

Review Group Report
Review Proposal Reference Number 0334
Post Implementation Review of System Funding and Governance Arrangements
Draft Version 0.1

This Review Group Report is presented for the UNC Modification Panel's consideration.

1. Review Proposal

It is proposed that the industry undertaking a review of the current Central System Funding and Governance Arrangements that have been in place since GDPCR.

Development of Current System Funding and Governance Arrangements

As part of the DN Sales process a transporter agency was created to ensure that transporters could continue to provide a common service and system interface to Code Parties. Though at the time of the DN Sales the funding arrangements for central system was maintained, it was Ofgem's belief whilst undertaking the Gas Distribution Price Control Review (GDPCR) in 2008 that *"the current funding model may provide poor incentives both on the GTs to provide anything more than a minimum level of service and on users (primarily shippers and suppliers) to manage xoserve's costs"*.

To resolve this issue, GDPCR separated funding for xoserve into two discrete areas; Core services, where the current funding arrangements would continue and User Pays services where charges are levied upon the User requesting the change. To allow Code Parties to assess the implications of any change, xoserve would provide a Rough Order of Magnitude (ROM) cost, with a Detailed Cost Analysis (DCA) undertaken if the modification was implemented.

These two changes fundamentally altered how Code Parties interact with central systems, in particular when looking to alter how services are provided, either via UNC modification proposals or User Pays Services outside of the UNC.

To support these new arrangements a suite of documents and operating procedures were developed. In addition to the UNC, these documents include:

- Agency Services Agreement(ASA)
- Agency Charging Statement (ACS)
- User Pays Guidance Documents
- Contract for Non-code User Pays services

These processes have remained fundamentally unaltered since they were implemented as a result of GDPCR.

Review Timing

The current regime has been in operation for two years. During that time several major changes to the UNC have been progressed and funded through both Core Services and the User Pays regime. This has provided useful practical experience in how the new regime operates. In addition industry developments (Project Nexus, the Smart Metering Implementation Programme and the forthcoming GDPCR) will be impacted by the current System Funding and Governance arrangements. It therefore seems germane to assess the current arrangements to see whether any lessons can be learned from past experience and identify improvements to the current framework.

Review Scope

The current funding and governance arrangements for central systems have a significant bearing on many aspects of the UNC. In light of this any review will require a wide scope. It is suggested that the following areas are examined:

- Funding of central systems, in particular cost allocation and recovery.
- Governance framework of central service provision
- Transparency and accountability of the current regime.
- Cost calculation, in particular how costs are incurred and calculated and the timescale they are provided in.
- Impact on change process of current regime.

Review Aim

The aim of the review is to assess the current funding framework, identifying areas of good practice, as well as those areas that may require improvement. Particular attention will be given to previous experience of how the current regime has operated since it was implemented.

Efforts will be made to identify both short-term solutions, as well as more fundamental reforms.

These findings will be then be summarised in the review group report.

2. Review Process

In accordance with the Modification Rules, at its meeting on 22 October 2010, the Modification Panel determined that this Review Proposal should be referred to a Review Group for progression. This Review Group Report was subsequently compiled by the Joint Office and approved by Review Group attendees.

3. Areas Reviewed

The following items were identified in the Terms of Reference as being included within scope of the group, and a summary of the discussions has been provided under each heading:

1. Possible Incremental Changes.

A number of potential changes that could improve the current process were identified:

- Creation of an account management framework within xoserve, which may help create increased customer focus.
- Joint Office to provide estimated costs for secretarial services associated with taking forward each modification proposal.
- Availability of early engagement with xoserve (through a formal or semi-formal process) in order to explore all options and arrive at the solution most likely to lead to implementation.
- UK Link Committee to be reviewed with a view to it being more engaged at the right time with the modification assessment.
- Change implementation to be aligned with planned release dates to ensure that all parties are working to fixed dates.
- All modifications that require systems development (other than minor maintenance changes) to be assigned to a Workgroup, which must complete an assessment to report stage.

2. Fundamental Changes

Gazprom Marketing & Trading – Retail (GMTR) presented a series of options that would fundamentally alter some or all of the current funding and governance

requirements.

- Oversight Committee;
 - This option creates a new committee with a focus on delivering changes on time and with the greatest cost efficiency. This committee could subsume the current activities of the UK link committee, though this group would have a much wider focus.
 - This group would have permanent members and would be comprised of Shipper and Transporter Representatives.
 - Each new modification would be sent to this committee for consideration at the same time as the relevant workgroup.
 - The committee would assess the changes needed to deliver the modification's intent and ideals and attempt to achieve them at optimum cost and timescales.
 - The committee would also be expected to suggest changes to the modification that would result in cost or time savings.
 - This new process would not require changes to the current licence regime and could be implemented via the UNC modification process.
- Alteration to xoserve board membership;
 - This option alters xoserve's current board composition to include Shipper representatives, either as executive or non-executive directors (similar for example to Elexon).
 - These board members would have the same powers and responsibilities as other members of xoserve's board.
 - Shipper representatives would be elected in a process similar to the UNC Panel Shipper election process.
 - This option would require changes outside of the UNC process, including licence changes and changes to xoserve's corporate structure.
- Competitive Tender process;
 - Central system activities would be defined as discrete activities and would be tendered for provision by third parties.
 - xoserve would act as the agent to ensure that the service is provided effectively and cost efficiently.
 - This option would require changes outside of the UNC process, including licence changes.
- Financial separation;
 - xoserve would have separate funding arrangements but would still be owned by the transporters.
 - This option would require changes outside of the UNC process, including licence changes.
- Ownership change;
 - xoserve would be owned by Shippers and Transporters.
 - Would require separate board and governance structure to direct strategies.
 - Board would be comprised of owners.
 - This option would require changes outside of the UNC process, including licence changes.

3. Summary of other items discussed

- Funding the development of change
- Transactional costs/market share
- PCR funding options
- Funding models used by other codes

- Funding Options

The following funding options were discussed by the Review Group

- a. *Apportion costs by Market share*
 - i. *Supply points e.g. Mod 224 (DME)*
 - ii. *Energy use/throughput*
 - iii. *Benefit of market share*
 - iv. *Transparent and easy to implement*
 - v. *Links costs to the modification*
 - vi. *Invoice once development work is complete?*
- b. *Only those who wish to use the service pay*
 - i. *Requires an allocation mechanism*
 - ii. *Market share/share of use of the service?*
 - iii. *Requires an early commitment by parties to take the service*
- c. *Bundling up the analysis and development costs and then invoicing the industry at a regular interval*
 - i. *Requires an allocation methodology*
 - ii. *Cost of development and payment not as clearly aligned to a particular modification*
 - iii. *Requires regular reporting to and monitoring by the industry*
- d. *An upfront central change fund*
 - i. *Need to agree how much each party puts in*
 - ii. *Approval of draw down of funds required*
 - iii. *How do we ensure fairness of use?*
 - iv. *Links costs to a specific modification*

4. Recommendation

4.1 Possible Incremental Changes.

The Review Group members considered the following potential changes could improve the current change management process:

- Review the current xoserve customer interaction with Shippers to deliver focused change, which may help enhance customer satisfaction.
- Where appropriate Shippers should approach xoserve/Transporters for assistance, with exploring and developing options and endeavour to arrive at a solution most likely to lead to implementation.
- xoserve to provide an early view on potential implementation timescales and indication of costs using a pre-defined matrix.
- The change process matrix should be reviewed on a regular basis and refined over time.
- Review the role and responsibilities of the UK Link Committee and involve the committee earlier during the modification assessment process.
- Implementation of system changes to be aligned with planned release dates to ensure that all parties are working to fixed dates, unless there are exceptional circumstances e.g. direction from the Authority or European Regulation.
- Enable the UNC Panel to recommend implementation dates for modifications, in line with the implementation plan specified by the proposer.

4.2 Fundamental Changes

The Review Group members considered there is an opportunity to develop further fundamental changes to the funding and operation of the change management process in addition to those specified above: **[to be discussed in more detail at the next meeting]**

- *Oversight Committee;*
 - *Create a new committee with a focus on delivering changes on time and with the greatest cost efficiency. This committee could subsume the current activities of the UK link committee, though this group would have a much wider focus.*
 - *This group would have permanent members and would be comprised of Shipper and Transporter Representatives.*
 - *Each new modification would be sent to this committee for consideration at the same time as the relevant workgroup.*
 - *The committee would assess the changes needed to deliver the modification's intent and ideals and attempt to achieve them at optimum cost and timescales.*
 - *The committee would also be expected to suggest changes to the modification that would result in cost or time savings.*
 - *This new process would not require changes to the current licence regime and could be implemented via the UNC modification process.*
- *Alteration to xoserve board membership;*
 - *Alter xoserve's current board composition to include Shipper representatives, either as executive or non-executive directors (similar for example to Elexon).*
 - *These board members would have the same powers and responsibilities as other members of xoserve's board.*
 - *Shipper representatives would be elected in a process similar to the UNC Panel Shipper election process.*
 - *This option would require changes outside of the UNC process, including licence changes and changes to xoserve's corporate structure.*
- *Competitive Tender process;*
 - *Central system activities should be defined as discrete activities and would be tendered for provision by third parties.*
 - *xoserve would act as the agent to ensure that the service is provided effectively and cost efficiently.*
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- *Financial separation;*
 - *xoserve to have separate funding arrangements but would still be owned by the transporters.*
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- *Ownership change;*
 - *xoserve would be owned by Shippers and Transporters.*
 - *Would require separate board and governance structure to direct strategies.*
 - *Board would be comprised of owners.*
 - *This option would require changes outside of the UNC process, including licence changes.*
- *Funding Options*
 - *Apportion costs by Market share*
 - *Only those who wish to use the service pay*

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- *Bundling up the analysis and development costs and then invoicing the industry at a regular interval*
- *An upfront central change fund*

Annex 1: Terms of Reference

REVIEW GROUP TERMS OF REFERENCE

CODE REVIEW PROPOSAL No 0334

Post Implementation Review of Central Systems Funding and Governance Arrangements

Version 1.0

Date: 05/11/2010

Nature and Purpose of Proposal

It is proposed that the industry undertakes a review of the current Central System Funding and Governance Arrangements that have been in place since the last TPCR and GDPCR.

Development of Current System Funding and Governance Arrangements

As part of the DN Sales process a transporter agency was created to ensure that transporters could continue to provide a common service and system interface to Code Parties. Though at the time of the DN Sales the funding arrangements for central system was maintained, it was Ofgem's belief whilst undertaking the Gas Distribution Price Control Review (GDPCR) in 2008 that *"the current funding model may provide poor incentives both on the GTs to provide anything more than a minimum level of service and on users (primarily shippers and suppliers) to manage xoserve's costs"*. (Para 8.3, www.ofgem.gov.uk/Networks/GasDistr/GDPCR7-13/Documents1/final_proposals.pdf)

To resolve this issue, GDPCR separated funding for xoserve into two discrete areas; Core services, where the current funding arrangements would continue and User Pays services where charges are levied upon the User requesting the change. To allow Code Parties to assess the implications of any change, xoserve would provide a Rough Order of Magnitude (ROM) cost, with a Detailed Cost Analysis (DCA) undertaken if the modification was implemented.

These changes altered how Code Parties interact with central systems, in particular when looking to alter how either NTS or DN services are provided, either via UNC modification proposals or User Pays Services outside of the UNC.

To support these new arrangements Standard Special Condition A15 Agency of the Gas Transporter Licence (see http://epr.ofgem.gov.uk/document_fetch.php?documentid=14192) requires the establishment of an Agency, and a suite of supporting documents and operating procedures have been developed. In addition to the UNC, these documents include:

- Agency Services Agreement (ASA)
- Agency Charging Statement (ACS)
- User Pays Guidance Document
- Contract for Non-code User Pays services

These processes have remained fundamentally unaltered since they were implemented.

Review Timing

The current regime has been in operation for two years. During that time several major changes to the UNC have been progressed and funded through both Core Services and the User Pays regime. This has provided useful, practical experience in how the new regime operates. In addition industry developments (Project Nexus, the Smart Metering Implementation Programme and the forthcoming RIIO) will be impacted by the current System Funding and Governance arrangements. It therefore seems germane to assess the current arrangements to see whether any lessons can be learned from past experience and identify improvements to the current framework.

Review Group Terms of Reference

Review Scope

The current funding and governance arrangements for central systems have a significant bearing on many aspects of the UNC. In light of this any review will require a wide scope. It is suggested that the following areas are examined:

- Overview of transporter agent funding arrangements.
- Review of the current UNC process including:
 - User Pays Guidance Document
 - Initial identification of funding requirement
 - Apportionment of funding
 - ROM & DCA process, including transparency and timescales
 - Development and levying of charges
 - The process for ACS changes.
- Review of the current non-Code User Pays Service process.
- Comparison of industry practices (gas and electricity) to identify possible improvements that can be applied to gas.
- Comparison of current process with commercial best practice, especially where central systems are used and the associated change process.
- Examination of previous Modifications progressed under the current regime to identify good practice, as well as areas of improvement.
- Consideration of the impact of the Code Administration Code of Practice and the associated changes to the Modification Rules.

Suggested Aims and Outputs

The aim of the review is to assess the current funding framework, identifying areas of good practice, as well as those areas that may require improvement. Particular attention will be given to previous experience of how the current regime has operated since it was implemented.

Efforts will be made to identify both short-term solutions, as well as more fundamental reforms, such as the scope for competition in meeting service requirements.

It is envisaged that this Review Group will produce a report detailing its findings, recommending any necessary changes to the UNC, any other industry code or organisation working practices. It is recommended that the Review Group completes its work within a 6 month period. If necessary this could be extended by seeking agreement of the Modification Panel.

The Review process will also support the Transporters' stakeholder engagement processes

as part of the forthcoming RIIO review of price control allowances.

It is not expected that this Review Group should attempt to develop detailed modification proposals as part of the final report.

Scope and Deliverables

The Review Group shall focus on changes to the UNC but also identify where improvements could also be made to related matters outside of the UNC.

The Review Group is to consider recommendations based on evidence provided during the meetings.

Limits

The Review Group will focus on developing recommendations that efficiently address any issues identified in a proportionate and cost effective manner. The Review Group will consider changes required to procedures and processes within UNC, however it will not develop changes for non-code processes but will request reports from review group members who can influence changes with the appropriate industry body.

Composition of Review Group

This review group is open to all Transporters and their agents, Code Users, Ofgem and consumer representatives.

A Review Group meeting will be quorate provided at least 2 Transporter and 2 User representatives are present.

Timetable

It is proposed that a period of six months be allowed to conclude this review, however given the complexity of the issues this may need to be extended depending on how this review develops.

Although the frequency of meetings will be subject to review and potential change by the Review Group it is suggested that the initial frequency of the meetings be monthly.

Meetings will be administered by the Joint Office and conducted in accordance with the Chairman's Guidelines.

Review Group Workplan	
Meeting Number	Topics for Discussion
1 – 05/11/10	Review terms of reference
2 – 22/11/10	Overview of existing funding arrangements (Transporters to present) Pass-through of costs (WWU to present) Review of current User Pays process for Code services (xoserve to present) Identification of Proposals which merit examination (ICOSS to propose)
3 – 15/12/10	To be confirmed

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4 – 07/01/11	To be confirmed
5 – 26/01/11	To be confirmed
6 – 16/02/11	To be confirmed
7 – 09/03/11	To be confirmed
8 – 30/03/11	Review of progress, including actions, recommendations and finalising report

