



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

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

codereform@beis.gov.uk
industrycodes@ofgem.gov.uk

16 September 2019

Reforming Energy Industry Codes Consultation

Dear Sir/Madam,

SmartestEnergy welcomes the opportunity to respond to BEIS' and Ofgem's joint consultation on reforming the energy industry codes.

SmartestEnergy is the UK's leading aggregator of distribution connected generation, a first mover in the aggregation of demand and frequency services and an established electricity supplier to large businesses. Founded in 2001, SmartestEnergy now employs over 300 employees, has a turnover of over £250million and is investing significantly to expand its operation in the UK and overseas.

Please note that our response is not confidential.

Overview

We can see that a strategic body may be required where a new policy direction is to be implemented, or for areas where industry alignment over the type of reform required is unlikely to be achieved. A totally new governance structure is probably not necessary and the simplest and most effective solution would be to give the role to Elexon by extending a licence obligation on National Grid. We do agree that there is some room for code consolidation.

In recent years, Ofgem have effectively fulfilled a similar role to that of the strategic body but going forward they should not hold the role or influence code administrators because they need to remain independent for the necessary appeals processes.

We are concerned that if a code manager has responsibility for proposing change and prioritising which changes are progressed then they will tend to favour their own proposals at the expense of industry proposals.

It is particularly important under the proposals outlined in the consultation document that the code administrator(s) do not financially benefit from the codes, because this could create perverse incentives to favour changes to systems which they control and could raise revenue from. Up until now, for profit code managers have not been such a problem because they have not had the power to prioritise.

Industry should not be excluded from or in any way prejudiced against in change proposals. Industry has the relevant expertise and is an absolutely fundamental stakeholder.

The energy markets are by their nature very complex and this is not in and of itself a bad thing. Nor does it necessarily lead to the conclusion that the arrangements need to be simplified. It merely means that there is a role (possibly one which could rest with Ofgem as they are the ones issuing licences) to advise parties of what they would need to do to enter the market.

To be "forward-looking" is an important objective, but it is also important to avoid making unnecessary changes and falling into the trap of picking winners i.e. making changes to give preferential treatment to a preferred technology which could lead to expensive changes in order to

accommodate that technology and which does not ultimately grow as expected.

We feel that the description of the problems in the document is ignoring the progress being made, for example, under the BSC with P370 'Allow the Panel to designate non-BSC Parties to raise Modifications' and P379 'Enabling consumers to buy and sell electricity from/to multiple providers through Meter Splitting.'

We are also of the view that it should not be taken for granted that utilities/public service providers are the de facto route for implementing government social policy, and direct support needs to be considered as an option in an open assessment process.

Consultation questions

We answer the questions below in the order in which they appear in the consultation document.

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.

The document states that the desired outcome is an energy code framework that:

1. makes it easier for any market participant to identify the rules that apply to them and understand what they mean, making it easier for new and existing industry parties to innovate to the benefit of energy consumers;
2. is forward-looking, informed by and in line with the Government's ambition and the path to net zero emissions; and ensures that codes develop in a way that benefits existing and future energy consumers;
3. is agile and responsive to change that benefits energy consumers, while able to reflect the commercial interests of different market participants; and
4. can accommodate a large - and growing - number of market participants, with effective compliance in an inter-dependent system.

We would tend to agree with points 3 and 4, because it is generally acknowledged that there will be a larger number of diverse business models in the future which will need to be accommodated in an easy manner where possible.

It would certainly be helpful for new market participants to be able to identify which rules apply to them, but the energy markets are by their nature very complex and this is not in and of itself a bad thing. Nor does it necessarily lead to the conclusion that the arrangements need to be simplified. It merely means that there is a role (possibly one which could rest with Ofgem since they are the ones who issue licences) to advise parties of what they would need to do to enter the market.

Whilst we do not disagree with the spirit of 2, it is clear to us that this should come about naturally as a result of the other outcomes. Here it is being used as the main driver/justification for the more fundamental structural changes, which in our opinion perhaps go a little too far. See below for further detail.

2. Do you agree with the problems we have 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.

No, on the whole we do not agree with the way the problems with the industry have been characterised.

- It is untrue that Ofgem have insufficient ability to implement process as they have made use of their ability to raise SCRs. These have had mixed levels of success and we would suggest that Ofgem is not best placed going forward to raise changes. Ofgem need to maintain their independence.
- It is true that some industry change has been slow, but it could have been expedited with a little more direction from Ofgem.
- To be “forward-looking” is an important objective. It is also important to avoid making unnecessary changes and falling into the trap of “picking winners” i.e. making changes to give special treatment to a preferred technology which could lead to expensive changes if the technology does not ultimately grow as expected.
-

- It is true that workgroups are resource-intensive, but it should be noted that the time is provided by industry free of charge and it is important that issues are considered by those who have the industry experience.
- It is true that the number of codes and the very different funding and governance structures make the regulatory landscape dauntingly complex. However, there is a reason why things are the way they are, and each code has a different range of stakeholders. Suppliers exist to ensure that all parties get paid on an equitable basis. This will clearly need to continue and BEIS and Ofgem need to consider whether the need to maintain equitability will ultimately constrain the ability to accommodate desirable new outcomes, and therefore may not justify the level of change proposed.
- We feel that the description of the problems in the document is ignoring the progress being made, for example, under the BSC with P370 'Allow the Panel to designate non-BSC Parties to raise Modifications' and P379 'Enabling consumers to buy and sell electricity from/to multiple providers through Meter Splitting.'

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

No

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

According to the consultation document the codes within proposed scope are: National Grid Electricity System Operator (NGESO) codes (CUSC, GC, STC) and the non-NGESO codes (BSC, MRA, DCUSA, DC, SEC, UNC, SPAA, iGTUNC, REC) as well as Smart metering (delivered by data and communications company - DCC), gas (delivered by Xoserve) and electricity (delivered by ELEXON) central systems delivery functions and the Data Transfer Service (DTS).

We note that the Smart Energy Code (SEC) is not explicitly mentioned, although there is a reference to "Smartmetering". We believe that the SEC should definitely be included.

We agree that there is room for consolidation in all of these areas.

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.

Not that we can think of.

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

The four areas identified for reform are:

"1. Providing strategic direction: ensuring the regulatory framework is forward looking and is informed by the Government's vision for the energy system. We propose creating a new function that can take account of that high-level vision and translate it into a strategic direction for codes that promotes the interests of consumers." We can see that a strategic body may be required where a new policy direction is to be implemented, or for areas where industry alignment over the type of reform required is unlikely to be achieved. In recent years, Ofgem have effectively fulfilled a similar role to that being proposed for the strategic body. Going forward Ofgem should not hold the role of the strategic body or influence code administrators because they need to remain independent for the necessary appeals processes.

"2. Empowered and accountable code management: a mechanism for ensuring that the strategic direction is delivered through appropriate changes to codes and that these changes are progressed in a clear and logical manner across codes." We agree with this so long as industry is not excluded from (or in anyway prejudiced against in) change proposals. Industry has the relevant expertise and is an absolutely fundamental stakeholder.

"3. Independent decision-making: rebalancing decision-making away from industry control, to arrangements that are agile and responsive to change

and work in the interests of existing and future customers." We disagree with the premise of this statement. It is misleading to suggest that current decision-making is under industry control as Ofgem approve all major modifications. We think that industry needs to be involved in and consulted on change. If any independence is required, it should be in area of removing Ofgem from their role as influencer of change and giving it to another independent body.

"4. Code simplification and consolidation: to improve accessibility: simplify and consolidate codes, removing unnecessary content, and ensuring codes are suitably adaptive to a changing industry." We agree with this.

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.

Given that both of these structures feed down from a "government vision", we fail to see how Ofgem, the independent regulator, could have any direct role in either model.

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.

Model 1 [Strategic body separated from Code Manager(s)] should create a separation that will make it simpler to understand how change is being driven.

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

Yes. It is misleading to suggest that Code Signatories currently approve modifications in any event.

10. Do you agree there is a missing strategic function for codes development in the energy sector and 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?

The document states the following: "There is no single organisation responsible for ensuring the codes are updated to take account of government policy or wider changes, or that the various codes and related IT systems evolve in a consistent and joined up manner, that is in the interests of existing and future customers." We would question whether this is really necessary. Of the options presented, the ESO is probably best placed to fulfil the strategic function. However, the strategic function would need to be properly resourced and ringfenced. The approach National Grid have taken to implement change as an EMR Delivery Body have not been effective, because they have not been sufficiently resourced and ringfenced, whereas the existence of higher-level bodies (e.g. LCCC) has been a waste of money. As mentioned above, Ofgem come with independence issues, and a new independent body would probably entail greater expense and complication. In light of this, we think an expansion of the Elexon role could be most effective solution.

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?

The objectives and responsibilities outlined in the document are:

1. Setting the strategic direction for codes, steering changes to the codes to deliver a smarter, more sustainable energy system that best protects the interest of consumers.
2. Ensuring codes and code governance remain agile and adapt as the sector transforms, including proactively identifying changes required to ensure a low cost, robust, effective energy system.
3. Working with the code manager function to unlock innovation

Of these we certainly agree with 2. We would say that 1 and 3 are laudable, but risk making unnecessary and expensive changes and falling into the trap of "picking winners."

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

It is not clear how day-to-day proposals which may not be clearly aligned with the strategic direction (but are considered necessary by the proposer and potentially wider industry) will be considered in the prioritisation process. We are concerned that there is a risk that such proposals could get left behind. There needs to be a consultation and appeals process to ensure that industry views on the correct prioritisation are heard. There also needs to be a consultation and appeals process to ensure that industry's view on specific proposals are heard.

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 think that engagement with (and the involvement of) industry will be vital in ensuring industry support. A strategy board with the right mix of skills and expertise from all sectors may help achieve this.

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.

Any strategic function should ensure equitability between all parties and fair market outcomes.

We are generally against using utilities/public service providers to implement government social policy. However, where it can be demonstrated that this can be done at a lower cost than "cash in hand" benefits then we can see the advantages. However, in each instance, this needs to be demonstrated in wider governmental cost benefit analysis i.e. it should not be taken for granted that utilities/public service providers are the de facto route for implementing government social policy, and direct support needs to be considered as an option in an open assessment process before handing the issue over to any strategic function.

15. Do you agree that in addition to the current responsibilities that code administrators have, that a. 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.

By and large we agree with the responsibilities outlined. However, please see our answer to Q12.

We would also like to point out that where the code manager and the system manager are one and the same and where they are responsible for prioritisation/influential in design, then there would be an incentive on them to prioritise complex system changes if this creates additional revenues for them. It is therefore very important that the code manager should be not-for-profit.

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?

Yes, end-to-end code and system managers would be ideal, but not easily achievable.

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.

Possibly.

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.

We would only be comfortable with this if there were obligations on the need to consult and on appeals (as we mention in Q12)

Ofgem could put a licence condition on the strategic body (especially if it were National Grid) and they should contract out the code manager function (possibly to Elexon). Much in the way that there was a licence requirement on NGT to create and maintain a BSCCo at the beginning of NETA.

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

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

Please see answer to Q18.

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

We would only be comfortable with this if there were obligations on the need to consult and on appeals (as we mention in Q12)

Code managers should at least be accountable in this way to industry because a) they fund it and b) they are a fundamental stakeholder.

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.

The NGT/Elexon model has worked well up until now. The BSCCo role has not been open to tender. Costs have thus far been controlled by accountability to those who pay the bills i.e. BSC parties. A licence requirement to ensure spending is efficient may suffice.

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.

Yes. Please see answers 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.

No. Please see our answers to Q10 and Q18.

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.

Please see answer to Q21. We do not see how price control would work because there is no revenue stream from customers. Scrutiny should come from those paying the bills. This may well mean industry participants.

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).

Presumably there should be an element of impartiality i.e. a party who would be subject to the codes should not be able to be a code manager.

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

Merging codes is going to bring together a lot of different types of party; distributors, generators, suppliers, etc. Ultimately, it is always the customer who pays, so it makes sense just to put the cost through suppliers, which would make it simpler and equitable. The licence fee proposal, however, presupposes that Ofgem are the strategic body.

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

One quick win could be to merge the CUSC and BSC, then add DCUSA at a later stage. We also feel that the REC and SEC could be merged early on and then roll into the above.

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

Ultimately, one. However, there is little benefit in merging gas and electricity at a wholesale level.

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

It is probably too early answer this question. The answer should be a function of the extent to which the codes can be consolidated.

Greater consistency can be introduced across the codes before/without consolidating code managers.

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



Ultimately Option A: consolidated into one - unified single code. However, this is not necessarily a must have.

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

Yes. However, we would be concerned if they were presented like the Energy Act online where it is difficult to tell whether you are looking at all the relevant clauses.

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

This should be a code manager role.

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

It probably makes little difference.

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).

We would have no issue with the IRMB fulfilling such a role, but decisions should be challengeable and ultimately there should be an independent arbiter.



Should you require further clarification on this matter, please do not hesitate to contact me.

Yours sincerely,

Colin Prestwich

smartestenergy

Head of Regulatory Affairs

SmartestEnergy Limited.

T: 01473 234107

M: 07764 949374