

Review Group Report
Review Proposal Reference Number 0334
Post Implementation Review of System Funding and Governance Arrangements
Version 0.6

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

1. Review 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 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, 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 Group consider scope identified in the Terms of Reference. The discussions covered some potential incremental changes, as well as more radical options for change. These are summarised below. More detailed explanations of each suggestion can be found in the attached matrix (annex 2), which highlights potential advantages and disadvantages, whether the Review Group had reached a consensus and the next steps.

3.1 Incremental Changes.

A number of changes that could improve the current process were identified and are listed below:

- Increase the visibility of the Xoserve change process to help improve understanding by extension of the account management framework within Xoserve.
- Joint Office to provide estimated costs for secretarial services associated with taking forward each modification proposal.
- Availability of early engagement with Xoserve.
- Xoserve to provide a rough cost matrix for early assessment of costs for a solution.
- Create an Oversight Committee or change the role of the UK Link Committee to include the following:
 - 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.
- The Proposer and Xoserve should develop a solution(s) for agreement within a Workgroup, including demand and costing information where available.
- Xoserve to proactively suggest solutions for modifications with the aim of resolving the issue in a fit for purpose manner.
- Review the implementation process to ensure information is available to UK Link Committee and proposer to enable them to provide guidance on the most cost efficient date/way for implementation.
- 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. (Excludes Urgent modifications) This should include a review of legal text and business rules for the solution.
- The modification template should be amended to identify if demand information is required to support the assessment process for the solution.
- Demand information should be requested from Users where the modification requests such information. Information can be provided confidentially where required.
- Improve the visibility of industry change programme.
- Change the governance of non-code services and ACS charges by bringing them into UNC, ensuring regard is given to allow services to be provided to non code parties.
- Subject to 1.8 above, the Joint Office should publish additional advice/guidance on the existing User Pays process to aid proposers.

3.2 Fundamental Changes

Gazprom Marking & Trading – Retail (GMTR) presented a series of options that could fundamentally alter some or all of the current funding and governance requirements. The Review Group members discussed the following options and concurred that the changes were significant and couldn't be considered without consideration of licence and legal changes:

- 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.
- Introduce 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 (PCR) but would still be owned by the transporters.
 - This option would require changes outside of the UNC process, including licence changes.
- Xoserve 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

3.3 Other Options discussed

- The Review Group considered a number of charging options for User Pays services (listed a to d below) to identify if there is an opportunity to standardise the approach to allocating User Pays charges.
 - Option a) Apportionment of costs by Market share:
 - By number Supply points
 - Energy use/throughput
 - Option b) Only those who wish to use the service pay
 - Option c) Bundling up the analysis and development costs and then invoicing the industry at a regular interval:
 - Requires an allocation methodology
 - Requires regular reporting to and monitoring by the industry
 - Option d) An upfront central change fund
 - Would require a cost allocation process
 - Approval of draw down of funds required
- The Review Group considered an additional funding mechanism for the pass through of system change costs:
 - Cost included in allowed revenue in the following Formula Year
 - Charged through Transportation Charges
 - Ofgem direction on Modification Proposal also used to determine qualification for inclusion in UP_t
 - Requires an allocation methodology
- The Review Group considered the implementation of the Code Administrators code of practice and should the Joint Office directly request cost estimates from Xoserve.

4. Recommendations

4.1 Incremental Changes.

A number of changes that could improve the current UNC processes were identified and are listed below. The Review Group recommends these recommendations are implemented in line with the action plan detailed in Annex 3:

- Increase the visibility of the Xoserve change process to help improve understanding by extension of the account management framework within Xoserve.
 - Availability of early engagement with Xoserve.
 - Xoserve to provide a rough cost matrix for early assessment of costs for a solution.
 - Create an Oversight Committee or change the role of the UK Link Committee to include the following;
 - 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.
 - The Proposer and Xoserve should develop a solution(s) for agreement within a Workgroup, including demand and costing information where available.
 - Xoserve to proactively suggest solutions for modifications with the aim of resolving the issue in a fit for purpose manner.
 - Review the implementation process to ensure information is available to UK Link Committee and proposer to enable them to provide guidance on the most cost efficient date/way for implementation.
 - Demand information should be requested from Users where the modification requests such information. Information can be provided confidentially where required.
 - Improve the visibility of industry change programme.
 - Change the governance of non-code services and ACS charges by bringing them into UNC, ensuring regard is given to allow services to be provided to non code parties.
- Subject to 1.8 above, the Joint Office should publish additional advice/guidance on the existing User Pays process to aid proposers.

4.2 Wider ranging changes will need to be considered during Price Control discussions and other Industry changes discussions, these are set out in section 3.2 above.

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

[Annex 2 – Issues Matrix](#)

[Annex 3 - Workplan](#)