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Dear Sir/ Madam -

CONSULTATION ON REFORMING THE ENERGY INDUSTRY CODES

We welcome the opportunity to respond to the above consultation.

Gemserve has extensive knowledge and experience of energy industry codes in our capacity managing the MRA (Master Registration Agreement), the SEC (Smart Energy Code), the IGTUNC (Independent Gas Transporters Uniform Network Code) and the GDAA (Green Deal Arrangements Agreement). We also have experience from across the wider energy market and other regulated industries.

Gemserve's investment in people, skills and knowledge can make a major contribution to code reform and enabling the energy transition. We have published 4 thought leadership papers on code reform over the past two years. The [most recent](#) was in July 2019, and we are pleased that many of our thoughts align with the proposals in your consultation document.

We have provided a detailed response to the questions in the consultation document at the Annex. In summary our views are:

- While the current code governance arrangements have been effective in supporting market developments since deregulation in the 1990s, we agree the system of energy industry codes is now outdated – being reactive, complex, and lacking coordination - and should be modernised to further support transformation of the energy market and deliver better consumer outcomes.
- We agree with the need for a new strategic direction function and would like this to be performed by Ofgem, building on its existing cross-industry coordination and regulatory responsibilities. Ofgem should appoint code managers through competitive procurement to drive value for money and desired outcomes, either through a contract or licensing relationship.

- We note the proposed shift in accountability of the code manager from industry to the strategic function. The ways in which industry parties engage with the decision-making process under this model should be strengthened and we offer views on how this can be achieved in our answer to Q.9 in the Annex.
- The funding needs of code managers should continue to be met by parties to the codes, with a consistent and transparent mechanism applied across all codes. We believe this should include provision for innovation funding which is necessary to drive continuous improvement. The review should also consider payment by results models and other incentives.
- We believe Model 1 for the institutional framework would deliver the reform objectives while maintaining closer industry engagement with least upheaval and cost. Bringing together the strategic guidance and code management into a single body as proposed under Model 2 risks that organisation becoming overwhelmed, constructs a single point of failure and raises concern over conflicts of interest between the two roles.
- The new REC (Retail Energy Code) is a step in the direction of Model 1 and we would like it to become an exemplar code. As such it's important that the design and operation of the REC is consistent with the direction of travel set out in the code review.
- Successful implementation of the reforms will require a significant change programme with delivery risks. To mitigate these, we suggest that the change programme begins with the new REC and then expands into the other codes and code managers.
- We are concerned with the proposal that a code manager must have no affiliation with an existing party to the industry codes as a way of ensuring independence. This goes too far in our view and would likely rule out many capable organisations from being a code manager. As is recognised in the consultation, there are many ways of ensuring independence of the code manager (including the current arrangements under which Gemserve operates) and we consider that these should be explored further.
- Digitisation of codes (and other market rules) can significantly reduce the regulatory burden for market participants and drive efficiencies across the code manager function. Indeed, Gemserve is already piloting a digitised version of the Smart Energy Code. Digitalisation should go hand in hand with a single market portal to enable easy access to the rules and other services, something Gemserve has long advocated.
- Some consolidation of codes by industry activity could drive efficiencies but this must go hand in hand with a rationalisation of the rules, their digitisation, and a single market portal. Consolidation in isolation will not drive the desired outcomes.
- There should be a market Performance Assurance function providing oversight and monitoring of industry compliance with the code, and this should be performed by the relevant code manager. There should also be performance monitoring of code managers themselves undertaken by the Strategic Function.
- We would encourage the Review to consider how a risk-based approach to market governance could be introduced as a way of reducing the administrative and regulatory burden.

- Finally, more is needed on the costs and benefits analysis of the different options and we would like to support the Review Team with this. Costs and benefits should be properly examined before options are decided.

We would be delighted to discuss our response with you and engage in further consultation on this important issue.

Yours faithfully



Trevor Hutchings
Director of Strategy and Communications

GEMSERV RESPONSE TO THE CONSULTATION ON REFORMING THE ENERGY INDUSTRY CODES

Gemserve's response to the consultation questions is set out below. We have grouped together some questions where the issues are overlapping.

1. Do you agree with our four desired outcomes for the code governance landscape by the mid-2020s? Yes/No/Don't know. Please explain.

If you disagree, please explain what you consider the outcomes should be.

Yes.

2. Do you agree with the problems we've identified (in chapter 1 – Background – and in later chapters), and that they present a persuasive case for reform of the current framework for energy codes? Yes/No/Don't know. Please explain.

3. Do you have additional evidence on the performance of the current framework?

We agree with the case for reform, but there should be acknowledgement that the system has served participants and consumers well since market opening in the late 1990s. Over that time the market has changed significantly with, for example, over four million switches now undertaken each year, coal has all but been removed from the system, and renewables account for a third of electricity production. The number of suppliers has increased 10-fold and there are high levels of confidence in energy security. That said, the climate emergency and advances in technology mean that current governance arrangements must modernise to support a well-functioning energy system going forward, and we believe that government intervention, working closely with industry and consumers, is needed to bring this about.

4. Do you agree with our proposed scope of reform? Yes/No/Don't know. Please explain. If not, which additional codes or systems do you think should be included/excluded?

Yes, but we think the Review should consider how the good ideas which have been proposed could apply to all rules of market participation. For example, applying a risk-based approach is as applicable to codes as it is to supply licensing and other market regulation. The same goes for digitisation. Likewise, the ambition for a single web portal through which market participants can access all market requirements – something Gemserve has strongly advocated – should include all market requirements and these clearly stretch beyond codes.

5. Are there any codes or systems that we should only apply a limited set of reforms to? Yes/No/Don't know. Please explain.

No. We believe the reform should take a holistic approach given the interdependencies across codes and systems as well as the need to reduce regulatory burdens and improve the market participant and consumer experience in the round.

6. Do you agree that the four areas for reform are required? Please provide reasons for your position and evidence where possible.

Yes, but please note our comments below regarding re-balancing decision-making away from the industry, and on the limitations of code consolidation.

7. Do you agree with the two broad models outlined? Please provide reasons for your position and evidence where possible. – further detail can be found on each model in the chapters that follow.

8. Which model do you believe will best deliver on our desired outcomes? Please explain. NB: – further detail can be found on each model in the chapters that follow.

We believe Model 1 would deliver reform objectives while maintaining closer industry engagement with least upheaval and cost. The new REC (Retail Energy Code) is already a key step in the direction of Model 1 and can be an exemplar code in this regard.

Model 1 could build on Ofgem's existing capabilities and responsibilities for regulation and codes but would require additional investment in the necessary capabilities to support this. For example, in strategic analysis covering technical, commercial and market issues, in cross-industry co-ordination activities, in oversight of code managers and delivery of change programmes, as well as existing compliance and regulatory activities.

The code managers should be responsible for contributing evidence to support Ofgem's strategic responsibilities, for formulation of delivery plans, and for delivery of the agreed strategies. This would allow them to focus on decision making and delivery performance.

Bringing together all functions into a single body as proposed under Model 2 would involve significant upheaval, and risks that organisation becoming overwhelmed leading to market disruption and poor consumer outcomes, outweighing any efficiencies that might be possible through consolidation into a single body. There would be a tension and potential conflict of interest between setting strategic direction and its role as code manager and we believe these functions should be kept separate. Furthermore, it is not clear whether it would drive any cost or operational efficiencies and there is a greater likelihood of delay as it would need a significant set up period.

9. Do you agree with the changes to the role of code signatories we are proposing?

The key issue here is the proposed shift away from industry self-governance (where the rules are largely decided upon by industry panels) to one where the strategic function and/ or code manager alone approve modifications. This risks losing buy-in, market insight and technical expertise, and while the code manager should be able to provide much of this, we would like to see the following safeguards:

- a) The code manager and/ or strategic function is required to consult industry and take account of their views (or explain why not) before approving modifications;
- b) The performance of the code manager should be regularly assessed under a performance monitoring regime;
- c) There should be cost control mechanisms agreed with the strategic body to ensure the code manager does not simply make work for itself in the absence of industry control; and
- d) A dispute/ appeals mechanism in needed whereby industry parties can raise concerns over decisions by the code manager.

10. Do you agree there is a missing strategic function for codes development in the energy sector and that introducing a strategic function with the responsibilities outlined in chapter 3 is the best way to address the lack of strategic direction? Yes/No/Don't know. Please explain. Who is best placed to fulfil the strategic function and why?

11. Do you agree with the objectives and responsibilities envisaged for the strategic function, and are there any additional objectives or responsibilities the strategic function should have?

12. How may this new function potentially impact the roles and responsibilities of other parts of the framework? Do you foresee any unintended consequences?

13. What are your views on how the strategic direction should be developed and implemented (including the option of establishing a strategy board to aid engagement)?

We agree that a strategic direction function should be introduced setting out a vision and objectives for the energy market, including clear delegated responsibilities for code managers and helping ensure a joined-up and more efficient approach to common market goals. We believe this function should be performed by Ofgem, with additional and ring-fenced funding for this purpose, and reporting requirements to ensure transparency and accountability for clearly defined outcomes. We believe the ESO is not sufficiently independent and a new body would introduce an additional governance layer to the market, and cost, and would face a particular challenge in attempting to reconcile views of government, the regulator and industry.

14. Do you think that the scope of the strategic function should be limited to taking account of the Government's vision for the energy sector and translating it into a plan for the industry codes framework, or are there other areas it should address (for example, impact on vulnerable consumers)? Yes/No/Don't know. Please explain.

The strategic function should also consult on and take account of industry and consumer views.

15. Do you agree that in addition to the current responsibilities that code administrators have, that the code manager function should also have the following responsibilities?

- a. identifying, proposing and developing changes (analysis, legal drafting, etc.), including understanding the impacts;
- b. making decisions on some changes, or making recommendations to the strategic body; and
- c. prioritising which changes are progressed.

Yes/No/Don't know. Please explain.

Yee. On point (b) we think the code manager should make decisions on changes but please note our answer to Q9 on how industry parties can engage and influence in this process.

16. What is the best way to ensure coherent end-to-end changes to the codes and related systems? For example, is it through having end-to-end code and system managers?

We think that end to end change design starts at the strategic level, where principles for end to end approaches can be set. This can then be implemented through a co-ordinated approach implemented by code managers and their system providers.

17. Should the approach differ on a case-by case basis (i.e. depending on the code or system in question)? Yes/No/Don't know. Please explain.

We are supportive of the principle of code managers being responsible for the end-to-end code change and related systems change. It will be important for the strategic function to hold the code manager to account for procuring systems with appropriate flexibility and which offer the best value for money.

18. Do you agree that the code manager function should be accountable to the strategic body and that this should be via a licence or contract? Yes/No/Don't know. Please explain.

Please note questions 19- 26 only apply in respect of Model 1 (code managers and a strategic body).

19. Are there more effective ways that the code manager function's accountability to the strategic body could be enshrined other than in a licence or contract? Please explain.

We agree that the code manager should be accountable to the strategic body on the basis that the strategic body is Ofgem as we have noted earlier. We think the code manager function should be procured through a fair and open competition and held to account through either a contract or licensing. We think an element of 'payment by results' or other model should be explored as a way incentivising performance of the code manager.

20. Do you agree that we should not consider further a model whereby the code manager function is accountable to industry? Yes/No/Don't know. Please explain.

See our response to question 9.

21. Do you have views on whether the code manager function should be appointed following a competitive tender process or other competition? Yes/No/Don't know. Please explain.

Yes, through a competitive tender process or other competition in order to help ensure value for money and drive innovation.

22. Do you think the code manager function should be established by the strategic body creating a body or bodies? Yes/No/Don't know. Please explain. If the code managers were established in this way, would we need to consider any alternative approaches to funding or accountability?

Yes/No/Don't know. Please explain.

No. Rather than setting up a new body, code managers should be appointed through competitive tender as noted in Q21 above.

23. In terms of establishing/choosing the code manager function, do you agree that we should not consider further:

- a. requiring an existing licensee to become the code manager; and/ or**
- b. requiring a licensee (or group of licensees) to create the code manager? Yes/No/Don't know. Please explain.**

We agree that this should not be considered further.

24. What would be the most effective way to ensure the code manager function offers value for money (for example, through price controls or budget scrutiny)? More broadly, what is the right incentive framework to place on the code manager function? Please explain.

We believe a combination of the following should help drive value for money:

- a) Procuring the code manager through competitive tender, with reasonable re-procurement frequency.
- b) Having more than one code manager operating in the market and therefore an opportunity to compare costs and service and ensure competition.
- c) Payment by results and other incentive models.

It is important not to confuse value for money with 'for profit' or 'not for profit' business models of the code manager. Both can deliver value for money which should be determined according to cost and service.

25. Are there any factors that:

- a. would stop parties (including code administrators) from becoming a code manager?**
- b. should prevent parties from becoming a code manager (e.g. do you agree that licensees should not be able to exercise control of the code managers)?**

Agree that licensees should not be able to exercise control of the code manager. Actual and perceived independence is important and the avoidance of any current or potential conflicts of interest.

We are concerned however with the proposal that a code manager must have no affiliation with an existing party to the industry codes as a way of insuring independence. This goes too far in our view and would likely rule out many capable organisations from acting as code manager. As is recognised in the consultation, there are many ways of ensuring independence of the code manager and we consider these should be explored further. For example, Gemserve operates under a Board of Directors which is independent of its shareholders and Board members do not sit on the Boards of the industry companies accountable for the codes that Gemserve manages. Oversight by the Strategic Body can also help ensure independence and code managers could establish independent panels to advise on modifications.

26. How should the code manager function be funded (for example through licence fees or by parties to the code(s))?

The funding needs of code managers should continue to be met by parties to the codes, with a consistent and transparent mechanism applied across all codes. We believed this should include provision for innovation funding which we believe is necessary to drive continuous improvement.

27. Are there any quick wins that could be realised in terms of code consolidation and simplification?

As noted below, digitisation of the codes can reduce complexity and the regulatory burden on market participants and can be brought forward quickly as indeed Gemserve has started to do through the digitisation of the SEC.

28. How many codes would best deliver on the outcomes we are seeking under these reforms?

29. Which option (one code manager versus multiple) would best deliver on the outcomes we are seeking under these reforms?

30. Which of our consolidation options would best deliver the outcomes we are seeking to achieve? Please provide evidence for your examples.

Some consolidation of codes by industry activity (Option B) with a different code manager for each (Option B) could drive efficiencies but this must go hand in hand with a rationalisation of the rules, their digitisation, a risk-based approach and a single market portal. Consolidation alone will not drive the desired outcomes.

We would like the Review to consider more fully a shift towards a risk-based approach. There would be minimum standards for all market participants, many of which could be principle based, with any additional rules applied according to the risk that they pose to the market. In practice this could mean a higher bar to market entry, for example to safeguard consumers if there are weaknesses in a new entrant's business model, as well as additional operating requirements, for example, more frequent reporting obligations and financial guarantees. Overall this approach would reduce the regulatory burden and costs on participants. This approach would be for the code manager to perform and it should be clearly articulated via objective setting and delegated authority from the strategic direction.

31. Do you agree that the codes should be digitalised? Yes/No/Don't know. Please explain.

Yes. In order to provide an enhanced user experience and to reduce the regulatory burden, codes should be digitised. This would enable market participants to undertake a 'smart search' meaning that the web portal is able to present only the information that is relevant to a certain user or use case. Furthermore, the technology can support more efficient changes to codes by highlighting all other areas which are impacted when a change is made to a single section or rule. It can also be used to facilitate industry collaboration on proposed modifications reducing the need for industry meetings. Gemserve has proven this technology through the ongoing digitisation of the Smart Energy Code

32. What role should industry have in monitoring code compliance or making decisions on measures needed to address any identified non-compliance?

33. Which of the two models we propose would better facilitate effective monitoring and compliance arrangements? Please explain.

34. With Model 2 - integrated rule-making body - should the IRMB have responsibility for imposing measures (where a party is non-compliant with the code) or should this be for another organisation? Please explain. Please note this question only applies in respect of Model 2 (integrated rule-making body).

There should be market level Performance Assurance providing oversight and monitoring of industry compliance with the code (including issuing sanctions for non-compliance) and of market outcomes including consumer expectations. We believe this Performance Assurance function should be

undertaken by the relevant code manager, with the Strategic Body being a route to appeal where sanctions have been imposed.

There should also be performance monitoring of code managers themselves, for example against code requirements, KPIs and of contract and/ or licensing obligations. This should be carried out by the Strategic Function with support as necessary.