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Dear Amanda

Further Review of Industry Code Governance

Cornwall Energy welcomes the opportunity to respond to this consultation. We are closely engaged with the code governance arrangements in our own capacity but also in the interests of many smaller market participants and have extensive experience of their operation.

The two phases of the code governance review to date have improved code governance arrangements in the energy sector but that there is clearly much more to do. We agree with Ofgem that small parties continue to find it difficult and complex to navigate code change processes and to adequately resource the many forums where decisions can and do have material impacts on their businesses. Furthermore some changes, particularly those that are contentious and/or complex, take a long time to make and it is not always the case that the length of time results in quality decisions.

We particularly share Ofgem's concern about the quality of industry analysis on complex changes, especially on the distributional impacts, where the impacts on new entrants, especially those with non-traditional business models, are often overlooked. There is also a tendency for those that oppose a change to delay and to talk up costs and business impacts, and code administrators can struggle to challenge these sorts of contribution. That said, we are naturally wary of changes that simply shoe-horn processes into more expedient timescales without taking proper account of the complexities of the issues or the need to ensure that all parties have been adequately consulted.

We have set out in the attachment our proposal to reform the structure of code governance, which would initially see the bringing together of the multiple code administrators into a single code administrator while retaining separate codes. We believe this would have significant advantages in enabling coordination of change, including where unrelated changes cause bottlenecks in industry resources, and dissemination of best practice across the suite of codes and their administration. It would enable market participants to have a single interface to deal with and would, with a consistent reporting framework, provide for better accountability. These thoughts go beyond the scope of most of the change options flagged by Ofgem, but we believe they logically build on the sentiment behind some of the more radical options outlined.

Indeed, we would have liked to have seen Ofgem be bolder in scoping the change options, especially as we are expecting the CMA to instigate further debate of code governance. In the longer term we think a single code administrator could pave the way for further reforms of industry governance. This could see governance of industry codes under a specifically designed design authority separate from the regulator, with its own mandate. The design authority would have strategic priorities set by government (or on its behalf the regulator) and set out in legislation but would have the mandate to make binding decisions on rule changes. It might also manage credit amounts posted by trading parties and mitigate the excessive credit collected under the different codes, which currently act as a barrier to entry.

The proposal for a single code administrator (or a design authority) would bring more benefits, we believe, than to try to consolidate codes. Our view is that there may be some limited potential to consolidate codes, for example the Grid Code and Distribution Code or the BSC and the MRA, but that ultimately the

different codes fulfil different purposes and create differing rights and obligations. Moves in this direction need to ensure the benefits are not outweighed by the resources and time consumed, particularly when there are a number of significant drivers for industry changes pending.

We consider below more fully the four main areas of change introduced under the code governance reviews.

Code Administration

While the changes introduced to code administration since 2010 have been positive, there is a lot more to do in terms of making code administration and processes consistent across the codes. As noted, our proposal is to move, as a minimum, to a single code administrator that would manage the change process for all the codes. This will make code processes easier to understand as a whole, more efficient and coordinated and in particular help smaller parties with fewer resources. With a common set of procedures, the code administrator can be more focused on acting as critical friend (which is applied fitfully at best at present), on identifying where there are cross-code implications, and on ensuring that code changes are progressed efficiently and in a coordinated manner.

The current initiative to introduce a further Principle to the Code Administrators Code of Practice, which seeks to ensure better cross-code coordination of change, is welcome but very modest. A single code administrator should be more efficient in drawing up timetables to progress change and managing processes to adjust these if necessary as events unfold.

With or without a single code administrator, there is a strong case for much greater harmonisation of the existing codes.

We think **all the panels should be independent with consistent objectives** against which to assess changes to the current baseline.

The current heterogeneity does not make for efficiency or for ensuring that the best decisions are reached. The DCUSA arrangements, where parties vote on recommendations to the Authority rather than a Panel reaching a recommendation, are particularly out of kilter. Ofgem noted in its recent decision on DCP214 *Voting,* which changed the threshold for an "accept" recommendation from all Party categories to a majority of Party categories, that a party voting system may not necessarily be an effective way of ensuring that change recommendations and decisions are made in reference to the applicable code objectives. We agree.

The default position should be that the decision-making processes and the objectives against which changes are assessed should be aligned across the codes unless good reasons can be demonstrated that they should be different.

Codes should also have **uniform procedures based on best practice**. Although all codes have a process of development and consultation, these are currently different for every code. For example, only the BSC consults on its initial recommendation to Ofgem on modification proposals. In the DCUSA there is usually one or sometimes two workgroup consultations before the change report is accepted by the Panel and sent for voting. Under the CUSC stakeholders are consulted at working group stage and then again after the Panel has accepted the modification report but before it votes on its recommendations. These different routes require participants to master multiple processes to understand what stage modifications proposals have reached. They are hard to rationalise for even well-resourced players, and confounding to smaller ones. A single common process would enable easier engagement by market participants and be much more efficient.

A further difference between codes is the degree to which alternative proposals can be raised. For the transmission charging SCR there were 26 Workgroup Alternative CUSC Modifications put to Ofgem to choose between in addition to the original, which presented different combinations of key features. This gave the regulator significant flexibility to choose the form of the final modification. By contrast there is only one alternative proposal possible in BSC modifications, which gave much less flexibility for the cash-out SCR. Under the BSC the working group has de facto control of the alternative and this mechanism has been used on many occasions to restrict the nature of solutions explored. There seems to be no obvious rationale for differences between the different codes.

The format of modification reports should also be aligned and based on a common template. While those of the BSC and UNC are in general clearly sign-posted and easy to navigate, some CUSC reports, for example, can run to hundreds of pages (including all responses), and it can be difficult to locate what alternatives have been proposed and are being taken forwards. In the at-length reporting of workgroup discussions it can be difficult to quickly appraise the key issues. Better consistency between the format of the reports of different codes would aid industry parties in understanding both the issues and process.[1]

The format should be prescriptive and identify non-discretionary content. This should include relevance to stated governance policies, distributional effects and impact on market entry. As in the BSC, reports should state for all codes that the Code is given effect without undue discrimination between Parties or classes of Party, but that due discrimination can be appropriate subject to revealing the supporting analysis.

The code administrator's **role as a critical friend should be enforced and, if necessary, strengthened**.

We agree that there is more scope to further support smaller parties. The views we have received from the forums we run for both smaller independent suppliers and generators confirm that they do not perceive that the code administrators provide sufficient support in terms of ensuring that they are represented and kept informed.

In the few instances where smaller parties do actively engage or, even more rarely, bring forward a change proposal, they are expected to commit resource that they often do not have. The rules of the game have been set by large utilities but the small players are expected to follow the same norms, which is not reasonable. Code administrators need to develop better networks into companies and do more to keep relevant people informed. These activities include such things as knowing who to contact about a specific modification and understanding the fact that business models and priorities differ.

The code administrators should treat this part of their role as a priority and consult with participants on what they would find most useful. For example, webinars may be one way to provide information and updates in a time-efficient way for smaller participants.

Significant Code Reviews

We have supported the SCR route to implement changes to industry processes in a holistic manner, especially where industry efforts have not worked towards necessary change or where issues straddle different codes. There are clearly lessons to be learned from the experience to date, for example, the need for more feedback to industry during the process, and less reliance on technical working groups that are prone to capture by large players and vested interests.

Ofgem has suggesting including the options for it to have a backstop power to draft modifications in order to ensure that changes resulting in the SCR "can be implemented in the most effective and efficient way". In this case industry parties would be continued to be involved in its development and for panels to vote on recommendations.

We do not believe the power to draft modifications would in itself tend to improve the code modification phase of an SCR more than the current arrangements to direct a licensee to raise a modification. Ofgem can already specify what it wants to be raised. It is the scope and content of the modification itself and how it is subsequently developed that is more important. For example, the scope of the CUSC modification for CMP213 *Project Transmit TNUoS Developments* was broad in its wording and left much work for the workgroup in developing specifics. Arguably its task was made that much more complex (unnecessarily so) by also including charging solutions for island links and HVDC circuits.

By contrast the proposals raised for cash-out in P304 and P305 were much more specific and, as only one alternative proposal could be raised, this made the process more efficient in terms of progressing it through the process. However, there remains significant concern among important sectors of the market,

[1] We note work is underway to introduce revised governance into the Grid Code under GC0086 *Grid Code Open Governance,* which includes a number of the code governance review changes. Again, this should be developed in order to ensure as much consistency as possible with the other codes.

particularly independent suppliers and non-flexible merchant generators that, with the exception of the single imbalance price, the changes will systematically disadvantage smaller and one-sided players and have a detrimental impact on competition.

The power to draft modifications will not be an effective tool if it does not improve the quality of the outcome. Arguably the ability to draft modifications could provide a temptation for Ofgem to curtail discussions in order to make faster progress at this stage in the process.

Likewise the ability to direct a timetable could curtail the necessary analysis that should be undertaken by the workgroup. Ofgem says it has ongoing concerns about the quality of industry analysis on complex change, but directing a timetable has the potential to make any problems worse if it means that issues identified cannot be properly addressed due to time constraints.

In each case SCRs have taken longer than the indicative timetable under the code governance review. This is partly because it may have underestimated the level of analysis and resources necessary for delivery the complex reforms. But a compounding factor has been Ofgem's approach to engagement with the industry and its sometimes one-sided approach to the debate on issues with a reluctance to adapt or review in the face of industry opinion. Opposition is not always intransigence in the face of change, and we believe the regulator needs to better engage to understand legitimate concerns.

A long and complex SCR raises evident difficulties for smaller participants, particularly with regard to engagement. Ofgem has stressed that it is at pains to be transparent and inclusive in engaging with stakeholders in conducting the SCR, and there have been numerous workshops, seminars and consultations. These need to be targeted as carefully as possible to ensure that the right people are attending and to limit the amount of stakeholders time that is needed, for example through the use of webinars. There also needs to be more feedback during the SCR process so that stakeholders are kept fully up to speed with the regulator's thinking.

Charging methodology governance

We agree that including charging methodologies within code governance has been a positive move, enabling more parties to raise proposals and engage with the process. It also enables a standardised process that sits alongside those for other code modifications.

We are wary of introducing a formal pre-modification process in place of the current charging methodology forums, as this has the potential for increasing the length and complexity of the process without any obvious gains, as work may need to be repeated in the modification process. Ofgem mentions that the approach of network operators in some cases may impact users' willingness to use charging forums for further development before formally raising charging changes. This perhaps indicates that the effectiveness of the existing forum needs to be improved, through looking at the format, timing and attendance at the meetings. It could also be used to allow that those raising the modifications to retain ownership from the beginning.

Modification windows as suggested by Ofgem might enable better prioritisation and planning of changes. However, there is a danger that this will simply delay the date when a modification can be raised and therefore the start of the process.

Self-governance

We agree that the facility for self-governance has delivered some benefits in the code arrangements, allowing non material changes to be progressed more efficiently. It also allows Ofgem to focus resources on more material changes. In general these arrangements appear to work without controversy and the facility to appeal any decision by a panel that a proposal should be self-governance provides an appropriate route for any party that is dissatisfied. In addition the fast track self-governance process, where implemented, has provided a proportionate route for very minor changes.

We consider the self-governance criteria set out in the licences are not inappropriate, though we would like to see code administrators and panels being bolder in taking on more responsibility. However, there are unhelpful and unnecessary variations in the use of the self-governance mechanism between codes. This arises because industry was invited to develop its own proposals on Panel and voting arrangements and

submit them to the regulator for approval. One anomaly, for example, is DCUSA does not include fast track self-governance because the code does not provide for Panel decisions.

As a minimum, differences in self-governance processes should be ironed out where possible and DCUSA modifications brought into line. While minor inconsistencies between codes may not be significant individually, in combination they act to put smaller parties that do not have the resources to become expert in the processes of each individual code at a disadvantage. Of course, a single code administrator (or design authority) would enable consistency and probably greater autonomy on the part of panels. Additionally, the onus should be on parties to show why any matter should be determined by the Authority rather than to make the case for self-governance.

Our responses to the consultation questions are set out in the attachment.

We would be delighted to clarify any aspect of this response, and please let me know if you would like to discuss it further.

Nigel Cornwall

Question 1: Do you consider the governance changes introduced under CGR and CGR2 have been effective in improving the code governance arrangements. In particular considering the efficiency and effectiveness of code change, the ability for large-scale reform to be implemented, and the accessibility of the arrangements for smaller/newer industry participants and consumer representatives?

The code governance reviews have provided greater consistency over the codes through the Code Administrators Code of Practice and introduced some useful new elements, including independent panel chairs, send back procedures, self-governance and SCRs.

SCRs have provided a route for large-scale reforms to be implemented but the execution has proved time-consuming and difficult for each of the three times the process has so far been employed. This has been for a number of reasons, which have been partly to do with the nature of the process - these are complex industry changes and therefore to some extent each one will be a one-off - but also to do with the way that they have been managed by Ofgem. For example differences of view, including between Ofgem and industry, on what is the right way forward, for example on the appropriate demand-side response mechanisms in the gas SCR, arguably made the process much longer than it needed to be.

As a general comment, there needs to be much more meaningful engagement, as currently engagement can appear one-sided and focused on expectation management. A more balanced assimilation of industry feedback is required and avoidance of a "pick and mix" approach to responses.

The arrangements for smaller/newer industry participants are still inadequate as these parties are still not properly supported through the code change process. Please see Question 2 below.

Question 2: Do you agree that there is a need to consider further reforms to the industry code governance arrangements? If so, what issues do you consider should be addressed, and what possible solutions do you identify?

The code governance arrangements should be further reformed as a regulatory priority. In particular we think the following are needed:

- further harmonisation of the arrangements between codes, including independent panels and alignment of processes where possible;
- further support to enable smaller parties to access the code arrangements effectively through more initiatives on behalf of code administrators, for example specific contacts within code administrators for particular modifications across codes (similar to the BSC), webinars to provide updates; and
- better quality analysis which focuses more effectively on the distributional impacts on code parties and gives more weight to the impact on new entrants and non-traditional business models. We note Ofgem's view not to re-open the issue of aligning code objectives with its objectives but the desire to include more information on the impacts of modifications on consumers, which should be considered further. This should be included in the terms of reference for workgroup deliberations.

We would also support consideration, as suggested by Ofgem, of whether code panels, code administrators and the wider industry can work more strategically to improve the code modification process, for example through a forward work plan for the year. As changes are raised on an ad hoc basis, this would probably need to be taken forward in tandem with a change window.

The criteria for determining which changes should receive priority treatment in these circumstances will clearly be critical and will also require cross code working where changes can affect more than one code. Clearly any such arrangements would need to be flexible to circumstances and the need on occasion for urgent changes otherwise there is the danger that needed modifications will be delayed. The antithesis of this is the current BSC Panel strategy, which states that the primary objective of the body should be to maintain the BSC arrangements in their current form.

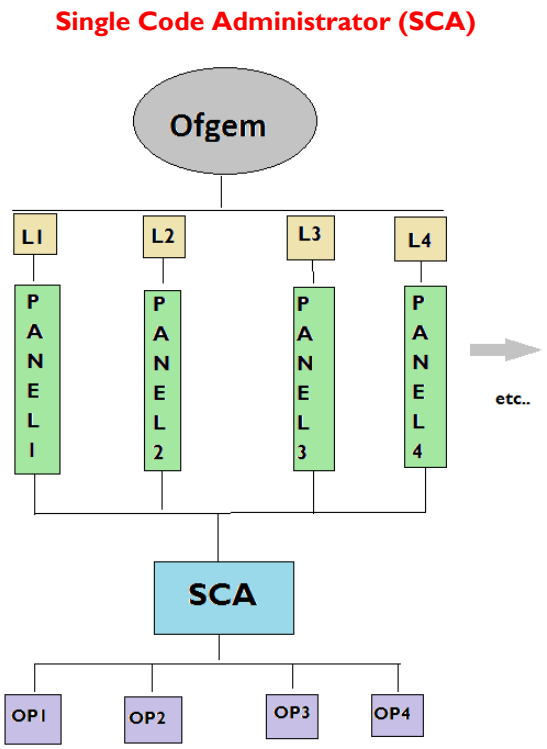
Ofgem has suggested that reform to Panel composition and improvements to working group arrangements may be needed to mitigate any risk that larger parties may have a greater influence/input into the code

process. We agree with this suggestion. The move could include all workgroups having an independent chair and possibly requiring that independent and impartial expertise is appointed to the workgroups in certain circumstances. We would welcome further consideration of these ideas.

Question 3: In addition to a post implementation review of our CGR reforms and potential changes discussed in this letter, are there any other areas of industry code governance that should be considered in this review?

There is a strong case for a rationalisation of code administrators, with one code administrator managing change processes for all the codes. With a common set of procedures it can be more focused on acting as critical friend, on identifying where there are cross-code implications and on ensuring that code changes are progressed efficiently.

Our proposal for the new structure is set out in the diagram below.



Under this structure the Single Code Administrator (SCA) would provide services to all the industry codes including both gas and electricity on a consistent basis. The licence obligations creating obligations to have the codes on the establishing licensees and then the obligations on other licensees to comply with them could remain as is.

It would be governed by a set of principles, as the separate code administrators are currently, which would include the requirement to act as a critical friend. It would operate using best practice procedures which are consistent between the codes and would report on activities consistently across the codes through key performance indicators.

The SCA would be organised into different operating areas (OP1,2 etc) with delivery bodies such as Elexon, Xoserve etc in the diagram above.

In the longer term we see the governance of industry codes under a design authority separate from the regulator. The design authority would have strategic priorities set by government and set out in legislation but would have the mandate to make binding decisions on rule changes, supported by the code administrator. A similar arrangement is currently in operation in Australia where the Australian Energy

Market Commission has the power to amend market rules and operates in accordance with a set of strategic priorities.

This would leave the regulator able to carry out significant reviews in order to bring about major change but would separate it from the day to day decisions on the detailed rules. The design authority could provide advice to government and would prioritise its tasks according to resources, with key performance indicators set for reporting, for example progress on work programme, expenditure against budget, and engagement with stakeholders.