

Consultation on Reforming the Energy Industry Codes

Moyle Interconnector Ltd. Response

Moyle Interconnector Ltd. welcomes the opportunity to respond to this joint BEIS and Ofgem consultation on potential reform of the energy industry codes. Moyle Interconnector Ltd. is a subsidiary company of Mutual Energy Ltd.. The Moyle Interconnector is a High Voltage Direct Current (HVDC) connection between Northern Ireland and Scotland, providing a total connection of 500MW between the all-Ireland Single Electricity Market and the GB market.

We are broadly supportive of the move to simplify the codes and make them more accessible to all market participants and new entrants. We support reducing the influence of a few established large firms by establishing more independent code manager organisations, however we envisage these code manager organisations to essentially act as secretariats, rather than giving them significant decision-making powers.

Despite the positive proposals in this consultation, we have some major concerns about the proposed moves away from industry ownership of the codes, and the proposed strategic function and government policy more directly feeding into the codes.

This has the potential to dilute the level of expertise present in code ownership and development, remove the ability of those directly impacted by the code to readily develop it or challenge decisions based on it, and may undermine the objective of making the code simpler and more accessible if government policy changes frequently. Furthermore, the proposed strategic function could reduce stability for investors in the energy sector, lead to underinvestment in energy infrastructure and, ultimately, higher prices for consumers.

1. Background

1. Do you agree with our four desired outcomes for the code governance landscape by the mid-2020s? Please explain. If you disagree, please explain what you consider the outcomes should be.

Network codes are essentially multilateral contracts between market parties. They are broadly agnostic to policy changes and instead primarily promote functionality of the market. For this reason, network codes are not the place to implement Government policy. Policy incentives to promote green technology etc. can be determined and implemented outside the energy code framework via primary and secondary legislation – this would allow fuller consideration of impacts on consumers and industry through the appropriate mechanisms of Government and Parliament.

The proposed outcomes listed seem to focus most on improving competition in the industry in order to arrive at the lowest cost for the consumer. Whilst we welcome increased competition, the phrase “reflect the commercial interests of different market participants, to the extent that this benefits competition and consumers” suggests that commercial interests of market participants will only be considered where this leads to lower prices for current end consumers. This could have ramifications on levels of investment in infrastructure, for example, and ignores the security of supply and decarbonisation elements of the energy trilemma in favour of the cost element.

Given Governments face re-election at least every five years, there will be a further incentive to use the proposed policy inputs into the network codes via the “strategic function” to keep consumer prices as low as possible to suit election cycles. This could have significant impacts in long-term investment in energy infrastructure, and in turn lead to higher consumer prices in future when existing infrastructure needs replacing, and critical new infrastructure needs to be built.

Furthermore, we would be concerned that by ‘consumers’, this only means consumers in Great Britain. Something that “benefits” consumers in Great Britain might have knock-on negative consequences for consumers in Northern Ireland. Despite energy being a devolved matter, the UK Government has a duty to both, and one group should not be prioritised over the other, the impact on both should be considered when changes to network codes are considered.

2. Do you agree with the problems we’ve identified, and that they present a persuasive case for reform of the current framework for energy codes? Please explain.

We agree that the current framework for energy codes is fragmented and overly complex, with unnecessary duplication and high barriers to entry and innovation.

We can see benefits in having a single organisation responsible for the codes to ensure that, for example, duplication is minimised, but also drawbacks in terms of undue market power if this organisation is not fully independent of all market participants and code signatories.

We can see that there may be a lack of incentive for change in the current framework, which is dominated by large, established firms. However, we also have concerns about the idea that consumers’ needs conflict with industries requirements. This type of thinking could lead to regulatory overreach and undue political influence in the market. This could lead to short-termism in decision-making and long-term underinvestment in critical infrastructure.

By removing code management from industry and centralising it, there is an increased risk that decision-making on specific, very technical issues could also be taken out of the hands of specialists and given to those who may have good intentions, but who lack relevant experience or expertise, potentially increasing the risk of unintended consequences. This could be particularly problematic when dealing with niche parts of the industry where expertise may be confined to a small number of individuals or companies, and where it is not efficient or desirable for a centralised code manager or strategic function to have significant expertise on these issues or parts of the industry.

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

No answer.

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

No answer.

5. Are there any codes or systems that we should only apply a limited set of reforms to? Please explain.

No answer.

2. Vision and options

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

We do not agree that the energy codes framework should be directly impacted by the Government's vision for the energy system. This could lead to short-term decision-making and damage investor confidence. This would make it more expensive or more difficult to secure investment for key infrastructure projects, and in the long-term erode the efficiency and security of the energy network. This would have long-term impacts on both consumers and industry.

Similarly, we do not agree that independent decision-making would necessarily be a positive development, as it could take decision-making out of the hands of those with experience and expertise in the systems and markets that they are operating in and put it into the hands of people who may not have the same level of detailed knowledge. Even though there would be an element of consultation with industry, the independent decision-maker would decide what weight they attach to any consultation or individual responses. This move therefore inherently increases the risk of decisions being taken that have negative unintended consequences.

We support a more accountable system of code management within the industry, which reduces barriers to entry and competition in the market, as well as appropriate incentives to remain compliant with the code.

We strongly support the idea of code simplification and consolidation as this would reduce barriers to entry and promote innovation. We are concerned at the suggestion that this would be done to make it easier to "rapidly change in response to strategic priorities", however. As explained above, this could reduce investor confidence in the energy market and lead to worse outcomes for consumers in the long run, as the regulatory framework for the industry could be less stable due to direct Government involvement.

7. Do you agree with the two broad models outlined? Please provide reasons for your position and evidence where possible.

No, we have concerns about the "strategic function" included in both models. Our full concerns are outlined in detail in our response to other questions.

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

We are agnostic as to which of the two models will best deliver on desired outcomes. However, we would like to emphasise that any code manager body with enhanced responsibilities should be fully independent of all code signatories. This means that arms-length or ring-fenced subsidiaries of larger organisations who are signatories to the codes should not be given the role of code administrator without first being made fully independent of their parent companies.

In both models the code is treated as a tool for implementing Government policy via the "strategic function". This means that there will be significant changes to the codes at regular intervals as Governments and policies change. This, and therefore both models, are incompatible with outcome 4, code simplification and consolidation. Rather than making the codes simpler for businesses, constant change builds complexity and will mean that businesses have to invest significant resources in keeping up with the changing policy and its impacts on the codes.

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

We do not agree that the role of oversight of the code administrator should be removed entirely from code signatories. Industry participants, as code signatories, are at the coalface of industry developments and will be the first to notice and feel the pain if code administrators are not performing their role adequately. By removing oversight and decision-making from industry, there is no formal recourse for those directly impacted by the codes to challenge, query or change the code administrators' decisions.

3. Providing Strategic Direction

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 in the best way to address the lack of strategic direction? Please explain. Who is best placed to fulfil the strategic function and why?

Network codes are essentially standardised contractual frameworks for industry participants. Code managers should be proactive in ensuring that the network codes are agile, streamlined and efficient and work for code signatories.

Given most infrastructure projects in the energy sector have extremely long lifespans, there is a benefit for network codes to be forward-looking and future proofed. As a result of this, and the fact such projects require high levels of initial capital investment, there is also a benefit for the network codes to remain consistent over time. Consistency provides investors with confidence that they will recoup their initial outlay over the lifespan of the project.

Governments face short-term (less than five year) incentives, as such moving to a situation where government policy has a key role in the industry's standardised contractual framework is likely to lead to a situation where there are drastic changes to the framework every few years. This will only serve to damage investor confidence, as they may see a scenario where they provide large up-front capital investment, but then after a few years the income to recoup this investment disappears.

Government has other methods for implementing its policy agenda and we do not believe that network codes are the appropriate lever for policy to be delivered.

In addition to the impacts on investment levels, there are also issues with oversight with this approach. By removing oversight of the code administrator and potential strategic body from code signatories, market participants who are the most impacted by the codes and who understand them best have no meaningful input to the codes or their direction. Additionally, if the strategic function determines the 'Governments vision' based on public statements, for example, there is no formal challenge or oversight even from political opponents, let alone industry experts.

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?

See question 10 above, we do not believe that network codes, as multilateral contracts between industry participants, are an appropriate lever for Government policies to be delivered and have concerns about the strategic function's role in setting the direction of the codes based on short-term Government policies.

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

No answer.

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)?

No answer.

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)? Please explain.

See question 10 above, we do not believe that network codes, as multilateral contracts between industry participants, are an appropriate lever for Government policies to be delivered and have concerns about the strategic function's role in setting the direction of the codes based on short-term Government policies.

4. Empowered and accountable code management and independent decision making

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;

We agree that code managers should have the opportunity to identify, propose and develop changes to the codes, including conducting impact analyses. However, all signatories to the network codes should have the opportunity to bring forward, develop, challenge and amend changes.

- b Making decisions on some changes; or making recommendations to the strategic body;

We do not agree that code managers should have the ability to make changes to the code. This should only be done by the agreement of code signatories.

- c Prioritising which changes are progressed

Code managers acting as a secretariat will inevitably make decisions around which code changes are prioritised. This is acceptable providing there is a mechanism for code signatories to challenge these decisions and insist that important changes are prioritised where appropriate.

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

No answer.

17. Should the approach differ on a case-by-case basis (i.e. depending on the code or system in question)? Please explain.

In the interests of simplicity and efficiency, every effort should be made to ensure a common framework for all codes.

18. Do you agree that the code manager function should be accountable to the strategic body and this should be via licence or contract? Please explain.

We do not agree that a strategic body should be created, please see answer to question 10.

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 do not agree that a strategic body should be created, please see answer to question 10.

20. Do you agree that we should not consider further a model whereby the code manager function is accountable to industry? Please explain.

We do not agree that this option should not be considered. Network codes are essentially multilateral contracts between the code signatories, as such they in some way 'belong' to code signatories. The proposals outlined in this consultation remove the ability of industry participants not just to amend the codes, but to challenge amendments made by non-signatories to what is effectively a contract. This seems like a bizarre situation and removing industry accountability is fundamentally incorrect, inequitable and could face legal challenge.

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

We are agnostic on how the code manager should be appointed; however, we feel it is important that once appointed a code manager, the organisation should be completely independent from any of the code signatories. That means that subsidiary companies of code signatories should cut ties with the code signatory, rather than just be ring-fenced or have Chinese walls established. For example, the code signatory must dispose of all shares in the subsidiary in the event that it is appointed as code manager.

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? Please explain.

We do not believe a strategic body should be created.

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 a code manager?

Please see answer to question 21.

- b Requiring a licensee (or group of licensees) to create the code manager?

Please see answer to question 21.

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.

No answer.

25. Are there any factors that:

- a Would stop parties (including code administrators) from becoming code manager?

Please see answer to question 21.

- b Should prevent parties from becoming a code manager (eg. do you agree that licensees should not be able to exercise control of the code managers)?

Please see answer to question 21.

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

If the code manager function is funded by code signatories, then it is entirely reasonable to expect that industry would have oversight of the organisation. Expecting code signatories to abide by the code, pay for the code manager, but have no recourse to change the code or challenge the code manager's decisions is an entirely unreasonable prospect.

5. Code simplification and consolidation

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

No answer.

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

Given the very different nature of the markets for the two commodities, we support at least keeping gas and electricity separated. Beyond this we are agnostic as to how many codes each market has.

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

We are agnostic as to how many code managers there should be but would reiterate our answer to question 21 regarding the need for code managers to be independent of code signatories.

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

No answer.

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

Yes codes should be digitalised, however where there are references to other parts of the code these should be easily navigable from the reference. Our experience with the digitalised Balancing and Settlement Code on the Elexon website is that it can be difficult to quickly navigate to other parts of code where there is a reference to them in the text.

6. Monitoring and compliance

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

Asking code signatories to police themselves could lead to potential discriminatory and anti-competitive practices. Whilst there could be a role for code managers in identifying non-compliance, ultimately the regulator should be the final arbiter of compliance.

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

See answer to question 32.

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.

See answer to question 32.