

Energy Codes Review: Terms of Reference

Context

While the energy sector is experiencing a period of unprecedented change, many of the rules and practices¹ governing it were designed several decades ago for an energy system and market that had yet to see significant growth in low carbon technologies or smarter, more flexible approaches. Many of these detailed rules are set out in industry-owned codes underpinning the operation of the electricity and gas networks, and the wholesale and retail markets.

Many in industry are critical of the existing system of codes and code governance, pointing out that it is:

- **Slow** to take decisions, with even simple decisions taking many years.
- **Reactive** to existing problems, rather than forward-looking in preparing the energy system for future changes.
- **Overly complex**, with the entirety of the codes estimated to run to over 10,000 pages and weighing 50kg. This is a barrier to new entrants and to innovation.
- **Resource-intensive**, leading to a lack of representation from smaller and/or newer parties.
- **Lacking coordination** between the different code bodies.
- **Fragmented**, with a large number of code panels and bodies which provides for a complex institutional landscape, making it difficult to take forward systemic changes to the rules.

As a result, there is a growing industry consensus that action is necessary in order to create a regulatory framework capable of delivering the changes that will be required to move to a clean, smart, and consumer led energy system, in line with the Industrial and Clean Growth Strategies.

Objectives

Government and Ofgem are launching a joint comprehensive review into the codes which govern our energy system.

The aim of the review is to consider options for improving the existing arrangements, including scope for fundamental reform. Previous reviews by Ofgem² have delivered notable improvements to code governance, but further changes appear to be necessary given the scale of ongoing industry change. We will revisit the CMA code governance remedies³ in light of the latest energy market developments.

¹ Overview of Industry Codes, Ofgem

<https://www.ofgem.gov.uk/licences-industry-codes-and-standards/industry-codes>

² Ofgem Code Governance Review site

<https://www.ofgem.gov.uk/licences-industry-codes-and-standards/industry-code-governance/code-governance-review>

³ Competition and Markets Authority, June 2016, Final Report

<https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf>

In addition to the codes themselves, we may also consider associated regulations, documents and processes where relevant. The review will consider how any changes can be made, including through primary legislation, if necessary.

Scope

The review will consider the entirety of the rules underpinning the electricity and gas networks, and the wholesale and retail markets⁴.

The questions to be addressed by the review include:

- **Purpose of Codes:** we will consider whether a code system is still appropriate for all the areas of rules in the energy system, and whether there is scope to handle some elements of codes differently – for example, in code guidance, commercial contracts, or consumer protection legislation. We will explore how a more risk-based approach seen in other regulated industries may apply to energy.
- **Content of Codes:** we will seek stakeholders' views on whether the content of codes is up-to-date, relevant and applicable, and whether and how it may be improved. We will explore the role that digital technology may play in this regard.
- **Governance of Codes:** we will assess the effectiveness of the current industry governance arrangements. In light of that, we will consider alternative models of governance and whether these may be more effective than the status quo.
- **Process of changing codes:** a key aim of the review is to develop a regulatory framework capable of delivering strategic, whole-system solutions in the interests of consumers. This means considering how we can make any new arrangements more forward-looking, rather than reactive.
- **Transition:** we will give careful consideration to the process of moving from our current code environment to the desired end state. We will need to develop a transition model which will ensure smooth running of markets, and minimise any transition costs.

Process & outputs

This review will work closely with ongoing policy work on the future of the retail market and a new approach to data⁵, given the close interactions between them.

We aim to consult on changes to the existing arrangements by summer 2019. The timeline for the introduction of any new arrangements will take into account wider market developments and seek to remain coherent with other reforms currently underway across the energy sector.

⁴ Balancing and Settlement Code (BSC), Connection Use of System Code (CUSC), Distribution Use of System Agreement (DCUSA), Master Registration Agreement (MRA), Grid Code (G-Code), Distribution Code (D-Code), System Operator - Transmission Operator Code (STC), Uniform Network Code (UNC), Independent Gas Transporter UNC (iGT UNC), Supply Point Administration Agreement (SPAA), Smart Energy Code (SEC).

⁵ <https://www.gov.uk/government/groups/energy-data-taskforce>

We will hold a series of stakeholder engagement workshops and webinars in early 2019. These will be held in London and Glasgow, with the details to be confirmed shortly on the review's website <https://www.gov.uk/government/publications/energy-network-codes-review>. Please sign up for the Ofgem RSS feed to be notified of any new publications and events by selecting the RSS Feed link at <https://www.ofgem.gov.uk/licences-industry-codes-and-standards/industry-code-governance>.⁶ We are also keen to hear from you at codereform@beis.gov.uk.

⁶ You can subscribe to the feed by cutting and pasting the URL into your feed reader or by clicking the URL if your web browser supports RSS. You may need to download the RSS reader.