

UNC modification panel action PAN 0501

RP to provide a legal view on the self-governance criteria set out in the Transporters' licence and if this would conflict with the new approach to self governance implemented with CGR3.

Below the advice WWU has received.

Recommendations

It is suggested that, in order to deliver Ofgem's Final Proposals and the specific requirements for the same set out in the annex to the 3rd May letter, steps are taken along the following lines:

- Retain the existing criteria for self-governance criteria (i.e. the test remains whether a material impact is unlikely to occur)
- Amend the modification process so that as part of the assessment of the self-governance criteria the panel is required to address whether the proposal if implemented would have a material impact
- The modification process should require the Panel to set out its findings with respect to materiality and likelihood and the reasons for its determination both in its self-governance statement and in a new "non-self-governance statement" to be produced when the Panel determines that the proposal is not unlikely to have a material effect and therefore should be determined by Ofgem
- Develop Guidance, in consultation with Ofgem and the industry, as to what does and what doesn't amount to a material impact on consumers competition etc.. Although Ofgem has asked the Code Administrators to develop this guidance, it would make sense for the guidance ultimately to be published by Ofgem, not the Code Administrators, reflecting the CMA's provisional recommendations

The first point preserves licence compliance and the second and third points (along with the guidance referred to at the fourth bullet point) would mean that the Panel appropriately addresses their minds to the materiality of any impact before deciding whether or not the material impact is unlikely to occur and hence whether or not the self-governance route should be used.

Reasoning and recommendations

A change to the modification rules so that proposals are subject to self-governance unless changes are likely to have a material impact (the "self governance default mode") would place transporters in breach of Standard Licence Condition (SLC) 11. The licence conditions as modified do not alter the requirement that the modification rules should provide that proposals only go to self-governance route if the proposal is unlikely to have a material impact (the Ofgem decision default mode).

There are two significant differences between the two modes. The first relates to the applicable default process - Panel or Ofgem decision. The second is that determining that something is unlikely to happen (which to my [WWU's legal advice not RP] mind implies a probability of it of less than @25%, though there is no precise measure of probability) is materially different to determining that it is not likely to happen (which to my mind requires the probability of it happening as being less than @60%).

However, no licence change is required in order to comply with Ofgem's final proposals or the requirement in the [Annex to its letter to the Panel Chairman](#) of 3 May. The latter requires "Modifications to codes such that Industry assesses whether a modification is material, and therefore requires the consent of the Authority, in deciding whether to use the self-

governance route". As for the Final Proposals document (even though there is some muddled thinking as to default processes of Distribution Code MRA etc, in paragraph 3.16), Ofgem's Final Proposal as to self-governance is "that modifications should be assessed as to whether they require an Authority decision – i.e. why they are material" (paragraph 3.15). Paragraph 3.17 provides that "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" – "this" being an assessment of materiality.

An assessment of materiality does not and cannot without a licence change require the modification processes to switch from Ofgem decision default mode to self-governance default mode. It simply requires an assessment of materiality to be incorporated into the process – and after all in reality it is materiality rather than probability that is really the issue - the probability of an impact occurring is entirely dependent on the materiality of the impact. If the impact of a modification would be material it is almost certain that the impact on consumers competition etc. will occur; and an assessment that there would be no material impact self-evidently amounts to a finding that a material impact is unlikely to occur.

This interpretation is entirely consistent with the CMA's [Provisional decision on remedies](#) and its conclusions on self-governance. These are discussed at length in paragraphs 47 to 53 of [Appendix 10.4](#), which include the following statements of particular relevance:

49... we note Ofgem's analysis of all code changes processed from May 2014 to May 2015, which concluded that the usage rate of self-governance during that period could have been as high as 50% if each of the code panels had interpreted the materiality criterion in line with Ofgem's understanding of that concept. Ofgem has stated that the discrepancy it has identified between the actual and possible usage rate is likely due to code panels taking an overly conservative approach in making such determinations...

50 ... we consider that Ofgem could accelerate the process by which code panels arrive at the 'correct' approach to interpreting the materiality criterion by publishing guidance on this subject. Ofgem should seek input from each of the code panels and code administrators in developing this guidance to ensure that the proposed guidance is of practical use to those entities. Therefore, Ofgem should publish guidance, developed in the manner described above, on how the materiality criterion should be interpreted for the purposes of self-governance...

51 ... As a separate matter, we note that as part of its ongoing Code Governance Review, Ofgem is considering making the self-governance process the default option to process any given code change that is not the subject of an SCR. This change would effectively reverse the evaluation undertaken to determine whether an MP is eligible for self-governance...

52. In our view, this change could help to overcome the current conservative approach adopted by code panels in interpreting the materiality criterion. However, we recognise that there is a risk of code panels taking an equally conservative approach in relation to submitting code changes for the ordinary modification process and that, as a result, the usage rate of the self-governance could be (significantly) higher than the 50% that Ofgem considers appropriate. This, in effect, would excessively restrict Ofgem's role in code governance, which we consider inappropriate. Therefore, regardless of which modification 'route' is established as the default option, we believe that Ofgem should provide guidance on how to interpret the materiality criterion in order to achieve an efficient usage rate for self-governance and monitor compliance with that guidance.

In other words the CMA has reservations about the adoption the self-governance default mode (which as indicated above is impermissible without a licence change), but regards a better assessment of materiality as key to the process, irrespective of whether the process defaults to self-governance or Ofgem determination.

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- The modification process should require the Panel to set out its findings with respect to materiality and likelihood and the reasons for its determination both in its self-governance statement and in a new "non-self-governance statement" to be produced when the Panel determines that the proposal is not unlikely to have a material effect and therefore should be determined by Ofgem
- Develop Guidance, in consultation with Ofgem and the industry, as to what does and what doesn't amount to a material impact on consumers competition etc.. Although Ofgem has asked the Code Administrators to develop this guidance, it would make sense for the guidance ultimately to be published by Ofgem, not the Code Administrators, reflecting the CMA's provisional recommendations

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