

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

16th September 2019

Dear Industry Code and Licensing Team,

Consultation on Reforming the Energy Industry Codes

I am writing on behalf of ESP Utilities Group ("ESPUG") (comprising the licenced companies ES Pipelines Ltd, ESP Connections Ltd, ESP Networks Ltd, ESP Pipelines Ltd and ESP Electricity Ltd). We welcome the opportunity to respond to BEIS and Ofgem's "Consultation on Reforming the Energy Industry Codes" ('the Consultation Paper'), dated 22nd July 2019.

Overall, ESPUG is supportive of the objectives of the review. We also broadly agree with the issues with codes identified in the Consultation Paper. This includes the problems of fragmentation, complexity and lack of incentive to change. ESPUG notes however, that some complexity is inevitable as industry systems reflect the integration of different parts of the energy supply chain such as generation, transmission, distribution and supply.

There are some practical design issues we see need to be resolved if either models 1 or 2 are chosen. Crucial to the role of code administration is neutrality. Whether the code manager or the Integrated Rule Making Body (IRMB) is chosen, the industry needs to be confident it would not operate in its own interests above industry or Government as there may be incentives to do so. The second design issue is that under either of the options, there will be an asymmetry of information, expertise, and knowledge between practicing industry parties and the code administrator or IRMB. This is likely to widen over time; the code manager would be an expert in code, and the industry's processes.

In the long run, it will be desirable to amalgamate the industry codes into a single entity and we have confidence that this can be achieved. We expect any lessons learned from the Retail Energy Code consolidation to go a long way in providing a guideline for this purpose.

If you wish to discuss any of the issues raised in our response or have any queries, please feel free to contact me on 01372 587500.

I confirm that this letter may be published in the public domain.

Yours sincerely,



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Appendix

1. Do you agree with our four desired outcomes for the code governance landscape by the mid-2020s?

Yes, the desired outcomes are well aligned towards the interests of energy consumers while simultaneously encompassing the commercial interests of industry parties, both existing and prospective.

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, we agree that the problems identified present a case for reform, particularly the challenge of fragmentation and lack of coordination between codes. Though the CACoP seeks to mitigate the issue of cross-code coordination, this has not always been perfect.

We would like to note that the issue of codes being reactive to existing problems instead of being forward looking and anticipating changes to the energy system is one that is likely to persist. New and smaller market participants are likely to be hesitant to implement changes that are not mandated by the regulator and which may not provide tangible benefits, realised or accrued, in the short term.

4. Do you agree with our proposed scope of reform? If not, which additional codes or systems do you think should be included/excluded?

Yes, we agree that the scope of reform should cover the outlined codes as well as general code governance.

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

We broadly agree with the areas of reform for strategic directing, accountable code management and code simplification. However, rebalancing decision making away from industry could potentially cause issues such as undue regulatory burden, slow uptake of change and erroneous changes that do not adequately consider the impact on industry and consumers. There is also an increased risk of disengagement, particularly from new entrants, due to a lack of decision making power.

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.

Yes, we broadly agree with the proposed models. The current industry codes are reactive to innovation and slow to change. They also lack a clear strategic steer that aggravates the issues identified. A strategic function, either standalone or integrated, would be able to implement and communicate a strategic direction while harmonising action across code signatories for the betterment of code governance.

8. Which model do you believe will best deliver on our desired outcomes? Please explain.

We do not see a significant difference between the two models and believe both could be capable of delivering the desired outcomes. The majority of the reform will come in the form of the direction and oversight of the strategic body which currently does not exist in the code landscape.

We note that the key difference between the models is that model 2 integrates the IRMB with a strategic function. Though this may bring the benefit of greater coordination, it could

potentially lead to inflexible and concentrated decision making with potential for issues relating to accountability and expertise to arise.

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

Code signatory input notwithstanding, we do not see the merit in removing signatories' decision making abilities as outlined in our comment to question 6.

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? Who is best placed to fulfil the strategic function and why?

Yes, we agree that the current codes lack a strategic direction and are reactive to innovation in the energy industry. For this reason, introducing a body with the power to make strategic decisions is essential in reforming the codes to act in a forward-looking manner and to be more malleable for the purpose of accepting significant change and innovation in the future.

We would gravitate towards the strategic function being provided by Ofgem or an independent body. Ofgem is best placed to provide an overall steer and currently have certain duties and interactions with the codes. An independent body would also be able to function in the role but would add complexity in the short term. Additionally, an independent body serving the strategic function adds an extra layer of communication that is not required at the outset.

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?

Yes, we agree with the responsibilities listed. We would note that an overarching body that provides a strategic function could potentially take on a growing number of responsibilities. Furthermore, it will be necessary to concretely define what responsibilities the strategic function will undertake and what roles would be better suited to the code manager to prevent an overlap of responsibilities and ensure that both roles complement each other.

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

We believe the greatest impact on current roles would be that the strategic function shares several responsibilities that code parties currently fulfil, including, but not limited to:

- Making strategic recommendations to Ofgem and BEIS
- Assuming accountability of the code manager
- Taking forward and developing complex code changes

An unintended consequence of implementing a strategic function could potentially be the stifling of code party engagement on innovation due to this service now being provided independently.

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)?

There are several avenues for how the strategic direction could be implemented. We would expect to see long-term and short-medium term delivery plans in place, as well as a framework for achieving the objectives of the plan more broadly. The code modification process could potentially be altered to align with these plans.

Additionally, we would support the establishment of a strategy board to communicate strategic developments, progress, forward work plans and for general engagement but would be wary that creation of additional bodies for different functions will begin to add the same complexity and potentially duplication in function that the reform is attempting to remove.

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 customers)?

We agree with the proposed scope detailed in the Consultation Paper but note that strategic coordination across policy areas is critical for the proper functioning of the codes, if the strategic function is implemented.

If this is the case, there will be a need for a strong steer on issues that sit outside of the current license framework. Additionally, any coordination must be clearly defined within the modification process and fully costed. To this effect, clearly drafted terms of reference may be required in order to detail the scope and principles of involvement to prevent overreach of the strategic function. If other policy areas are to be considered by the strategic function, we envision this would need a principles based approach similar to the CACoP in order to ensure a holistic perspective is considered.

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?

Yes, we believe code managers should retain these responsibilities. We would like to note that prioritising which changes are progressed is a responsibility that may be better suited to a single governing body and not split between code managers, administrators and the strategic function. To this extent, it would be logical to have the prioritisation responsibility lie with the strategic function.

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?

Having end-to-end code and system managers would drastically improve code governance and current modification processes. It would reduce the duplication of communications, code administrator tasks and meetings as evidenced in the current system of cross code arrangements and inject efficiency in a currently segmented process. There may be difficulties in implementing an end-to-end code manager under model 2 as there is potential for resources to be detracted from the strategic function of the IRMB. A significant downside of implementing end-to-end managers would be the sizeable expertise and upskilling requirements required to efficiently manage the code as well as the system. Additionally, in the event the codes are consolidated, this downside increases drastically.

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?

We would agree that the code manager function should be accountable to the strategic body. We would also like to see accountability to code signatories as mirrored in the current format.

21. Do you have views on whether the code manager function should be appointed following a competitive tender process or other competition?

We see no reason why the code manager should not be appointed by competitive tender provided they meet appropriate criteria including but not limited to previous experience/track record and a demonstrated ability to manage the code.

22. Do you think the code manager function should be established by the strategic body creating a body or bodies? Please explain. If the code managers were established in this way, would we need to consider any alternative approaches to funding or accountability?

We would expect, if the code manager were propped by the strategic body by way of a new body, that the new body can adequately demonstrate its ability to manage the code effectively. This alternative would also require adequate consideration for funding and accountabilities though we see no issue with these mirroring the current landscape.

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?

We would support a hybrid approach as outlined in the proposal, with additional consideration, in later stages, for budgetary scrutiny.

As a starting point, we would expect an incentive framework for the code manager to consist of KPIs that encapsulate, among others:

- How quickly enquiries are dealt with
- Number of code modifications that were implemented within an approved timescale
- Alignment of code with strategic direction
- Number of non-compliances corrected within agreed timescales

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

We do not have any issues with the current set-up of code administrator funding arrangements. However, in the event that two or more codes are consolidated, we note that it will be vital to determine a methodology that appropriately and fairly allocates different areas of the code to code parties as there is a high possibility of parties bearing costs for actions, processes and areas of code that do not impact them.

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

In the long run, having one code manager for all codes (or for one unified code) would be able to deliver the outcomes of the reform, particularly by reducing fragmentation and cutting down on communication times between codes. There will be issues regarding required expertise for adequate functioning but these can be mitigated by a well-developed progress plan.

We would like to note that though this is our favoured option, it is a low priority for current energy regulation and will be an expensive and time consuming transition that is likely to cause disruption in the short term. In addition to this, a code reform of this magnitude is likely to require significant resources and expertise from the industry, from code parties and code managers. Therefore, we would advise that the code reform should be conducted so as not to clash with other reforms or SCRs that require the same or similar resources for development.

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

We believe the consolidation of all codes into a unified single code would be the best option to deliver the outcomes of the reform and reduce the issues of fragmentation and lack of coordination identified in the current landscape. There would be numerous realised benefits such as:

- Harmonised changes across fuels
- Simplified governance requirements
- Increased engagement capabilities with signatories
- Communication between code areas that is lacking in cross code areas for change
- Reduce regulatory burdens for new entrants

31. Do you agree that the codes should be digitalised?

Yes, digitalisation of the codes will fundamentally improve and ease code management and add transparency and clarity for code signatories and interested parties. In the long run, the impact of digitalisation will be apparent in terms of the process required to manage changes and smoothen the due diligence and expertise required to raise a change and implement the required end-to-end processes.

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

We believe that monitoring code compliance and addressing non-compliances should sit with the code manager who will have the requisite expertise to carry out these functions. Industry will have access to the performance reports and findings prepared by the code manager and can use these, where appropriate, to facilitate changes in code that address the root cause of any identified non-compliances.

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

We would suggest that model 1 would facilitate a more effective monitoring and compliance regime. The code manager would have a high level of technical expertise and code understanding, leading to potentially clearer communication of compliance arrangements and the facilitation of corrective actions where required.

Alternatively, placing monitoring and compliance oversight requirements on the IRMB may be misaligned with its primary goal of providing a strategic oversight and direction. The set-up of an independent performance assurance body that reports to the IRMB would be advantageous.