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Sent by email only to: CodeGovRemedies@ofgem.gov.uk

Dear Laura

Industry Code Governance: Initial consultation on implementing the Competition and Markets Authority's recommendations

This is the British Gas response to Ofgem's final proposals in relation to the above consultation. Our response is non-confidential and can therefore be published on your website.

We welcome the opportunity to comment on this initial consultation that considers the output from the Competition and Markets Authority's (CMA) recent review of industry code governance arrangements. The industry is reliant on code governance, code administration, and central systems for the efficient day to day operation of the industry. Change is also a fundamental necessity in the industry and we welcome initiatives that may improve the management of change, whether it is small tactical changes, or significant strategic change.

We have been supportive of the CMAs recommendations and look forward to working with Ofgem and other industry participants to develop these recommendations into practical solutions that can be delivered in appropriate timescales, at reasonable cost whilst delivering the maximum benefit.

The consultation covers three key initiatives that are proposed to be delivered over the next 3-4 years. We appreciate that these proposals are in their infancy and that it is therefore important to make sure that the objectives of each one are clear, coherent and deliverable within the timescales. Whilst we believe this has already been largely achieved for the strategic direction and consultative board aspects, we have reservations about the licensing of code bodies and systems delivery bodies.

Strategic direction

We are supportive of the proposed strategic direction as set out in the consultation document. A cross-cutting strategic direction for industry codes should be central to aligning code parties' objectives, and system delivery bodies' objectives, with that of agreed policy and wider changes in the market. Accountability is crucial to having a robust and valued strategic direction and a suitable supporting governance framework.

Consultative board

We are supportive of the consultative board principle. We believe it should be an advisory function with a clear focus on ensuring that cross-cutting code issues are dealt with and that

code changes across multiple codes and/or systems are coordinated to ensure their effective and economic delivery. We also support the creation of a cross code industry plan that the consultative board would be responsible for.

Licensing of code managers and delivery bodies

We have concerns that a full licensing approach for both code managers and system delivery bodies would not be a proportionate approach. The regulatory burden, time and cost implications would be onerous and there may be other approaches to delivering the majority of the benefits of a full licensing solution. We therefore urge Ofgem to consider alternative, more tactical and shorter term remedies, such as using and strengthening the existing Code Administrators' Code of Practice (CACoP), to deliver greater accountability, greater consistency across codes and increased competition within the existing code administration sector.

If alternatives, such as CACoP, are subsequently not deemed to be appropriate then we can see merit in pursuing licensing for system delivery bodies. The merit and suitability of licensing system delivery bodies would need to be assessed individually for each specific code. For example, for the Smart Energy Code (SEC), the Data Communications Company (DCC) already act as a licensed system delivery body and therefore further changes are unlikely to be required, For the Uniform Network Code (UNC), Xoserve are the system delivery body, they are not licensed but have historically been owned by other licensees. Ofgem have recently delivered fundamental changes to the funding, governance and ownership arrangements to ensure greater accountability, transparency and industry involvement. Whilst this falls short of a licensing regime it may well be an alternative model to consider when looking at the implications of a licensing regime on other codes.

Our detailed responses to the consultation questions are attached in Appendix 1. Please do not hesitate to contact me, or Simon Trivella (simon.trivella@britishgas.co.uk), if you require any further detail on our response.

Yours sincerely,

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Appendix 1

Chapter Two: Scope of arrangements

Question 1: *Do you agree that the codes and functions we have identified (i.e. the codes within the scope of the CACoP and their associated central system delivery functions) should be within scope of the new regime?*

Yes, we agree that the codes and functions that have been identified should be within scope of the new regime (or aspects of it).

Group 1 codes ("NETSO codes") do have scope to impact the delivery of strategic projects and we therefore agree that they should be within scope. Due to the National Electricity Transmission System Operator's (NETSO) central involvement, system ownership, and existing licensing regime, it may not be appropriate, or necessary, for further licensing, or creation, of a code manager or a system delivery body. However, we see that a strategic direction and the consultative board could cover NETSO codes and hence we agree that they are suitable to be within scope.

Group 2 codes ("Non-NETSO codes") cover the majority of industry change, particularly retail and consumer facing changes, and numerous existing strategic projects. We believe it is within this group, along with group 4, that the proposals may have the greatest impact as they have the potential to play the most material role in delivering strategic changes to the energy market. The different codes vary in their governance structures with a range of different code administration arrangements. We believe careful consideration needs to be given to the future of these codes, for example as mentioned below in relation to the faster and more reliable switching (F&MRS) programme, and that any changes made are done so in conjunction with any other agreed longer term strategic objectives (e.g. the introduction of a retail code that would also be part of Group 2). We do not see how the licensing of code managers could be consistently applied across these codes without significant change. We discuss this further later in this response.

Group 3 codes ("Other codes") cover other codes that are much narrower in their application. We agree that these codes are less likely to have a material impact on the delivery of strategic change and it is therefore not necessarily appropriate to bring them into the scope of the new arrangements. We also agree that, despite its wide ranging impact, there is not a strong argument for the System, Security and Quality of Supply Standards (SQSS) to be within scope. This is mainly due to the arrangements being administered by NGET, an existing licensee, and changes only being permissible via licence change. However, we would comment that an overall strategic direction, and the applicability of the consultative board, may be worth considering for this group, albeit to a lesser extent (e.g. other codes may be required to have regard to the new arrangements rather than, say, being bound by any particular requirements or obligations).

Group 4 codes ("Central system delivery (SEC, UNC, BSC)") covers the core centralised retail systems that can, and do, have a material impact on the delivery of strategic change. As with Group 2, we believe that the implementation of these proposals, or aspects of them, could have the greatest benefit in this area. However, as with the related code administration arrangements, the way in which the UNC, SEC and BSC systems are owned, managed and governed varies quite considerably. Therefore we agree there may not be a one size fits all solution.

Group 5 ("Wider delivery functions") covers wider systems and services that are unlikely to impact on strategic change. However, that is not to say that, at the very least, the governance arrangements for these delivery functions should necessarily be out of scope. As with Group 3, there may be scope for the governance of such functions to have regard to the strategic direction and the consultative board. Some of these governance arrangements already fall within codes that are within scope (e.g. the Theft Risk Assessment Service (TRAS) and the Meter Asset Managers Code of Practice (MAMCoP) reside within the Supply Point Administration Agreement (SPAA)) and we therefore support further consideration of whether other functions should also be brought within scope.

Question 2: *Are there any other codes or systems that should be within scope and if so please give your reasons?*

No, we do not believe there are any other codes or industry systems that should be within scope.

Question 3: *Are there any other factors you think we should consider when making this decision?*

The timing of this work will overlap with the implementation of code reform elements being progressed via the major strategic programme of work known as Faster and More Reliable Switching (F&MRS). Whilst design work is still underway within the F&MRS programme, it is vital that the objectives of these projects remained aligned and that we do not make changes to code governance arrangements without fully understanding the target state of holistic code governance arrangements post F&MRS implementation.

Part of the F&MRS work has been looking at the regulatory design in a faster switching environment. Stakeholders have provided views on what changes could be made to existing codes (e.g. code consolidation or simplification) and have considered whether a new dual fuel 'Retail Code' would be a more suitable governance vehicle for future market arrangements. These types of changes will have a significant impact on wider code governance arrangements. We should therefore avoid making, what could be unnecessary changes to code arrangements ahead of receiving clarification of code governance related changes being made by the wider F&MRS implementation.

Chapter Three: Licensing and Competition

Question 1: *What are your views on our proposed approach of including the code manager and delivery body function in a single licence?*

Whilst we agree that the synergies between code management and the delivery element of code change are sufficiently strong, we do not agree that the proposed approach of having a single licence to cover both roles is an effective or proportionate way in which to combat the Adverse Effect on Competition (AEC) that the CMA identified.

We have concerns that a full licensing approach for both code managers and system delivery bodies would not be a proportionate approach. The regulatory burden, time and cost implications would be onerous and there may be other approaches to delivering the majority of the benefits of a full licensing solution. Also, we do not see that a one-size fits all solution would necessarily be appropriate for each code within the groups that Ofgem has identified. We

would therefore welcome Ofgem leading further industry engagement in order for appropriate solutions to be developed and implemented where required.

Our broader concerns with the licensing of code managers is the lack of clarity in terms of roles and responsibilities, general accountability, and the potential negative impact it may have on existing arrangements. For example, under many codes there is a representative Panel that is supported via code administration and secretariat services. These services are often procured via an executive body, constituting Panel members, which effectively perform a contract management and performance role. It is not entirely clear to us on how these existing relationships, and contractual arrangements for code administrators, would need to change under these proposals. Furthermore, with code managers in place, industry participants may no longer have the same influence on code governance arrangements, and have less of an ability to drive strategic change.

The proposed licensing regime will require changes to primary legislation, presumably both the Gas Act and the Electricity Act, as code administration and central system delivery would need to be a prohibited activity to then create a licensing framework. Whilst we have been supportive of the CMA's findings, we urge Ofgem to consider alternative, more tactical and shorter term remedies, such as using and strengthening the existing Code Administrators' Code of Practice (CACoP) as detailed below, to deliver greater accountability, greater consistency across codes and increased competition within the existing code administration sector.

Within some codes, the central systems are owned and operated by an existing licensee (or owned by a number of licensees). As with code administration, many of the arrangements have direct links back to licence holders, whilst others are intrinsically linked to the delivery systems, and some have been procured through competitive tender. With such a range of arrangements we would support some further analysis work being carried out by Ofgem, along with stakeholders, to address the shortcomings of any particular existing arrangement and the identification of 'best practice', where code arrangements and system delivery is shown to be working well.

A number of the codes identified as being within scope of this work are also subject to the Code Administration Code of Practice (CACoP). We believe CACoP has been a valuable initiative but could be developed further to bring greater consistency across industry code processes and arrangements. For example, industry code change management processes must follow the CACoP principles but, even though this has been adopted, we still see significant differences which make the progression and timing of delivering cross-cutting industry change challenging at times. We would support a greater focus on further development of CACoP and believe that this could, in the relative short term, deliver some significant benefits when done so in conjunction with the proposed strategic direction and the consultative board. For example, CACoP have recently published the first edition of the Energy Industry Forward Workplan. This is the first time such a comprehensive view of industry change has been produced in a single document and is the result of a significant collaborative effort by the code administrators. We would expect this now to evolve and, in the context of the consultative board, develop into the first version of the consultative board's industry plan.

If successful, CACoP could deliver a number of the benefits that are associated with the proposed licensing regime, for example, greater consistency and alignment across code change processes, performance improvements through comparison of metrics and Key Performance Indicators (KPIs), financial efficiencies through the creation of 'value metrics' and prioritisation of cross-cutting industry change. We therefore suggest that this should be seen as the preferred alternative to licensing and at the very least as a forerunner to progressing changes to implement complex licensing arrangements.

We also believe that consideration should be given to the way in which existing code administrators are procured and, where possible, how competition in this sector could be introduced without a licensing regime. This could be extended to look at whether code administration could be further simplified across codes by having collective procurement (e.g. a single code administrator covering more than one industry code). Again, this may well deliver the aims and objectives of the CMA's recommendations without the establishment of a licensing regime.

Any solution taken forward should be aligned with the work being undertaken as part of the F&MRS project implementation. This approach would help to ensure greater efficiencies in code governance reform development by having the appropriate target governance models in sight for both initiatives. For example, stakeholders have considered the option of faster switching arrangements being part of a new dual fuel retail code that; we would expect to subsume other retail code arrangements from existing single fuel codes. This could have a significant impact on code governance arrangements, and in particular on code administration, and therefore the final F&MRS outcomes should help to inform this package of work and any resulting solutions.

Whilst we have reservations around the licensing of code managers, we do see merit in the licensing of system delivery bodies. However, as with code administration, each code needs to be looked at individually as there may be greater benefit in the development of licensing in certain areas only. An example of this is the core central systems for gas industry arrangements that are currently managed by Xoserve. Whilst Xoserve are owned by a number of existing licensees, it was felt that the licensing regime was not sufficient to ensure strategic change can be delivered effectively. It is questionable that moving from a multiple licensing regime to a single system delivery body licensee would have a demonstrable benefit. As an alternative to licensing, Ofgem have undertaken an extensive amount of work over the last three years with industry stakeholders to review, and change, the Funding, Governance and Ownership arrangements (FGO) of Xoserve. These arrangements are due to go live in April 2017 and time will tell as to whether they deliver the necessary improvements to accountability and performance. If proven to be effective, this governance model could be extended to other system delivery bodies as an effective alternative to licensing.

An example of where licensing is already used for system delivery is for the role of the Data Communications Company (DCC) in respect of smart metering. In this arrangement the DCC is already the licence holder and has obligations under both its licence and under the Smart Energy Code (SEC). However, this licensing regime is in its early days and it is not yet clear whether operating under both code and licence arrangements will deliver effective strategic change. The DCC is also entirely funded through its code and licensing arrangements, via a Price Control Regime (PCR). Whilst funding of system delivery via a PCR may be appropriate in this instance, it should not necessarily apply to other licensing regimes, especially in respect of code managers.

Question 2: *What are your views on strengthening the licence of NGET to include new code management requirements rather than holding a tender to identify an appropriate code manager?*

We agree that it seems sensible to strengthen the licence conditions of NGET to introduce the new code management responsibilities instead of competitively appointing an alternate code manager. Whilst there could be a perceived conflict of interest with NGET's wider role in the

market, we believe that the design of licence conditions and code governance arrangements can be suitably robust to mitigate this risk.

Question 3: *What are your views on the merits and drawbacks of the four identified models for competitively licensing code management where applicable?*

We believe it may be too early to determine the model to be used for competitively licensing code management for the reasons given above. However, if the regime were to progress, then we do agree with Ofgem's initial analysis of the four options. Model 3 has clear advantages in terms of benefit delivery and ease of implementation although other models, such as Model 2, may be more appropriate to smaller codes or roles if these were considered appropriate to be in scope.

Chapter Four: Strategic Direction

Question 1: *Do you agree with the purpose of the strategic direction?*

Yes, we agree with the purpose of the strategic direction as set out in the consultation document. A cross-cutting strategic direction for industry codes to deliver strategic change should be central to aligning both code parties' and system delivery bodies' objectives, with that of agreed policy and wider changes in the market for the benefit of consumers.

Question 2: *Do you have any views on how the strategic direction should be developed and implemented?*

We believe it is important to determine what detail the strategic direction should contain and the level of detail necessary. This needs to be the right balance of being able to give clear direction to industry participants whilst not being overly prescriptive such that it could then have a detrimental impact on the ability to implement in a flexible and fluid way (as is often necessary).

Accountability is crucial to having a robust and effective strategic direction. It must be clear as to which party, or parties, are responsible for the various elements. Along with accountability for delivery there also needs to be accountability for support and participation in strategic change.

To deliver the appropriate level of accountability, there needs to be a supporting governance framework in place. This could be as simple as acknowledgement of the strategic direction within code Relevant Objectives or as a general requirement within any code administration agreement (whether we have licensed code managers or not).

Question 3: *How much detail do you consider should be included in the strategic direction?*

As above, the strategic direction should be the right balance of being able to give clear direction to industry participants whilst not being overly prescriptive such that it could then have a detrimental impact on parties' ability to implement change.

The strategic direction should contain an explanation of the key outcomes and a view of the cross-code reform that will be required and be clear on the overall benefits to consumers. In terms of accountability, the strategic direction should also outline the roles, responsibilities and accountabilities of stakeholders in delivering the strategic direction. Given the volume of strategic change parties will be expected to deliver over the next few years, clear direction over prioritisation will be essential.

Question 4: *Which specific projects do you consider should be included in the initial strategic direction?*

Activities and projects in Ofgem's annual forward work plan should be included within the strategic direction where there is an impact, or potential impact, on any of the industry codes or systems within scope. The strategic direction should also indicate any reliance, interaction or dependencies between projects.

If not captured by Ofgem's forward work plan, any other projects, that could be a result of BEIS or EU led work, should also be in scope of the strategic direction.

Chapter Five: Consultative board

Question 1: *What do you see as the core role and functions of the consultative board?*

We believe that the consultative board's focus should be on ensuring that cross-cutting code issues are dealt with and that code changes across multiple codes and or systems are coordinated to ensure the effective and economic delivery of strategic change.

We see the consultative board as an advisory forum with appropriate representation from industry code arrangements. This should include, but not necessarily be limited to, Code Panels, system delivery functions, suppliers, network owners, BEIS, Ofgem and consumer representatives. It is also important that the consultative board is established with representatives with the appropriate experience or skill and who can undertake this important role objectively and independently.

Whilst knowledge of the energy industry is an obvious advantage it is as equally important that there is input from members with project management and delivery experience, impact assessment skills, procurement knowledge and IT / systems awareness. For example, the industry recently undertook a process to appoint four Shipper Nominated Directors (SNDs) to the Xoserve Board, as part of the new FGO arrangements. The approach taken during the appointment process sought to identify individuals with specific experience and skills as defined by a detailed candidate specification that was developed by a group of cross-sector shippers. As an advisory body we see an important role developing for the consultative board with the ongoing review of the strategic direction and the development of a joint industry cross-code change plan.

We broadly agree with the proposed list of functions for the consultative board, as detailed within Table 6 of the consultation document and look forward to working with Ofgem and other stakeholders in further developing these proposals later in the year. We also see an important role for the consultative board in ensuring that the gas and electricity markets, and related industry process and systems, evolve in unison and that strategic change for a single fuel doesn't frustrate or prevent change in the other.

Chapter Six: Moving to new arrangements

Question 1: *What are the main impacts of the proposed new arrangements on existing projects?*

We agree that the implementation of a strategic direction and the consultative board could be done with little or no detriment to existing or upcoming projects. On the contrary, a strategic direction and consultative board could help to ensure that existing and future projects are delivered more effectively by providing a clear view on prioritisation where delivery conflicts exist.

The licensing of code managers and delivery bodies presents a far greater implementation challenge and would undoubtedly have a major impact on current arrangements and existing projects (depending on the extent to which this element is taken forward). We have also highlighted our concerns with the interaction with the F&MRS programme and how the potential introduction of a new retail code, and possible code consolidation, should be considered prior to any changes to code administrators' roles or responsibilities or the introduction of licensed code

managers as these changes could fundamentally alter the industry code landscape in operation today.

Question 2: *Would Ofgem's enhanced powers over strategically important modification proposals mean that our Significant Code Review (SCR) powers will be obsolete, and will the new powers form an effective substitute? Please explain your reasoning?*

If these measures were proven to be successful then we would agree that the existing Significant Code Review (SCR) powers would be obsolete.

If Ofgem are granted new powers, outside of the SCR arrangements, to initiate and to prioritise change, have backstop 'call-in' powers and the regime is supported by a strategic direction and the consultative board, we concur that the SCR process should no longer be required. We do not believe that the licensing of system delivery bodies and or code managers is necessarily required for the SCR powers to fall away, however, if implemented; the new arrangements would not be a barrier to ending the SCR arrangements.

Question 3: *What are your views on staggering the implementation of competitive applications for licences?*

We believe it is too early to determine the detailed process and timings for the competitive applications for licences. If implemented, this would not take place until later in 2018 and we believe there is, as mentioned above, significant work yet to do on the design of suitable licensing regimes and determination of where and how they will apply.

We also believe that further consideration should be given to the further enhancement of code administration (or code manager) arrangements that would apply across a number of codes, rather than dealing with them on an individual basis. For example, a code administration body, or code manager, could be responsible for a collective group of codes which would lessen the burden on any procurement or licensing activity and may deliver greater benefits to cross-code coordination and strategic change implementation. We believe this could be done within the existing code governance framework and should be considered alongside the work being done within the F&MRS programme.

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