



Consultation on reforming the energy industry codes

Written response by Shell UK

September 2019

Code Reform - Electricity Systems Team
Department for Business, Energy & Industrial Strategy
3rd Floor, Abbey 1,
1 Victoria Street,
London, SW1H 0ET

Industry Code and Licensing Team
Office of Gas and Electricity Markets
10 South Colonnade
Canary Wharf
London, E14 4PU

By email to: codereform@beis.gov.uk and industrycodes@ofgem.gov.uk

17 September 2019

Dear All

Consultation on reforming the energy industry codes

Shell UK welcomes the opportunity to respond to this consultation on reforming industry code governance (the **Codes Consultation**). Several Shell UK companies, including Shell Energy Retail Limited, Shell Energy Europe Limited and Limejump Limited, are subject to various codes. In addition, our employees have also sat on relevant code bodies and participated in various governance processes.

Shell agrees that a review is both necessary and challenging.

First, the policy framework is changing significantly. The Codes Consultation sits amongst a wider set of reviews, including the recent Flexible and Responsive Retail Market review and the forthcoming Energy White Paper. We likewise note that any reforms to code governance *"interact with wider questions of system governance, including the current split of*



*responsibilities across Ofgem, the system operator and Government.*¹ We welcome the confirmation that Government is considering this area and will be publishing a position paper on “system governance” in 2020.

Second, as the Consultation acknowledges, the industry is undergoing a significant period of regulatory and technological change, including the move to smart meters; faster and more reliable dual-fuel switching; market-wide half hourly settlement in electricity, and the changes made by Project Nexus in the gas market.

It is clear that policy, regulatory and technological change is continuing apace, and this needs to be more appropriately and rapidly filtered through into industry codes.

At the same time, the pace of change itself makes a clear review of code governance challenging: governance arrangements should ideally be tied to the market that develops rather than as an outcome in and of itself.

In some ways this comprehensive review may therefore be slightly prescient: it may make more sense for Government and Ofgem to consider a more phased approach to changing governance arrangements, and to make greater use of existing tools, such as the Significant Code Review process, to enact rapid change where this is required to enact a specific policy goal.

A final complexity is that codes are legal contracts between different participants in the energy market. Restructuring them wholesale may therefore be difficult.

Some governance structures appear to have developed from the need to have in place a legal entity who is able to procure services, while others are mandated by the nature of the processes set out in the code itself, e.g. a BSCCo is needed to carry out balancing services under the Balancing and Settlement Code (BSC). This does not mean these governance structures remain fit for purpose given evolving aims for the energy system, but it does require a very clear distinction between the different roles played by different parts of each Code, not all of which are strategic or can be easily reformed.

Taking all of the above into account, we set out below our initial views on the aims and proposals set out in the Codes Consultation:

Case for a Strategic Body

¹ Please see p. 48, Code Consultation.



- We agree that the industry codes should be reformed to ensure the delivery of a cost-effective energy transition.
- However, as Ofgem has previously acknowledged, the trade-offs between security of supply, sustainability and affordability can be difficult for any regulator to make.
- We therefore agree that there is a case for a strategic body to better transpose Government policy (and in the case of the net zero goal, legislation) into industry codes, and to appropriately direct trade-offs.
- This body should sit within and not conflict with the existing institutional framework. We agree that its objectives should be outlined in legislation, and it should be accountable to Parliament, government or another appropriate body (such as Ofgem).
- The strategic body should be separate from, and oversee the code management function, to ensure appropriate accountability. At the same time, we take it as read that industry and other impacted stakeholders will be feeding into the strategic direction and requirements as these are developed

Cost and complexity of the current process

- We do not agree that “industry led” is necessarily the reason why codes can be slow to change and overly burdensome to manage. The codes are complex and individual code modification processes can be resource intensive. There are currently around 200 live code modifications which is too much for any company to reasonably engage with. In some instances, we consider that industry codes are being asked to do too much, for example, where modifications result in a significant redistribution of value between market participants.
- It is also worth noting that “Code governance” is not necessarily a single set of mechanisms and more consistent governance may not of itself help with code complexity. The industry codes reflect the complexities of the systems, processes, technical and commercial challenges inherent in a coordinated set of systems - simplicity may not be possible in all cases, as we set out below

Empowered and accountable code management

- We believe the codes themselves should reflect strategic policy but not determine it.



- Code managers should be accountable to Ofgem or the new strategic body. Material changes to one or more codes can have significant cost impacts on code parties. These changes are paid for by consumers. We can envisage an appropriately managed means for a code manager to kick off an assessment of a change, potentially on behalf of non-parties if the costs aspect can be resolved fairly. Should such a change be material (defined to include e.g. requiring material participant system, process or other change at material cost), it could be escalated to the strategic body, as arbiter of whether such a change meets the statutory requirements/purposes, including but not limited to the energy transition
- There is scope to streamline and harmonise the roles, responsibilities and objectives of code managers (which are quite diverse) and ensure these appropriately reflect government policy. Code managers should be empowered to organise the modification ("**Mod**") process, develop mods and recommend mods for approval. Having said that we do not believe that all changes currently being progressed require a full code mods process.
- We also do not consider that code managers should propose OR approve mods.
- We do have doubts that the range of functions potentially ascribed to the code manager in the Codes Consultation naturally fit together as a group of functions deliverable through a contract mechanism or potentially within the overall designation of "code management", including new entrant support, pro-active change management, compliance assessment and enforcement. Some of these roles could be better split.
- We are still considering the specific options outlined in the consultation for future code management. We believe that the two options proposed do not cover all means which could work, given consolidation is not a goal in itself. We recognise that other models exist for an energy codes framework, including that proposed by the Competition and Markets Authority (CMA), which included a *licensed* code management function. Procuring a *code manager* and setting out in a contract with a, or the, relevant legal entity their functions and powers risks not providing the necessary accountability to that entity as well as for those impacted by its decisions on code management and change to and of the codes. Further, experiences of those participants subject to the costs of service provision in this context include many negative ones - delivery being delayed whilst charges still accrue and must be met. The benefits of a direct contract - to



manage non-performance - are not in place here and the proxies available do not quite work to plug the gap

- It also raises the question of what can and should be done should any arbiter, deciding between different views of a change, make a decision that adversely impacts a code participant. We would support appropriate appeal and review rights, which can build up a body of practice and decisions that guide all parties as the codes evolve and are encouraged to see that this is recognised in the Codes Consultation.

Managing scale change – the Significant Code Review Process

- Complex contracts tend to have complex change processes (from operational to system-based and significant). It is not clear code management as a function could address the challenges the industry has with scale change.
- We think an umpire is needed. This may mean that, for cross-code change, a code manager is not the most appropriate option to generate and prosecute change. Given the increasing numbers of parties to the codes (and those taking account of other codes if not party to them), scale change needs to be provided for. We consider the Significant Code Review (SCR) process post-Project Nexus - while costly and time-intensive - is a strong basis from which to develop this.
- We would be supportive of considering further the need to beef up the SCR processes and provide Ofgem itself with the powers, skills and resources needed to avoid having to contract for costly programme management support alongside developing an appropriate and robust industry and stakeholder participative model or models (depending on the changes);

Simplification and consolidation

- We agree that there is scope for simplification and consolidation of some codes.
- However, we do not see a benefit of merging gas and power codes, except in some limited areas (like the Retail Energy Code).
- Gas governance - and the gas industry itself - has already gone through a period of substantial change (including Project Nexus and the Funding Governance and



Ownership (FGO) process)². In addition, the issues identified in this paper are primarily on the power rather than the gas side.

- Whilst we think there is scope of consolidation of some of the detail of the codes, consolidation for its own sake may not achieve simplicity or shorter codes - simplicity can also be derived from a separate and scoped governance process managing specific codes, e.g. SMICoP. Government should fully interrogate perceived synergies before consolidating specific codes, and we would advocate a phased review.
- The Retail Energy Code (REC) was not the first solution for a code for change of supply/faster switching but emerged from the very real concerns of trying to include such processes within another code, the Smart Energy Code (SEC). While the SEC could absolutely benefit from concerted efforts to consolidate it down, some of the complexity comes from the many different functions it includes (e.g. security, communications, interfaces, ordering processes, AltHAN, etc.).
- Just as consolidated governance is not a goal in itself, simplicity in and of itself may not enable or support entry or interaction by parties or non-parties that beneficially disrupts the energy systems. Here Government should seek to give voice to non-participants whilst also ensuring that the costs of change to support innovative entry are fairly incurred across participants, including innovative entrants. We recognise that this may need to include innovation that may not be successful (however that is measured) and that it is also important to support credible tests and trials, as well as live environment tests and trials in pursuit of energy systems fit for the energy transition and beyond.
- We agree that a cross-code digital mapping approach is needed, in order to create an online, easily-accessible and searchable repository of indexed codes, with increasing groupings around themes as the market develops, e.g. as appears to be emerging with flexibility services. Such a system would manage code interactions and potentially support the raising of coordinated change proposals where an anchor proposal has been adopted following impact assessment.
- We note that Electralink has pursued this course for SMICoP (called CodeNavigator) and other administrators are considering doing so - given digital mapping is being taken up per code, it is possible that this important strand can be more fully supported as a transitional development as governance and management options are more fully worked up.

² The FGO review was commenced by Ofgem in 2013 ([link](#)), with the industry implementation phase completed in 2017 ([link](#)).



- Certain of the codes, e.g. the Unified Network Code in gas, are multilateral contracts between licensed parties. We would query whether these codes can fully be instruments of policy in the manner described in the Codes Consultation. In particular, it is worth bottoming out whether Government and Ofgem concerns are always linked to specific aspects of certain codes, e.g. meter splitting under the BSC, or are linked rather to horizontal relationships which may in fact need changes beyond the code(s) impacted, such as metering-related codes and agent relationships.
- In some cases, the role of multilateral contracts could be more usefully expanded, noting the party-to-party obligations which can help ensure the smooth delivery of service. A case in point is erroneous transfers of customers, where direct supplier-supplier enforcement would be a reasonable outcome to incentivise better processes. This may mean that the overarching processes designed to manage this could be scaled back.

Funding

- Each code currently has its own discrete administration/management and funding arrangements, including but not limited to charge controls and services where the provider is able to profit from service provision.
- Rationalisation to ensure cost recovery would, in our view be highly beneficial, given profit maximisation inevitably raises the question of conflicts of interest.
- We recognise that some reward, or gain share, may be needed for the provision of some new functions and services.
- The above issues may of themselves shape the means for governance, control and service provision.
- Whichever models are decided upon for further detailed consideration, accountability is key.
- Finally, we would conclude that, despite the need to reform the current costly code governance process, change is also far from cost-free. Project Nexus, for example, was introduced at significant cost and disruption to the industry, a feature of many large-scale programmes which should be considered should Government and Ofgem seek to make significant systems changes as a result of new Code Governance arrangements.



- The costs of change for industry stakeholders - and their customers - are significant amidst other costly and resource-intensive change programmes and must only be justified if outweighed by the benefits.

In conclusion, we welcome the intent of this consultation, but propose a phased and evidence-based approach to reform given the complexity of the current arrangements.

We look forward to working with BEIS and Ofgem as policy develops further.