

Ofgem Forward Work Programme 2016 - 17

Energy UK response

17 February 2016

Energy UK is the main trade association for the energy industry, with over 80 members; representing energy generators and suppliers of all sizes. Our members supply gas and electricity and provide network services to both the domestic and non-domestic market. Energy UK members own over 90% of energy generation capacity in the UK market and supply 26 million homes and 5 million businesses, contributing over £25 billion to the UK economy each year. The industry employs 619,000 people across the length and breadth of the UK, contributing £83bn to the economy and paying over £6bn annually in tax.

Introduction

Energy UK welcomes the opportunity to respond to Ofgem's Forward Work Programme and commends Ofgem's open engagement and transparency over upcoming work. To keep our response as concise and useful as possible the format of this response follows the outline of the forward work programme consultation document. Energy UK's comments are made by exception.

Energy UK strongly believes in the value of a competitive energy market and a stable and independent regulatory regime. Together these can foster innovation, support market development, bring benefits to consumers and help provide the certainty that is needed to encourage investment and enhance the competitiveness of the energy sector as a key part of the British economy.

Energy UK also believes that it is energy policy and regulation can no longer be looked at in isolation and that a whole system approach across electricity, heat and transport is needed in order to achieve decarbonisation objectives in the most efficient and cost-effective way for consumers.

Energy UK asks Ofgem to be explicit about how it has taken stakeholder responses into account when it publishes its final Forward Work Programme. Periodic updates on Ofgem's progress against the actions set out in the FWP would be useful to stakeholders.

Executive summary

Energy UK welcome Ofgem's review of its regulatory framework and new structure; including its look at the future of retail regulation, the importance of impact assessment processes and ongoing effort to streamline information request methods.

On the transition to principle based regulation, Energy UK are very supportive, however, for such an approach to be successful, in the interests of consumers, greater trust is needed between the industry and the regulator. Energy UK will be responding to this consultation and look forward to engaging with the programme as it progresses.

Members support Ofgem's corporate strategy so far as the corporate strategy emphasises the importance of Ofgem's role as an economic regulator that does not engage in social policy or make decisions that have significant redistributive implications.

Energy UK recommends that Ofgem dedicates more resource to providing practical guidance on REMIT. We also encourage increased engagement between Ofgem and market participants to build mutual understanding, which will promote greater certainty and contribute to more effective implementation of REMIT.

Energy UK considers it important that all Ofgem initiated industry change take into consideration other change initiatives which suppliers may be implementing concurrently. Taking a holistic view across the industry, across both retail and generation is important to industry implementing changes.

The EU network codes will continue to play a central role in establishing the Internal Energy Market and Energy UK would like to ensure continued engagement on this issue.

1. Regulation of Network Companies and other Monopolies

Data and Communications Company regulation

Energy UK encourages Ofgem in its engagement with the Data Communications Company (DCC) and the Department of Energy and Climate Change (DECC), as the smart metering rollout programme moves towards commencement in August 2016. Of particular note is the recent case of Ofgem holding the DCC to account over costs. Nonetheless, Energy UK asks that Ofgem continues to maintain scrutiny of the DCC's operational costs, ensuring that it provides value for money for consumers.

With DECC Live due in 2016 Energy UK asks that Ofgem continue to provide Smart DCC with the support and guidance required to ensure that the mass roll out of smart meters can be delivered in a timely and effective manner.

Interconnection and cap and floor

The Cap and Floor regime has been successful at attracting new prospective interconnector projects which may not have been developed otherwise. Given that consumers are effectively underwriting these investments, it is very important that each project is closely scrutinised in terms of value for money under a variety of future scenarios. Energy UK believes that Ofgem should carefully consider differences in policy costs between the UK and the rest of the EU when agreeing cap and floor contracts. Ofgem should additionally consider market arrangements on either side of interconnectors in the pursuit of a level playing field. Additionally, Energy UK continue to welcome more transparency and engagement from Ofgem on the Cap and Floor regime.

2. Setting the Rules for Markets

Half hourly settlement

Energy UK has explored the effects of concurrent and uncoordinated policy initiatives on suppliers' ability to deliver effective policy and generate the best outcomes for their customers, and identifies four potential improvements which Ofgem should undertake as part of its cost-benefit analysis. It is important that all Ofgem initiated industry change take into consideration other change initiatives which suppliers may be implementing concurrently. As a part of Ofgem's cost benefit analysis, it is suggested that Ofgem:

- a) takes a centralised view of change: A central understanding of all the collective changes affecting this industry is needed to ensure that policies and changes affecting suppliers' functions do not overlap significantly;
- b) ensures central co-ordination and prioritisation: Rather than leaving the process once a decision is made, we believe one body should be accountable for co-ordination for each programme;
- c) considers an impact assessment on the change pipeline: There should be overview of all changes going through at the same time, to ensure that multiple policies do not impact the same systems at the same time;
- d) includes a feedback mechanism: The cost estimate produced at the early stages may not reflect the actual cost and time taken to implement a change because much of the detail has not been specified at the early consultation stages. A joint government and industry review would allow learnings to be shared.

Flexibility

Energy UK welcomes Ofgem's flexibility strategy and is supportive of the continuing work in this area: including the decision in the short term to focus on clarifying the role of aggregators and implications for industry arrangements, increasing participation of industrial and commercial consumers in flexibility opportunities, and deciding how electricity storage fits into the legal, regulatory and industry framework.

Ofgem should also consider how flexibility markets can develop going forward; in particular how to improve the market for ancillary services in terms of suitability for a range of providers (generation, DSR, storage etc.). Furthermore developing a market that endorses the principle of cost reflectivity and a high level of transparency. Critically, Energy UK is confident that a competitive, market led approach will best deliver this. As part of this Ofgem will need to look at whether the right incentives are in place for TSOs and DNOs/DSOs to tender for ancillary services with view to the long term needs of the system and minimising costs.

System Operation

Energy UK supports further work by Ofgem to look at the future of system operation. The rapid, ongoing evolution of the GB energy system means the role of the System Operator and the Distribution Network Operator is becoming increasingly complex, and this is set to continue with developments in embedded generation, distribution level storage solutions and the drive towards integrated energy markets across Europe.

There are many areas to assess such as how best to co-ordinate System Operation across both Transmission and Distribution Networks given the amount of renewables on the electricity system and growth of embedded generation. Only once sure about the issue to be addressed, can the various roles, responsibilities and interactions be assessed. Whatever the outcome, a robust Cost Benefit Analysis will be required to ensure that the costs of moving to a different model will result in long term improvements to system operation and ultimately not increase the cost to consumers.

Code Governance Review (Phase 3) Initial Proposals

Code governance varies across the different electricity, gas and retail codes creating a complex, resource-intensive regulatory framework which can be challenging for small and large companies alike. This becomes more challenging when multiple large changes occur across the energy industry in a short period of time without being fully considered in the whole across industry systems. Any changes to the code governance framework should look to simplify the framework and increase accessibility for all market participants.

Energy UK considers that it may be better to have fewer codes and, where possible, to rationalise their content and identify synergies. While Energy UK acknowledges that it would take a lot of work/resource to rationalise the codes, it could lead to cost and resource efficiencies. Energy UK also considers it beneficial for programme management capability to build around Code changes. Streamlining will provide a clear vision of the optimal structure of industry codes.

DECC's proposals to make it easier for Ofgem to amend industry codes to implement faster switching and half-hourly settlement is a concern because it would give the Authority powers to make modifications without having to do an impact assessment or the possibility of being challenged on the merits of the case. In the past Ofgem's use of the SCR have meant that suitable alternatives have been developed in conjunction with industry allowing the Authority to ultimately decide which option to approve.

Energy UK has concerns about proposals to remove suppliers' statutory right of appeal on the merits to the Competition and Markets Authority (CMA). Energy UK believes interested parties such as suppliers and consumer groups should retain the right to appeal Ofgem decisions on substantive grounds. Judicial Review will not assist in creating a stable or predictable environment as the substance of a policy decision cannot be scrutinised effectively by an appeal court.

Objections

Energy UK members take a keen interest in Ofgem's review of the objections process. The outcomes of the review may have a profound impact on how suppliers operate and serve customers, the impacts of which could be borne by customers and suppliers for years to come.

Energy UK welcomes Ofgem's confirmation that it will carefully consider the potential effects on customer and supplier behaviour, and on interactions between them when considering policy options. In any resulting assessment, Ofgem should ensure that it takes into account the fact that the market will evolve, both in response to potentially removing/limiting debt objections and due to other innovations independent of this it.

3. Effective Competition

Future retail regulation

Energy UK welcomes the publication of Ofgem's consultation on its Future of Retail Regulation project. Energy UK is supportive of Ofgem's ambition to transition to a principles/outcomes-based to retail market regulation. However, for such an approach to be successful, in the interests of consumers, greater trust is needed between the industry and the regulator. We will be responding to the consultation in due course and look forward to engaging with the programme as its progresses through 2016-17.

In considering the transition to a principles/outcomes based approach Ofgem must, however, remain mindful of:

- a) Impact of the CMA investigations finding and remedies.
- b) Impact of potentially prescriptive European regulation of retail energy markets (i.e. outcomes of the Commission's New Deal).
- c) The development of policy during the transition (i.e. PSR, quicker switching, objections)

It is important that policy development in the interim is consistent with transition to principles/outcome based regulation.

Consumer vulnerability strategy

Energy UK will be responding to Ofgem's final proposal on Priority Services Register reform (PSR). It is vital that Ofgem ensures that any changes to the PSR are proportionate and practical for suppliers of all sizes to deliver. Energy UK remains very keen to work with Ofgem, suppliers and the networks with regards to how it can best take forward both the development of the PSR and its Consumer Vulnerability Strategy more generally.

Company performance monitoring

Ofgem has consulted on publishing customer service indicators, retail market indicators and wholesale market indicators. This year it will be consulting on a potential replacement for the SMI and may make further changes to customer service indicators. Ofgem should ensure it consults fully with industry to produce a set of indicators which help customers make switching decisions and not have unintended consequences

Wholesale market integrity and transparency

Energy UK and its members place huge importance on wholesale market transparency. Energy UK continues to publish its monthly wholesale market report. However, we believe that Ofgem could help improve transparency by using the REMIT data it now receives to produce a monthly retrospective wholesale market report. This will help improve the completeness of the transparency initiatives that are already existence.

It is important that Ofgem monitors the wholesale electricity market and its ability to deliver effective outcomes for consumers. In order to do this the impact of Secure and Promote in improving access to the market must be analysed as well as market liquidity. Ofgem needs to develop measures of success against which to judge Secure and Promote arrangements to date. Energy UK would welcome further engagement on this topic.

Non-traditional Business Models

Energy UK welcomes Ofgem looking into non-traditional business models and look forward to reading Ofgem's discussion paper later in the year on local energy.

4. High Standards of Outputs and Protection

Consumer empowerment and protection in a smarter market

Energy UK looks forward to continuing to engaging with Ofgem's Consumer Empowerment and Protection project.

Third Party Intermediary regulation

Energy UK believes trusted third party intermediaries (TPIs) provide key customer engagement tools. It is important that Ofgem, through its development of a non-domestic TPI Code of Practice and its review of the Confidence Code, continues to promote a TPI environment which means customers get a clear, fair, transparent and accurate experience when procuring electricity and gas, regardless of the route they choose to access the market. Energy UK will continue to support Ofgem in this area.

Ofgem E-Serve currently has an important role in relation to supplier obligations for environmental schemes, as government moves forward with plans to extent replace ECO and WHD, however, Energy UK would support the simplification of Ofgem's approach to the administration of supplier obligations in order to:

- a) Make obligations simpler to deliver for suppliers and the supply chain,
- b) Make schemes more cost effective, and
- c) Ensure that schemes and the role of suppliers is more comprehensible to consumers.

Energy UK is supportive of the ongoing Bonfield Review of advice, quality and standards. It is important Ofgem engage with the Review. If it is to be considered a success it is vital the Bonfield Review delivers an accreditation and certification framework for energy efficiency that can be relied upon by Ofgem to demonstrate compliance with Building Regulations e.g. Competent Person Schemes, PAS 2030. If Ofgem have evidence-based concerns that such schemes are not fit for purpose, this should be feed into the Bonfield Review and shared with the relevant authorities to help drive improvements.

5. Partnership with Government and Stakeholders

EU coordination and engagement

Energy UK welcomes Ofgem's involvement in vital European regulation. Energy UK anticipates Ofgem will do its best to ensure that the direction of travel in EU regulation does not conflict with developments in the UK regime. Where there are discrepancies Energy UK expects Ofgem to take the appropriate action to minimise any negative effects on energy consumers in the UK. In particular, it is important Ofgem consider how EU law will interact with the CMA's conclusions and the ambitions of Ofgem's Future of Retail Regulation project.

EU regulation and network codes implementation

The EU network codes will continue to play a central role in establishing the Internal Energy Market. We welcome the progress made in the last months and the adoption of 5 (out of 8) EU electricity network codes and implementation of the gas capacity allocation and balancing codes in 2015. We hope that Ofgem, notably through its role within ACER, will ensure that the remaining three electricity codes will be approved smoothly in the next months and that the gas transmission tariff code is also finalised.

Apart from the swift adoption process, Energy UK would also like to highlight a number of areas where we would like to further engage with Ofgem, given the importance of the issues to the industry:

- ▶ It should be a priority to establish an appropriate, transparent and flexible process to modify the EU Network Codes. This should ensure that industry stakeholders are fully and properly

involved from an early stage and that TSOs and other market participants are placed on an equal footing in being able to propose amendments;

- ▶ The EU network code implementation would require a number of national arrangements to be updated, in particular the industry codes. As the complexity of industry arrangements continues to be hailed as a potential barrier to entry, we therefore consider that the EU network code implementation provides an excellent opportunity to revisit the existing electricity industry codes structure. We would expect Ofgem to engage with the industry on that topic.
- ▶ The gas transmission tariff code is not yet finalised but implementation timescales are likely to be ambitious. We call on Ofgem to fully engage in implementation of this code and adopt an open mind with respect to implementation of its charging review.

E-serve

With regards to Ofgem E-Serve's role in implementing government policy, Energy UK believes that the administration of future social environmental schemes should be subject to a formal tender process. In the instance that Ofgem E-Serve remain a scheme administrator, Energy UK would expect it to engage effectively and provide relevant information to all participating stakeholders.

REMIT

Energy UK recommends that Ofgem dedicates more resource to providing practical guidance on REMIT. We also encourage increased engagement between Ofgem and market participants to build mutual understanding, which will promote greater certainty and contribute to more effective implementation of REMIT.

6. Trust and Confidence

Security of supply and a functioning market

It is important that Ofgem monitors procurement and dispatch of SBR and DSBR closely to ensure that it is used in a cost effective manner and impacts on the wholesale market are minimised.

It is also important that Ofgem is able to explain clearly and simply to the public how the electricity market works and in particular the impact that recent cashout changes has on near term prices in the balancing and wholesale markets.

7. Efficiency and Reduced Regulatory Burdens

Reducing burdens

Energy UK have responded to Ofgem's Simplification Plan, which is [currently on our website](#). Energy UK has, on several occasions prior to this, commented on the need for Ofgem to streamline its information requests process. Suppliers of all sizes receive many information requests from a number of bodies which may overlap, be issued at short notice, duplicate other requests or simply involve intense data management efforts. We will be asking both Ofgem and Citizens Advice for a schedule of upcoming information requests in order to better manage this burden.

Optimising outcomes for energy customers

Energy UK welcomes Ofgem's new organisational structure; particularly the division dedicated to improving regulation, and the introduction of a new analytical excellence team.

Impact Assessments

Energy UK would like to stress the importance of impact assessments. Improvements to process include: adopting the Government's impact assessment template, ensuring independent scrutiny and being transparent in resolving perceived conflicts between statutory duties

8. Budgets and Spend

Energy UK would also welcome greater clarity and granularity from Ofgem with regards to Ofgem's operational spend on smart metering.

For further information, please contact:

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