

By e-mail to: [CodeGovRemedies@ofgem.gov.uk](mailto:CodeGovRemedies@ofgem.gov.uk)

Laura Nell  
Code Governance Remedies  
Ofgem, 9 Millbank, London SW1P 3GE

1 February 2017

Dear Laura,

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

We welcome the opportunity to comment on the proposed reforms to industry code governance being considered as part of work to implement the recommendations of the Competition and Markets Authority (CMA).

As you are aware, ELEXON is the code administrator for the Balancing and Settlement Code (BSC). However, our remit extends beyond basic code administration. We are responsible for managing and delivering the end-to-end services set out in the BSC. This includes responsibility for the delivery of balancing and imbalance settlement and the provision of assurance services to the BSC Panel and BSC Parties. We manage not just the assessment, but also the development, operation and implementation of changes to central systems and processes.

The views expressed in this response are those of ELEXON Ltd, and do not seek to represent those of the BSC Panel or Parties to the BSC.

We summarise our overall considerations below. Responses to the specific consultation questions can be found in Appendix 1. We offer more detailed commentary of the proposals in Appendix 2.

**ELEXON support for the overall objective**

We note Ofgem's overriding objective of these reforms is '*to achieve greater coordination across codes for identifying and delivering strategic change that benefits consumers and competition*'.

We recognise the need for greater co-ordination across codes and support this overriding objective.

We also support a 'responsibilities re-set' that provides for autonomous, empowered, pro-active code bodies. This is an important component in achieving the overall aim.

However, it is important that the overall outcome of the CMA's work leads to a reduction in complexity and cost to existing parties and new entrants and not to have the opposite effect. The recommendations and proposed actions must be carefully tested against this requirement and should be proportionate to the issues they seek to resolve.

**ELEXON does not believe that making code services a licensable activity is proportionate. We believe there exists simpler, proportionate and timely proposals to achieve the overall objective**

We do not support making code services a licensable activity since it has the potential to increase cost and complexity, and could inhibit innovation. Licensing alters the relationship between users and code service providers which, under the BSC, could mean the end of our independence from other institutions.

It remains unclear how a licence award process will lead to better delivery of strategic change. We explore this more fully in our detailed commentary (Appendix 2) but we summarise our proposal for a more proportionate and effective model which can achieve the same outcome, at the end of this cover letter. We ask Ofgem to articulate what would have been different in recent years if code bodies had been licensed as this would assist in understanding the issues that Ofgem is trying to address.

The development of a licensing regime will require primary legislation. We are concerned that this work will require parliamentary time and effort leading to delay when the overriding objective and expected outcomes could be delivered earlier by other means.

We believe that provisions already exist in the BSC that give Ofgem and the Gas and Electricity Markets Authority considerable influence of change. Equivalent provisions could be (i) expanded within the BSC as necessary and (ii) extended across all codes without the need for new licences.

Overall, we are of the strong view that the licensing approach is disproportionate to the perceived problem. A comprehensive cost-benefit analysis should be undertaken to determine the case for introducing a new licensing regime in comparison to other approaches. This assessment should be completed ahead of any primary legislation or subsequent development work.

**If Ofgem, notwithstanding this and other responses, were determined to proceed with a licensing regime for code services:**

- we agree it is right to consider end-to-end services as an essential pre-requisite for effectively co-ordinating the implementation of strategic change (i.e. one licence per code/delivery body (e.g. one for each of BSC, SEC&DCC, UNC&Xoserve));
- We believe all central systems delivery should be included (including the Data Transfer Service (DTS)) in any regime;
- We do not understand why a 'special case' would be proposed for the NETSO codes (CUSC, GC, STC). Indeed we believe this proposal challenges the whole concept of the need for licensing because:
  - All industry codes and delivery services originate through existing licence obligations (in the case of the BSC this is through the transmission licence);
  - If there is an argument (which we do not accept) to apply a regime to code services the argument must apply to all;
  - If Ofgem believes that competition is not necessary for certain codes because a particular licence is already in place then why has Ofgem been unable to drive strategic change under these arrangements?

**Strategic Direction**

We support the concept of a strategic direction. We can see benefits in Ofgem providing a vision for strategic change and introducing mechanisms to provide clear resourcing signals for industry. Steps to ensure there is clarity in accountability should also be welcomed to ensure that change is delivered in the interests of consumers and that benefits to consumers and competition are delivered efficiently. The strategic direction needs to look forward to the next 5-10 years to ensure industry and code managers can plan their costs, resources and any commercial considerations to support strategic change.

Ofgem could ensure that it is engaged and resourced to support any new regimes, and should make better use of existing opportunities to exercise its influence and input through the existing channels (engaging in industry change through attending and contributing to code panels and working groups discussions).

We encourage Ofgem to publish a strategic direction earlier than Q4 2017 as code managers are already planning change and investment towards the end of this decade.

### **Consultative Board**

We are uncertain of the benefit of a consultative board. There is risk that such a body would introduce additional costs and a new tier of governance. Membership could only be determined once the purpose of the board is understood (for an example if it was an 'expert' group this would not lend itself to participation of senior personnel from across the industry, whereas 'strategic' group would).

We would be supportive if such a board could be constituted in a way which does not introduce unnecessary bureaucracy or costs, or any clouding of responsibilities. If so we would agree with the CMA's observation that it is essential for code administrators and delivery bodies to be active members of the proposed consultative board. In addition, the activities of the consultative board need to be backed up by firm commitments from organisations that will fund and support strategic change (energy industry participants).

### **Industry code panels**

We believe clarity is required over the enduring role of industry code panels. We believe industry code panels are an important check and balance in the code management and change process. It is not clear how Ofgem intends that existing code panel responsibilities evolve in light of the proposals to make code managers owners of their respective codes with powers to drive changes to their respective codes. We would observe that the current BSC Panel comprises of a wide cross section of members from across industry (but required to act independently), consumer groups and independent members as well as Ofgem.

A licensed code regime would also change the perception and relationship between code managers and Code Panels (and indeed code users). Code managers are less likely to be seen as independent, respected advisors and will be perceived as an agent of the regulator.

Further, since industry code panels are not legal entities, we do not see how code panels can act as contract counterparties in the appointment of licensed code bodies.

### **ELEXON's alternative proposal for a proportionate, timely and effective model for delivering strategic change**

We believe the stated overall objective and expected outcomes could be achieved by other means, as follows, using existing powers and without encountering the delay associated with the introduction of licences. Provisions already exist in the BSC (and the Code Administration Code of Practice) that give Ofgem and the Gas and Electricity Markets Authority considerable oversight of change. This includes the capability for the Authority to, at any time, request that the BSC Panel re-prioritise Modifications, and amend timetables for the development, assessment and implementation of changes. The Authority is also able to direct National Grid (the licence holder) to step in to deliver the BSC Modification process where ELEXON (or the BSC Panel) has failed to comply with the Modification procedures or any Authority direction in relation to the Modification procedures. Ofgem has never had the need to execute such provisions, however equivalent provisions could be extended across all codes.

Ofgem has the Significant Code Review (SCR) mechanism at its disposal to marshal cross code change. Ofgem could utilise its SCR powers and could ask Code Managers to lead on specific pieces of work or project manage changes under these processes.

ELEXON has a long and proud history of successfully providing support for strategic change in collaboration with industry and Ofgem. This is demonstrated through providing expert advice and guidance on activities such as the smart metering technical solution, our [proposals](#) for moving to full

half hourly settlement (first submitted to Ofgem in 2012 and later taken by Ofgem under its Smarter Markets programme), our work on developing the original CACoP and our innovations in Code management (code forward work plans and cross code forums). We have been able to provide this support through clearly signposting our activities and costs through transparent budget and planning activity. Ofgem should require equivalent provisions to be extended across all codes.

Work is already underway between code managers to bring together Panel plans into a single forward looking plan and to co-ordinate implementation of European Network Code changes.

In short, many of the key provisions Ofgem would presumably seek to include in a licence could be included instead in each code to the same effect, in a more efficient, timely and proportionate manner.

### **Consolidation and consideration of models for Code services**

We believe that consolidation of code administration services will probably bring more benefits than licensing. Consolidation can also be achieved without first introducing licensing. It would allow for industry parties to have a reduced number of interfaces for managing code activities and changes. Consolidated services may improve co-ordination and harmonisation of change and change processes.

Ofgem should consider what the best operating model for a Code Manager/Delivery body is. Ofgem has a number of existing bodies to compare and it can assess their performance against the behaviours and objectives it is seeking. For example, such criteria could include customer satisfaction, transparency of costs and performance KPIs, proactiveness, service improvement, thought leadership, independence, cost control, support to industry, Ofgem and government. As part of this Ofgem could reflect on the different business models of the various bodies including current funding, for profit vs not for profit, governance and incentives to identify what aspects, if any, of those business models are driving those behaviours. Ofgem can then set out the features of what the operating model should look like and use this to shape how code services are delivered.

### **We believe it is possible to achieve the desired outcomes in a more timely and proportionate manner and using existing Ofgem powers by:**

- amending code panel and code manager/delivery body objectives in the existing codes/licences including relative prioritisation by Ofgem of such objectives if necessary;
  - include a specific Applicable Objective under each code that refers to the need to consider benefits to consumers;
- inserting appropriate Ofgem oversight of change into code provisions;
- adding step-in powers into industry codes (equivalent to the BSC);
- appropriate empowerment of code managers to raise changes;
- the provision by Ofgem of a strategic direction (in accordance with proposals in this consultation);
- Utilising the existing SCR powers, as they are intended to drive strategic change;
- Code administrators/delivery bodies required to provide a service based on plans and budget that has been transparently shared with the stakeholder community setting out the priorities and activities to be delivered in alignment with the strategic direction, based on operating models Ofgem believes best delivers the objective.
- Ofgem take a more active approach in, and articulate its position more, when participating and contributing to industry Panels and workgroups;

- Industry and Ofgem support for the current initiatives to develop a cross code forward work plan and plan for implementing European Network Code changes.

We are not convinced of the benefit of the consultative board. However if a board was established that added value and did not introduce unnecessary cost and bureaucracy we would see the potential for it to provide oversight (with code manager/delivery body participation) to develop and manage cross industry plans for delivering strategic change. It could also create a feedback loop between Ofgem revising strategic direction and taking advice from the consultative board in setting any revised direction.

#### **Continued engagement with Ofgem**

As experts in code administration and code delivery with deep industry knowledge, especially expertise in settlement, we will continue to offer support to Ofgem in implementing the CMA's recommendations.

If you would like to discuss any areas of our response, please contact David Jones, Head of Strategy, on 020 7380 4213, or by e-mail at [david.jones@elexon.co.uk](mailto:david.jones@elexon.co.uk).

Yours sincerely,

Mark Bygraves  
CEO, ELEXON

List of enclosures

*Appendix 1 – Responses to specific consultation questions*

*Appendix 2 – Detailed commentary on proposals*

## Appendix 1 – Responses to specific consultation questions

### CHAPTER: Two: Scope of the new 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?

No, ELEXON does not believe a licence regime is a necessary, timely or proportionate approach to delivering greater strategic change. Please see our detailed commentary for further clarification. However if a licence regime is required then this should apply to all centralised codes and services, not just the CACoP Codes.  
We do believe, however, there is merit in greater co-ordination across existing codes and services under a consultative board and the proposed Ofgem strategic direction.

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

See Q1

Yes, if licensing is required then all codes and services, including the DTS should be included. The DTS as it forms part of the infrastructure that's needed for the market to function and will certainly be subject to impacts from strategic change, it would therefore be consistent that changes are not frustrated by having central services outside the new regime.

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

Yes – We do not see any justification for making code management and delivery body services a licensable activity. We remain concerned that the proposed regime has the potential to increase cost and complexity, and could inhibit innovation. It remains unclear therefore how a licence regime is proportionate and would equate to better strategic change. ELEXON has supported a range of strategic activities over recent years, including our current support on Ofgem's Half Hourly Settlement and Faster Switching programmes. We are concerned that the proposed regime may hinder the provision of such support in the future.

**A comprehensive cost-benefit analysis should be undertaken to determine the case for introducing a new licensing regime ahead of any primary legislation or subsequent development work.**

We are of the strong view that the licensing approach is disproportionate to the perceived problem. The development of a licensing regime (which requires primary legislation) will require parliamentary time and effort with associated delay, when the overriding objective and expected outcomes could be delivered earlier by other means as follows.

**It is possible to achieve the desired outcomes in a much more timely and proportionate manner using existing Ofgem powers by:**

- amending code panel and code manager/delivery body objectives in the existing codes/licences including relative prioritisation by Ofgem of such objectives if necessary (the existing "Applicable Objectives" are akin to principles and have been expanded in the past). For example include a specific Applicable Objective under each code that refers to the need to consider benefits to consumers;
- inserting appropriate Ofgem oversight of change into code provisions;
- adding step-in powers into industry codes (equivalent to the BSC);
- appropriate empowerment of code managers to raise changes;

- the provision by Ofgem of a strategic direction (in accordance with proposals in this consultation);
- Cross code initiative on forward work plans
- Utilising the existing SCR powers, as they are intended to drive strategic change;
- Code administrators/delivery bodies required to provide a service based on plans and budget that has been transparently shared with the stakeholder community setting out the priorities and activities to be delivered in alignment with the strategic direction, based on operating models Ofgem believes best delivers the objective.
- Ofgem take a more active approach and articulate its position more, when participating and contributing to industry Panels and workgroups;
- Industry and Ofgem support for the current initiatives to develop a cross code forward work plan and plan for implementing European Network Code changes.

We are not convinced of the benefit of the consultative board. However if a board was established that added value and did not introduce unnecessary cost and bureaucracy we would see the potential for it to provide oversight (with code manager/delivery body participation) to develop and manage cross industry plans for delivering strategic change. It could also create a feedback loop between Ofgem revising strategic direction and taking advice from the consultative board in setting any revised direction.

See our more detailed response on consultative board below.

**Subsequent revisions to the Code Administration Code of Practice, prompted by Ofgem's third review of industry code governance, have placed a clear obligation on code bodies to co-ordinate their activities.**

This expansion in the remit of code bodies is a key differentiator compared to the obligations in place at the time of the CMA's review of historic changes (e.g. P272. which was progressed when no such obligation to co-ordinate change existed, although notwithstanding this the non-BSC issues were signposted to Ofgem by ELEXON during the BSC discussions).

**Proposals to extend the full regime to some, but not all code managers appear anomalous.**

We do not understand why a 'special case' would be made for the NETSO codes (CUSC, GC, STC). Indeed we believe the proposal to exempt these challenges the whole concept of the proposal because:

- All industry codes and delivery services originate through existing licence obligations (in the case of the BSC this is also through the Transmission Licence making it a NETSO Code and should be treated consistently as such);
- If Ofgem believes that licensing competition is not necessary for certain codes because a particular licence is already in place then why has Ofgem been unable to drive strategic change under these arrangements?

**If licensed code managers are to be held to account under their licence for the delivery of change there must be clarity regarding the decision-making responsibilities of both licensed code managers and unlicensed code panels.**

Further, since industry code panels are not legal entities, we do not see how code panels can act as counterparties in the appointment of licensed code bodies.

**We remain concerned that licensing code bodies will not change the behaviour of those (already licensed) industry players who, in the view of the CMA, are slowing change.**

**Impact on roles, accountabilities and relationships of affected entities**

*Code Managers:* The consultation introduces the concept of a code manager as an extension of the code administrator role. The code manager would deliver strategic change and provide services to the industry. This would include working with the industry to prioritise change. We believe ELEXON already offers these services under the BSC.

We note, however, that a barrier to pro-active change delivery is the limitation in the codes framework that prevents code bodies from proposing change. We therefore support the CMA proposal that code managers should be given the capability to raise changes to their respective industry codes. A further extension of these powers might enable code managers and industry code panels to raise changes in other industry codes. This might be limited, for example, to circumstances where such changes were needed to facilitate the development and/or implementation of changes under their own industry code.

*Code Delivery bodies:* Ofgem proposes these entities would be responsible for delivering and managing the systems that underpin the code(s). They would be required to deliver co-ordinated system and process change. ELEXON already does this under the BSC by managing the assessment of potential changes, undertaking the systems impacts and cost (across BSC central systems and other party systems) and planning and implementing the required changes.

*Code Owners:* Ofgem proposes the code manager may also become the 'code owner'. This implies moving the obligation to have a code in place from current licensees (e.g. National Grid) to the code manager. We recognise that changes would need to be made across many licences to put this element of Ofgem's proposal into effect but question the objective and effect of transferring this obligation.

*Code Parties:* Ofgem notes that licences may need to be amended to oblige licence holders to support strategic change. This clearly demonstrates that, if the problem is incumbents not participating in change processes or otherwise delaying the implementation of change, there already exists a mechanism (their licence) by which they could be obliged to participate).

*Code Panels:* Code panels are an important check and balance in the code management and change process. Ofgem proposes code administrators become autonomous and empowered to deliver strategic change and therefore the relationship and responsibilities between the code panel and code manager will need to be re-assessed.

The role of industry code panels varies from one code to another, however, at the core, industry code panels primary responsibility is to make recommendations and determinations in respect of changes to industry codes. This includes (to various extents) oversight of the assessment, development and implementation timetables. It is not clear how Ofgem intends existing code panel responsibilities might evolve in light of the proposals to make code managers the owners of their respective codes with powers to drive changes to their respective codes.

**Accountabilities of Code Managers.** If as Ofgem proposes, licensed code managers are to be held to account under their licence for the delivery of change there must be clarity regarding the decision-making responsibilities of both licensed code managers and unlicensed code panels. This is important since the entity with responsibility for the following key decisions will drive the change agenda. These include:

- Raising / rejecting new changes;
- Prioritising or re-prioritising changes;



- Setting assessment timetables;
- Establishing workgroups (including membership and terms of reference);
- Directing consultations;
- Assessing proposed changes against clear objectives;
- Recommending (or reviewing and revising) implementation dates; and
- Assessing and determining the progression route for a change (i.e. is it code panel self-governance, fast-track, urgent, standard or strategic and subject to regulatory oversight).

Further, the current code panels are, generally, founded in the industry codes which are established by existing licenses. Their composition varies. Members are drawn from industry and non-industry organisations. Some of these organisations are already licensed, some are not licensed. Some members are required to act impartially, others act as representatives. Significantly, industry code panels are not legal entities. Since industry code panels are not legal entities, we do not see how code panels can act as contract counterparties in the appointment of licensed code bodies.

**Relationship of code bodies to Ofgem.** We are mindful of the value that parties place on the impartiality of code bodies. We are concerned that code managers and delivery bodies may be perceived as delivery arms of the regulator, rather than impartial, independent critical friends.

**Consolidation.** We believe that consolidation of code administration services will probably bring more benefits than licensing. Consolidation can also be achieved without first introducing licensing. It would allow for industry parties to have a reduced number of interfaces for managing code activities and changes. Consolidated services may improve co-ordination and harmonisation of change and change processes.

While code administration processes could (we assume at least initially) remain set out in their individual codes, consolidation of service provision would offer further consistency in how these separate processes were delivered. We note, however, that the BSC would need to be amended to overcome the “vires” issue before any organisation (whether ELEXON or its successor or importantly, any subsidiary company could provide (or seek to provide) any code administration services in addition to the administration of the BSC. This is because the BSC prevents ELEXON (or anyone else performing the ELEXON role) from participating in tenders and activities outside the current services defined in the Transmission Licence and the BSC.

We strongly believe it is essential to avoid further proliferation of code administrators. Any opportunities for consolidation should enable all existing code administrators to be eligible and the existing restrictions on our participation in any other activity must be removed.

If consolidation of code bodies is a goal of Ofgem, then this could more efficiently be achieved by Ofgem encouraging the senior leadership teams within the industry participants which are (with the exception of the DCC) the shareholders in each code body, to bring about consolidation. Clearly major decisions, such as choice of funding model for the consolidated services, would have to be determined up front.

## **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?

We support an end-to-end approach for code services. We agree it is right that end-to-end services are an essential pre-requisite for effectively co-ordinating the implementation of strategic change (i.e. one licence per code/delivery body (e.g. BSC/SEC&DCC/UNC & Xoserve)) to ensure there is no conflict of resourcing and planning across the end to end process. This will ensure that a single entity has oversight and responsibility for change and allows for greater efficiency in managing and co-ordinating change and avoid unnecessary duplication or potential for something to be missed.

**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 do not support this approach – it is inconsistent with the arguments that suggest competition between code bodies will drive service improvements and efficiency.

If it is simply a matter of strengthening the existing licence for NGET we cannot comment on the merits of this as we do not know what 'strengthening means'.

However if it is believed that adding new obligations to NGET's licence will be adequate then we would agree this can be the same for all existing codes (for example the BSC is derived from the transmission licence and should be considered and treated as other NETSO codes; other codes are also derived from licences which could therefore be 'strengthened'). We have highlighted how consistency could be achieved across code services to support strategic change in our proposals in this response for '*A proportionate, timely and effective model for delivering strategic change*'.

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

We have a marginal preference for bespoke, sole-provider, licences. While these imply a greater role for the regulator they maintain a through-line of accountability.

We doubt whether permissive licences would promote more competition in code management services as interested bidders would participate anyway and a permissive licence acts as an additional step in advance of any potential pre-qualification for a specific service.

**Question 4:** What are your views regarding which model(s) may be appropriate for different codes, or types of codes?

We believe all codes should follow the bespoke (sole provider) licence model. However there is a need to ensure there is no conflict between the obligations placed on the code manager by its licence and those placed on it under the relevant code or any separate contract awarded by an unlicensed entity (e.g. code panel or other award body)

## **CHAPTER: Four: Strategic direction**

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

Yes – We can see benefit in Ofgem setting clear expectations regarding policy and the outcomes needed from industry codes to deliver this policy. We therefore support the production of strategic direction that translates BEIS (or DECC as was) Strategy and Policy Statement into appropriate signals as to how Ofgem expects high-level policy decisions to be implemented via code changes.

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

Yes – input should be sought from code managers and code panels as well as industry parties. The direction should take account of cross-code forward work plans. The consultative board should support the development and maintenance of the strategic direction. In addition Ofgem should understand how the newly formed Energy Innovation Board will input to the setting of strategic direction.

*Interaction with forward work plans*

We agree with the observations made regarding the development of code administrator work-plans. We believe these work-plans could provide significant value illustrating how industry codes will need to develop to deliver Ofgem’s stated strategic direction.

ELEXON has already developed a forward work plan with the BSC Panel for the purposes of assessing the future change landscape that will impact the BSC. This work plan has been well received by industry. We have also worked with our code administrator colleagues across the industry to implement a cross-code forward work plan. We believe this activity and the resulting plan will be an important component in better co-ordinating change and in supporting the development and maintenance of an Ofgem strategic direction.

Together, Ofgem’s strategic direction and the industry code work-plans will enable industry parties, code panels, administrators and delivery bodies to monitor and allocate capacity across the portfolio of change. Code panels, administrators and parties will also be able to better interpret what should be considered as ‘material’ for the purpose of determining their relative position in the change process (i.e. self-governance, nominal code panel oversight, or Ofgem-led strategic change).

We note there may need to be changes to existing codes in order to recognise and accommodate the strategic direction.

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

We believe the strategic direction should focus on required outcomes, rather than dictating the details of required changes. The time horizon should be greater than 3 years (e.g. 5-10 years) to facilitate longer-term planning consistent with the needs of industry parties to consider change programmes and investment decisions. The direction should also allocate clear responsibilities for supporting and delivering outcomes.

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

HH Settlement (elective and mandatory); Faster Switching; European Harmonisation and Network Codes/Guidelines; Demand Side Flexibility, Storage and Aggregation.

**CHAPTER: Five: Consultative board**

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

We are not convinced of the benefit of the consultative board. However if a board was established that added value and did not introduce unnecessary cost and bureaucracy we see the key roles as providing the following which is consistent with the findings of the CMA:

- a) **Strategic planning input:** a forum for Ofgem, code administrators and the industry to discuss the development of Ofgem's strategic direction and industry code work plans, and ensure consistency across codes. The board could assign a lead code manager to any cross code work;
- b) **Tactical advice:** a forum for Ofgem, code administrators and the industry to discuss cross-cutting issues, best practice considerations and the system-level functioning of the code regime; and
- c) **Further governance reform:** a forum for Ofgem, code administrators and the industry to consider long-term system-level issues, such as revisiting the scope of codes, governance arrangements or reducing the complexity of the regime (e.g. by harmonising certain processes).

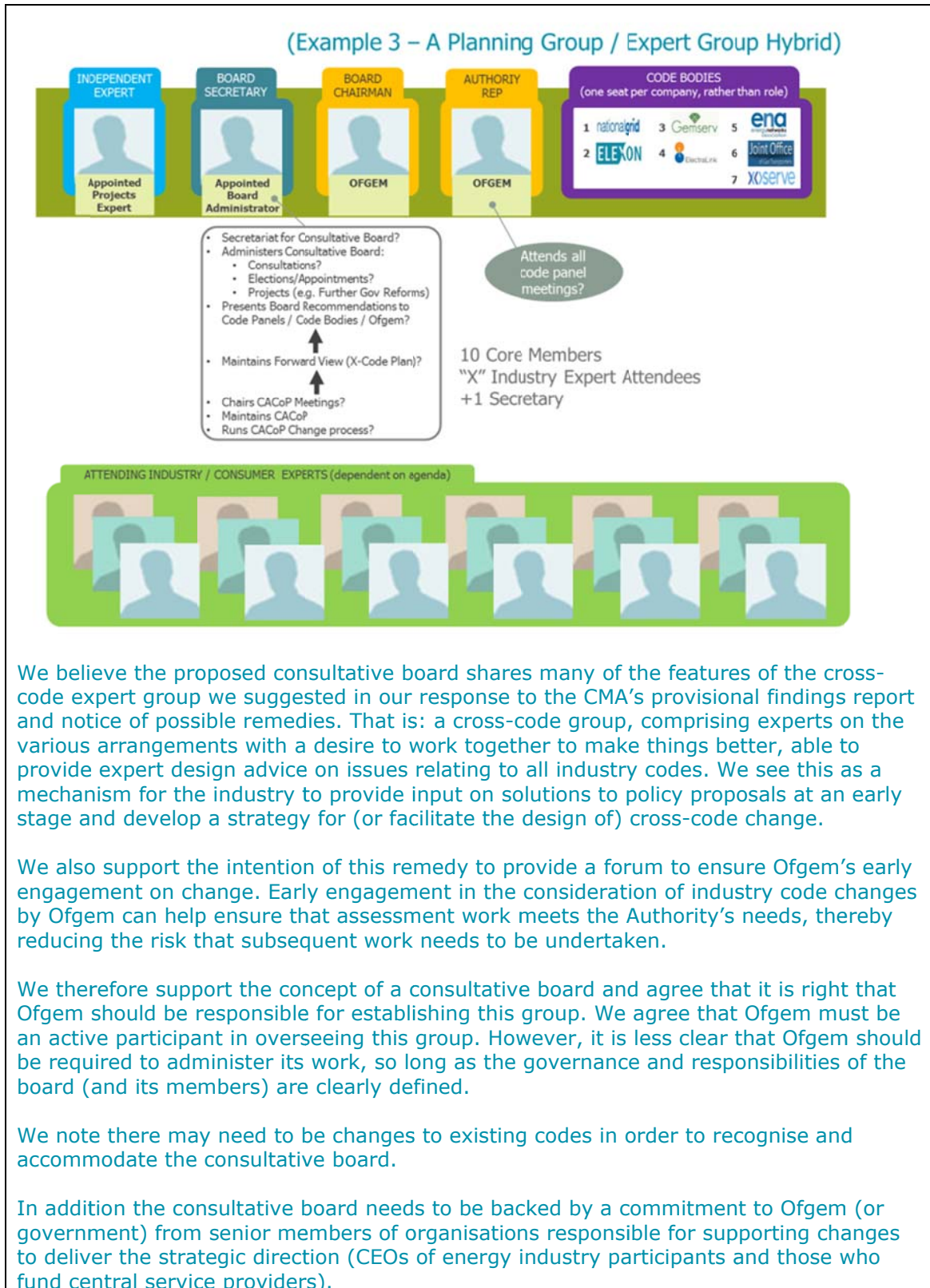
We do not believe, and therefore do not agree with the CMA findings, that this body should be responsible for:

- monitoring the performance of code managers (and, we assume, code panels) – this is a role for the regulator under the terms of a licence or the client organisation/Panel (or Parties) under the terms of the contract;
- operational activities conducted by code managers (these should remain the responsibility of the licensed entity, otherwise responsibility is confused); or
- the commissioning of third parties to manage the implementation of change.

To deliver effectively it should be:

- Focused on co-ordinated delivery of codes (in response to Ofgem's Strategic Direction)
- Small enough to be agile
- Able to liaise with experts / consider expert group findings as needed without creating bureaucracy
- Able to engage with strategic experts / establish sub-groups to consider governance as needed
- Able to take action to ensure required changes are considered (if not forthcoming from industry)

Its composition could be:



Careful consideration will need to be given to the mechanisms by which a consultative board would deliver its operational support, monitoring and control activities to ensure these dovetail with the standard industry change processes and responsibilities.

#### **CHAPTER: Six: Moving to new arrangements**

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

Not enough information to comment at this stage.

**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.

Yes, these new provisions would appear to supersede the need for an SCR process. However the existing SCR process could be used to great effect without the need for further change. See our detailed comments for more information.

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

We do not believe there is benefit in making code services a licensable activity.

## Appendix 2 – Further commentary on proposals and BSC specific issues

### 1.1 General Principles

#### Responsibilities re-set

1.1.1 We support a 'responsibilities re-set' with autonomous, pro-active code bodies.

- We agree with the CMA's conclusion that the independence and impartiality of code administrators is important.
- Code administrators should be code managers and should be more proactive. They should further develop their independent, impartial autonomy, expertise and critical friend functions.
- Code managers and code delivery bodies should have a responsibility to co-ordinate change across codes and work in line with any published strategic direction.
- We support the CMA's proposal that code bodies should be given powers to raise changes to their respective industry codes.
- Existing code panels<sup>1</sup> (in addition to code managers/delivery bodies) should also have a responsibility to co-ordinate change across codes and work in line with any published strategic direction.
- We agree with the CMA's recommendation that code bodies act in the interests of competition and consumers. We believe that this requirement should be further reflected in the codified objectives of code managers and industry code panels.
  - It should be clear that code panels have a responsibility to act impartially and in the interests of competition and consumers.
  - Code panels should support and follow the principles of critical friend (as set out in the CACoP).
  - Code panel objectives should be aligned across codes and should be consistent with those of the regulator to ensure self-governance decisions taken by code panels are consistent with regulatory objectives.
- There must be transparency in the interactions between code administrators and their various stakeholders.

#### Licensing and competition

1.1.2 Licensing and competition are different and will achieve different things. One does not require the other. They can be delivered independently but are not mutually exclusive. Each carries pros and cons compared to the status quo.

- **Licensing** offers control by the regulator and can drive behavioural change/improvement through regulatory effort (e.g. via the development and application of standards and incentives). We note that the CMA indicated the purpose of licensing code administration and code delivery to be twofold:

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<sup>1</sup> We use the term code panels to refer to existing code panels and equivalent code change bodies across all current (and future) industry codes.

- To ensure that code administrators act independently of industry parties in the interests of competition and consumers; and
- To enable Ofgem to monitor the performance of code bodies in relation to the project management of change and intervene (by use of appropriate incentives and powers) to remedy underperformance.

Competition offers the opportunity to consolidate service provision.

## 1.2 Commentary on the CMA's case for change

- 1.2.1 We have been advocates of half hourly settlement for many years and have been actively utilising a forward view of industry change with the BSC Panel for some time. We were therefore interested in the CMA's conclusions<sup>2</sup> that:
- established industry participants, whose interests are not aligned with those of customers, have undue influence on decision-making; and
  - code changes that are in customers' interests have been delayed or not implemented due to parties' conflicting interests and limited incentives to deliver the reforms.
- 1.2.2 **We see important differences between the CMA's references to Project Nexus as an issue in the gas sector and P272 in relation to electricity.**
- 1.2.3 Project Nexus has suffered from a lack of co-ordination between separate IT projects being progressed to implement the required changes. In contrast, the issues associated with Modification P272 are found in the assessment of complementary changes across codes (rather than the specific implementation steps themselves). These include a lack of defined responsibility (or powers) for co-ordinating complementary changes across codes and the provision (by incumbent parties) of information and support when changes are being assessed. Unfortunately these P272 issues were predicted in discussions between ELEXON and the BSC Panel back in early 2012 when Ofgem was encouraged to raise a Significant Code Review to ensure sufficient cross code coordination. However this was not an approach Ofgem adopted.
- 1.2.4 We are pleased that the CMA's report offers no criticism of ELEXON in respect of P272. Indeed, it indicates that code bodies should be given powers to raise changes to their respective industry codes in order to facilitate the timely progression of strategically significant changes. We agree that the independence and impartiality of code administrators is important in this regard.
- 1.2.5 We also note that subsequent revisions to the Code Administration Code of Practice, prompted by Ofgem's third review of industry code governance, have placed a clear obligation on code bodies to co-ordinate their activities. This expansion in the remit of code bodies is a key differentiator compared to the obligations in place at the time of P272.
- 1.2.6 However, with respect to licensing of code bodies, we consider the theory of "principal-agent" particularly relevant. That is: the body to suffer the consequences of an act (remedies under a licence) should be the body best able to deliver the desired behaviour. Our concern is that

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<sup>2</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/531204/overview-modernising-the-energy-market.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531204/overview-modernising-the-energy-market.pdf)



licensing of code bodies will not change the behaviour of those (already licensed) industry players who, in the view of the CMA, are slowing change.

### 1.3 BSC-specific concerns

#### Profit / Liability

- 1.3.1 While ELEXON Ltd. is a wholly owned, arms-length subsidiary of National Grid, our funding arrangements (which see our costs transparently issued to industry for comment and passed directly on to BSC Parties) enable us to operate impartially and independently from our shareholder (who bears no liability or obligation to provide finance or financial support to ELEXON Ltd).
- 1.3.2 Our delivery of impartial services to the industry is further underpinned by our not for profit status and our ownership structure (which mitigates the risk of undue influence by electricity suppliers or generators both collectively and individually). Such impartiality is particularly important in relation to the assessment and implementation of change.
- 1.3.3 While we understand that governance and funding arrangements varies across industry codes, we remain concerned that our not-for-profit funding model (which we believe supports our independence) may not be compatible with the use of incentives (e.g. penalties) imposed under a licence.
- 1.3.4 The prospect of such incentives changes the risk profile associated with delivering BSC services. It could be that such risk would need to be priced into the delivery of BSC services. Moving away from the current cost pass-through model (mandated in the BSC) is likely to have funding, financing and liability implications for ELEXON. This will inevitably increase the cost of delivering the BSC borne by BSC Parties and ultimately by the consumer.

#### Vires

- 1.3.5 We are currently restricted from delivering services that are not provided for under the BSC. These restrictions would need to be removed before any organisation (whether ELEXON or its successor or, importantly, any subsidiary) could provide (or seek to provide) any code administration services in addition to the administration of the BSC.

#### Award of contract

- 1.3.6 The consultation references award of service via a contract let by code panels. As we have previously noted, this would require a fundamental re-set in the nature of code panels since they are not, in themselves, legal entities and are therefore unable to enter into contracts. In addition code Panels may not be suitably experienced in procuring services.
- 1.3.7 In a number of cases, thin shell companies hold responsibility for delivering code services (e.g. MRASCo) and the directors of these shell companies often sit on the relevant code panel. They may even comprise the same personnel, but they are different entities with different responsibilities and obligations. However, this is not the model under the BSC.
- 1.3.8 Consequently, a new entity would need to be created in order to contract with ELEXON.
- 1.3.9 Having considered the implications for the BSC we believe it remains unclear which entity would be licensed. For example, would it be:
  - Shell-BSCCo (a new shell company operating as the BSCCo) or ELEXON Ltd. (the provider to the new Shell-BSCCo)?

- ELEXON Ltd. (a thin shell company) or 'new-ELEXON' (a newly formed company comprising assets and systems transferred and staff TUPED from the old ELEXON Ltd that provides code management services)
  - Or some other variant.
- 1.3.10 We believe establishing these new organisations, with associated funding, financing and contracting mechanisms / variations would represent undue cost and bureaucracy that would outweigh the perceived benefits of a licensing regime.
- 1.3.11 We also believe that any licensing and competition regime should seek to provide for a level playing field and would therefore welcome clarity on how the BSC situation might compare to the situation for other codes. For example:
- Is it that MRASCo would be licensed, or would it be the provider (currently Gemserv)?
  - If MRASCo is to be licensed, does the MRA Executive Committee (MEC) appoint MRASCo? As the personnel on the MEC and MRASCo Board are the same individuals, this would create a conflict of interest.
  - If the Joint Office is licensed, who lets a contract to it since the UNC Panel is not a legal entity?
- 1.3.12 We therefore believe that if this situation arises it is appropriate for Ofgem to make the awards/appointments. If it is not to be Ofgem then we query whether there should be a central appointing entity. This might appear similar to the LCCC, established under EMR. However, given that the LCCC, which was originally intended to be a shell company awarding contracts now comprises over 50 people, we note that putting such a body in place creates yet more cost and bureaucracy and so do not advocate this approach.