

Code Reform – Electricity System Team  
BEIS

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16<sup>th</sup> September 2019

Dear BEIS & Ofgem,

**Ref: innogy's response to the consultation on reforming the energy industry codes**

Innogy Renewables UK Ltd, as a developer and operator of renewable generation located on both the transmission and distributed networks, and owner of Belectric Battery Storage Ltd welcomes the opportunity to respond to this consultation. This is a non-confidential response.

Questions 1-5

We agree with the four desired outcomes for the energy code framework. As an existing player in the market we experience frustrations over the complexity of the existing arrangements as well as the slow pace of change, lack of meaningful or consistent strategic direction and resource intensive fragmented decision-making

By way of example, the numerous proposals from Code signatories over the last 4 years, designed to help those who compete in the Capacity Market, have had the potential or consequence to cause significant damage to renewable generation which has been largely collateral damage. The cost to Innogy Renewables of attempting to keep on top of the volume of change proposals has been significant. For example, in addition to workshops for each CUSC modification (which according to the consultation averages 16 days), we have also needed to spend time assessing the impacts of proposals upon our business and the potential consumer costs, particularly as the workgroup reports rarely include a detailed impact assessment beyond a simple 'low', 'medium' or 'high' impact.

We also agree the scope of the reform as outlined in the consultation should encompass the relevant existing industry codes. However, it also needs to include licenses, the impact upon which would need to be considered to understand the inter dependences and avoid unintended consequences. Implementation of the European Network Codes will also need to be considered.

### Question 6-9

We have the following observations regarding the four areas which are being considered as facilitators of reform:

1. Providing Strategic Direction: We support that it would be helpful for the regulatory framework to be informed by the government's vision for the energy system. The vision should be stable and consistent with delivering ongoing investment in the energy market. Net zero should be front and centre in this vision.
2. Empowered and accountable code management: The Code Manager should be fully resourced to deliver a clear, logical and professional service across all the Codes. This includes fully assessing the impacts of change proposals on different network users and against the vision.
3. Independent decision-making: We agree that decision-making should be independent – which is reflective of today's arrangements where the Authority is the independent decision-maker. We do not agree with or recognise the assertion in the consultation that industry currently has control over decision-making. We would have reservations about the Code Manager making decisions about changes it has proposed as this would not be independent decision-making.
4. Code simplification and consolidation: We have some concerns that code simplification and consolidation could have significant commercial impacts on legally binding multi-party agreements and license obligations. Whilst the we support the reasoning behind the desire to carry out this task we caution against underestimating the resources required – including from existing code administrators, industry input/oversight and the significant legal input that would all be required to ensure that the amendments did not cause a change in legal or technical meaning.

We agree that both governance models could work in theory, however we support model 1. Model 1 introduces an element of independence for the strategic body while model 2 more closely resembles the structure today (where Ofgem have some strategic function via the Significant Code Review process).

We do not believe that the ESO is an appropriate body to take on the strategic function. This is way beyond the remit of their current role and has implications in that it is a private company. In addition, we do not believe that there is good reason for creating a new strategic body. The Authority would be better placed to take on this role – but it would require the statutory obligations of Ofgem to be refreshed to better support their role in the energy transition. A

review of Ofgem which published its conclusion in 2011<sup>1</sup> found that government and Ofgem should make some changes, not all of which have been addressed in the time since. In particular, an updated Strategy and Policy Statement was never finalized. The strategic body – whether it is Ofgem or not – should have core legislated policies such as net zero as a key driver of the vision.

The new governance models create new roles and responsibilities for code parties. More clarity is needed on exactly what the information in Tables 3 and 4 will mean in terms of obligations in practice.

#### Question 10-14

Innogy considers that how the strategic vision is developed, scrutinized and implemented is the most important consideration for BEIS and Ofgem in this consultation. We agree that the strategic plan should be robust, stable and reflective of government policy. Careful consideration needs to be given to who would be the most appropriate body to operate as the strategic function and how this strategic function is accountable to government, parliament or Ofgem such that it can be subject to appropriate scrutiny from stakeholders. A 1-3 year plan is too short to be meaningful or stable over investment timescales. Ideally the strategic vision would have both a short-term (1-5 year) roadmap and longer-term milestones (5-10 year chunks between now and 2050) which together provide a clear and tangible policy direction to encourage investment and engage the market to achieve net zero.

There will be several layers at play based on the descriptions in Chapter 3 of the consultation: 1) the strategic direction of government, 2) the strategic vision including deliverables to be developed/delivered as a result by 3) the strategic body. Exactly how these interact is key to the success of the strategic vision in attracting investment to the market, delivering net zero and protecting the interests of current and future consumers. The translation of the government's strategic direction to the strategic body requires careful consideration. For example, will the deliverables contained within the strategic vision resulting from this direction be consulted upon? Furthermore, the body with the strategic function must have a clear remit. For example, it must be prescribed how much influence or power the function would have over issues including carbon pricing or market mechanisms such as the Capacity Market / Contracts for Difference.

There have been numerous "strategic reviews" of the energy industry and its governance framework in recent years. For example, the "Electricity Market Reform" (EMR) strategic review of industry governance enshrined market rules in legislation with strategic direction residing with government (via the Secretary of State) with a role for the system operator as a delivery body.

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<sup>1</sup> [Ofgem Review – Final Report](#). DECC, July 2011.

The existing Codes have also been subject to reforms via the existing industry governance processes – either via government legislation (eg price caps) and changes to licensing (market making obligations).

We are currently in the midst of two Significant Code Reviews (TCR and the Electricity Network Access Project) being led by Ofgem which have proposed network charging reforms. The cost-benefit analysis associated with these proposals has been shown by several subsequent reports to be flawed, having focused on a very narrow set of assumptions and not including various feedback loops. These independent analyses have demonstrated that the proposals would actually hamper progress towards legislated net zero targets by limiting the deployment of low-cost new renewables<sup>2,3</sup>. The modelling in Ofgem's cost-benefit analysis also failed to accurately reflect current government policy regarding CfDs and used incorrect carbon figures. As a result, it has required two 'add-on' consultations which still do not solve the problems. This lack of strategic focus is very likely to cost consumers money in the long run<sup>3</sup>. We therefore absolutely agree with the assertion in the consultation document that these SCR processes are not going to deliver wide-ranging and strategic reforms.

What is clear from this example is that whilst some kind of strategic function does exist already, the evidence shows that it is not working effectively towards achieving a broad coherent objective or even legally binding decarbonisation targets (indeed, it is undermining these in some cases) or fully capturing the consumer impacts of proposed reforms designed to accommodate the changing landscape as a result of the energy transition. This needs to be rectified as soon as possible.

We do not believe that there is a strong case for creating a new strategic body. As set out earlier the strategic function could be delivered by an independent, arms-length function sat within Ofgem, with independent decision-making through GEMA. Such a strategic function would need to have regard for legislated policy, including the UK's commitments under the Paris Agreement, net zero legislation and carbon budgets to be underpinning all its decision-making. Achieving these commitments at best value for the consumer should be the primary focus. On 1 May 2019 the UK Parliament approved a motion to declare an environmental and climate emergency. The costs of the climate emergency will only escalate over time<sup>4</sup> costing the consumer more money if actions are delayed – which is not good value for money.

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<sup>2</sup> [Reforms to network charges: The Targeted Charging Review and its implications](#). Aurora ER, May 2019

<sup>3</sup> [Ofgem's Targeted Charging Review Impact Assessment](#). A review by Oxera, April 2019.

<sup>4</sup> The Economics of 1.5°C Climate Change. S. Dietz, A. Bowen, B. Doda, A. Gambhir, R. Warren. Annual Review of Environment and Resources 2018 43:1, 455-480.

Questions 15-26

We are in agreement that the Code Manager function could provide a more broad-thinking and forward-looking aspect than the existing Code Administrators do, which would support the more strategic future that is being envisaged for the Codes. The roles of Code Manager and Code Administrator are very different.

Chapter 4 offers some good insights into why model 1 could be the preferred option. For example, we support a route of appeal being available to code parties by the code manager. The consultation suggests this appeal could be to the strategic body – who in model 2 would be the same integrated body. This is not desirable and represents a conflict of interest to independent decision-making. We also do not agree that the code manager function should have decision-making powers (with the possible exception of changes for ‘housekeeping’ purposes). The code management function should operate independently as an administrator of the code management process – a role which should include developing changes proposed by relevant parties, analysis, legal drafting and undertaking impact assessments.

It is very important for the strategic vision to inform and drive code development. The strategic body could maintain strategic oversight of the overall market design and architecture whilst the code manager is responsible for code administration and delivery of changes in an efficient and professional manner. We strongly support code parties retaining the right to propose changes for consideration, as they do today.

The code manager function should be accountable to the code parties regarding effective and efficient administration of the code and code changes. Decisions on code changes should be made by an independent body (eg GEMA) and one of the key objectives of code changes should be to better align the codes to the strategic vision.

The consultation document suggests that the current framework is accountable to industry. We do not agree or recognise this assertion. The code change process is subject to oversight by Ofgem under the legislative framework and enforced through licences.

As part of this code governance review Innogy suggests that the nature of each code is considered in the context of reforms. For example, multi-party agreements (eg BSC, CUSC) will require direct input from the code parties. Other codes are technical documents with compliance requirements (eg Grid Code).

The code manager should be established under a relevant licence. This is the case for most of the current codes, with the notable exception of the EMR regulations and rules. The code manager function, including roles and responsibilities, could form part of the code itself.

A competitive tender process may be appropriate if the code manager role is specified appropriately within the code itself. This would need to clearly set out expectations for standards of performance and value for money criteria. Any tender process would need to focus sufficiently on performance and not just on delivering lowest cost (because lowest cost is not the same as value for money). A service delivered on a shoe-string would be unlikely to offer value for money when considered in terms of its overall impact to the market or to attract and retain suitably qualified expertise to effectively deliver its role.

Code management should be funded by the parties to the code through cost reflective charges and, if appropriate, under the price control of the relevant licensee subject to the code administrator meeting relevant performance standards.

#### Questions 27-31

In considering options for code consolidation we consider it essential that the nature of each relevant code is considered. For example, the BSC and the CUSC are multi-party agreements but the Grid Code is a technical document requiring compliance. There will undoubtedly be cross-code and probably licensing implications of changes in any consolidation process, and once this is looked at in detail it will be more appropriate to comment on how many codes there should be.

The example given in the consultation document regarding National Grid's simplification of a section of the CUSC does not, insofar as Innogy are aware, consider whether the simplified text retains the same legal and technical meaning as the original text. This consideration will be crucial to the process of reform and will undoubtedly be a resource-intensive process (as industry will want to be involved to protect its own legal status).

#### Questions 32-34

We agree that code information should be available electronically and that digitalization is a good idea as long as it can be kept appropriately up-to-date.

The current compliance arrangements based on legislation, licences and multiparty agreements should be maintained. This ensures that the compliance arrangements are proportionate, manageable and enforceable.

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Yours sincerely,



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