco’s current Licence Objectives, and the current relevant code Objectives (which can only really be changed following an associated Licence change.)
- In taking into account additional criteria when assessing the merits of a Modification Proposal, there is the risk that the primary requirement to better facilitate achievement of the relevant objectives may be lost or diluted.

11. Summary of the Representations (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

Transco received 12 representations to the Proposal from the following:

Association of Electricity Producers	AEP	
BP Gas Ltd	BPG	
British Gas Trading	BGT	
EDF Energy plc	EDF	
E.ON UK plc	EON	
The Gas Forum	GFO	
Genserv	GEM	
RWE npower plc	RWE	
Scottish and Southern Energy plc	SSE	
Shell Gas Direct	SGD	
Statoil (UK) Ltd	STA	
Total Gas and Power Ltd		TGP

11 of the respondents supported the Proposal.
 1 respondent (GEM) provided comments.

Existing Processes

Two respondents (BGT and SSE) acknowledge that “the existing processes have on the whole delivered a workable methodology” and that “Transco’s stewardship of the process to date has been largely satisfactory”. TGP state that “the driver behind the proposals has been to encapsulate and formalise best practice within the process, recognising that much of the time this best practice is already followed”.

Transco Response

Transco is also of the opinion that the existing processes have, and continue to work well and therefore questions the requirement to formalise and add complexity and potential conflict to the current arrangements by making these changes.

Management of the proposed Principles of Governance

Six respondents (BGT, EDF, SSE, EON, TGP and GEM) believe that the Principles of Governance should not be an Ancillary Agreement, but be a “referenced document” which is made available to the industry. BGT, EDF and TGP believe the Modification Panel should maintain the document.

GFO state “these proposals would improve the governance regime by introducing greater transparency and equality”. AEP believe that the proposals “provide for greater transparency of process and lead to more efficient and effective modification arrangements”.

Transco Response

It has not been made clear in the Proposal how changes to the Principles of Governance might be proposed or approved. Transco is concerned that without a formal change process allowing Users to propose changes and put forward views on other proposed changes, the Principles of Governance could be changed by the Panel to suit their requirements, which is not transparent, equitable or non-discriminatory.

Transco does not see how this Proposal would make the governance process more efficient. Indeed, to require the Panel to consider additional criteria against which the merits of Proposals are measured would seem to make the process more onerous and complex with the potential for conflict between the proposed Principles of Governance and the code relevant objectives.

As it is proposed that the document is “maintained” by the Panel and does not suggest that Users or the Authority be given an opportunity to propose changes or influence its maintenance, Transco does not believe this is transparent or equitable.

Implementation Timescales

Five respondents comment on the implementation timescales of this Proposal. TGP, EON, GFO and SSE believe the Proposal could be implemented without delay. GEM state, “there seems little impediment to immediate implementation”.

Transco Response

Transco does not support implementation of this Proposal.

Complexity

Four respondents (GEM, TGP, EON, and BGT) do not believe the Proposal would make the governance process overly complex.

Transco Response

The role of the Panel is to assess whether or not a Modification Proposal is likely to better facilitate the achievement of the code relevant objectives. These objectives are set out in Transco’s GT Licence. It is Transco’s belief that the addition of further criteria and principles on which the Panel must assess the route to be followed for a Modification Proposal will add complexity to the process, and in considering Proposals against a set of Principles, the primary requirement to better facilitate the achievement of the code relevant objectives may be lost or diluted.

Relevant Objectives

EDF believe that this Proposal will “better facilitate the relevant objectives as defined under amended license standard condition 9 (b), which states that Transco is required to efficiently discharge of (sic) its obligations”. GEM supports the proposer’s views that the Proposal “would better facilitate Transco’s discharge of its licence Condition 4D. Since relevant objective b) in licence Condition 9. 1 is “.... the efficient discharge of its obligations under this licence” each of the proposals must therefore further facilitate the relevant objectives”.

Transco Response

In making its decision as to whether a Modification Proposal should be implemented, Ofgem are bound to consider each Proposal on its own merits, and with regard to better facilitating the achievement of the code relevant objectives. The Panel are also bound by these requirements and therefore should not be considering Proposals against a separate set of principles.

The code relevant objectives are contained within Transco's GT Licence. Therefore any amendment or addition to these objectives that may be required should be achieved by changing the GT Licence.

In its decision letter regarding Modification Proposal 0679: Formally Include the Network Code Modification Rules within the Network Code, Ofgem "*notes that the Balancing & Settlement Code refers specifically to promoting efficiency in the implementation and administration of the balancing and settlement arrangements. However, in judging whether a change to the modification rules themselves would or would not be worthwhile it does not seem that an objective of this type adds any particular clarity. Ofgem holds the view that the current objectives as defined in Standard Condition 9 of the Gas Transporters Licence, in particular objective b), are adequate for judging the benefits of a modification proposal on rule changes, though Ofgem will continue to monitor the situation and give further consideration to the possibility of reviewing the Network Code objectives at a future date, if appropriate*".

Transco agrees with Ofgem that the current objectives are adequate for judging the benefits of a Modification Proposal on rule changes.

In relation to whether or not the Proposal better facilitates the code relevant objectives, Transco considers that the addition of the Principles of Governance against which a Proposal should be assessed adds unnecessary complexity to the governance regime and therefore is not consistent with the code relevant objectives.

12. The extent to which the implementation is required to enable Transco to facilitate compliance with safety or other legislation

Transco is unaware of any such requirements.

13. The extent to which the implementation is required having regard to any proposed change in the methodology established under Standard Condition 4(5) or the statement furnished by Transco under Standard Condition 4(1) of the Licence

Transco is unaware of any such requirements.

14. Programme of works required as a consequence of implementing the Modification Proposal

If this Proposal were to be implemented in its current format, Panel members would need to develop and agree, by Panel Majority, a set of "Network Code Principles of Governance". The process and governance to be utilised to develop and agree these new principles has not been clarified.

15. Proposed implementation timetable (including timetable for any necessary information systems changes)

No implementation timetable has been proposed.

16. Recommendation concerning the implementation of the Modification Proposal

Transco does not recommend implementation of this Modification Proposal.

17. Restrictive Trade Practices Act

If implemented this proposal will constitute an amendment to the Network Code. Accordingly the proposal is subject to the Suspense Clause set out in the attached Annex.

18. Transco's Proposal

This Modification Report contains Transco's proposal not to modify the Network Code and Transco now seeks agreement from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

[Draft] Proposed Legal Text

MODIFICATION 714

Use of Principles of Governance in Applying Section Y of Network Code

Section Y: Modification Rules

Insert the following in the appropriate place in paragraph 2.1:

“Network Code Principles of Governance”: a set of standing guidelines so titled and issued by Transco, which may be amended from time to time by Panel Majority.”

Paragraph 6.2.1

Delete paragraph 6.2.1(c) and replace with the following:

"6.2.1(c) set out the basis upon which the Proposer considers that it would better facilitate the achievement of:

- (i) the Relevant Objectives; and
- (ii) in the context of a modification to Section Y and so far as is consistent with 6.2.1(c)(i), the Network Code Principles of Governance;”

Paragraph 6.2.2

Delete paragraph 6.2.2(c) and replace with the following:

"6.2.2(c) set out the basis upon which the Proposer considers that it would better facilitate the achievement of:

- (i) the Relevant Objectives; and
- (ii) in the context of a modification to Section Y and so far as is consistent with 6.2.2(c)(i), the Network Code Principles of Governance;”

Paragraph 7.2.2

Delete "meeting of the Modification Panel." from the end of paragraph 7.2.2(f)(ii) and replace with the following:

" meeting of the Modification Panel; or".

Insert the following new paragraph after paragraph 7.2.2(f)(ii):

“iii) that the Modification Proposal be referred back to the Proposer for amendment and the Modification Panel shall prepare and issue to the Proposer its reasons as to why the Modification Proposal does not facilitate the achievement of the Network Code Principles of Governance.”

Paragraph 7.2.4

Insert the following after paragraph 7.2.4:

“7.2.5. Where the Modification Panel discusses a Modification Proposal which has been previously discussed and referred back to the Proposer in accordance with paragraph 7.2.2(f)(iii) the Modification Panel may:

- (a) make a determination in accordance with paragraph 7.2.2 (d) or 7.2.2 (f); or
- (b) determine that the Modification Proposal should be dealt with in accordance with paragraph 7.3.”

Paragraph 7.3

In paragraph 7.3, delete the words "or 7.2.4(b)(i)" and replace with the following:

“7.2.4(b)(i) or 7.2.5(b)”

Paragraph 8.6.1

Delete paragraph 8.6.1(a) and replace with the following:

"8.6.1(a) provide an analysis of whether and if so the extent to which the Modification would better facilitate the achievement of:

- (i) the Relevant Objectives; and
- (ii) in the context of a modification to Section Y and so far as is consistent with 8.6.1(a)(i), the Network Code Principles of Governance;”

Paragraph 8.9.3

Delete paragraph 8.9.3(c) and replace with the following:

"8.9.3(c) provide an analysis of whether and if so the extent to which the Modification would better facilitate the achievement of:

- (i) the Relevant Objectives; and
- (ii) in the context of a modification to Section Y and so far as is consistent with 8.9.3(c)(i), the Network Code Principles of Governance;”

In paragraph 8.9.3(r) delete the words "relevant objectives" and replace with the following:

"Relevant Objectives and, in the context of a modification to Section Y and so far as is consistent with the Relevant Objectives, the Network Code Principles of Governance."

Paragraph 11.4

Insert the following after the words "Relevant Objectives" in paragraph 11.4:

"and, in the context of a modification to Section Y and so far as is consistent with the Relevant Objectives, the Network Code Principles of Governance"

Paragraph 11.9.3

Delete the word "or" where it appears, at the sixth occurrence, at the end of paragraph 11.9.3(b).

Delete paragraph 11.9.3(c) and replace with the following:

"11.9.3(c) to change the Chairman's Guidelines, or;"

Insert the following new paragraph 11.9.3(d) after paragraph 11.9.3(c):

"11.9.3(d) to change the Network Code Principles of Governance"

Signed for and on behalf of Transco.

Signature:

Richard Court
Commercial Frameworks Manager
NT & T

Date: