



## **Consultation: Industry Code Governance: Initial consultation on implementing the Competition and Markets Authority's Recommendations**

### **Response from E.ON**

#### **General Comments**

Reform of industry code governance arrangements has been ongoing since Ofgem first started to examine the issue almost 10 years ago. Since then we have experienced 3 'code governance review' initiatives by Ofgem. The recommendations within the CMA investigation into the retail energy sector regarding industry codes can be seen as a continuation of this activity.

It is perhaps inevitable that arrangements that are designed to manage and facilitate change will themselves be scrutinised and amended. We support proposals that will make the industry change process more efficient and responsive to the industry and consumer's needs. Some of the recommendations within this consultation, if implemented correctly, could have the potential to improve the functioning of the change process therefore we would support the work proposed by Ofgem.

The activity articulated in the consultation can be divided into 3 key work areas and we have some general observations to make against these:

#### **Strategic Direction**

Having an overarching strategic direction of change for the industry is a sensible aspiration. It should provide clarity to all parties with regard to what changes can be expected and when. It could provide clarity regarding potential conflicts that may exist between the delivery of different policy initiatives and also provide visibility for areas of policy development that have interdependencies.

Two elements are required for the proposed Strategic Direction to be successful. Firstly it needs to be 'owned' by someone who has appropriate accountability and also relevant oversight of all relevant industry policy areas. It can't be left 'for industry' to own and to maintain. The logical choice for custodian of the Strategic Direction is Ofgem although they would need to consult with industry and Government on a regular basis to ensure that it is kept up to date.



The second key requirement is for the scope of the Strategic Direction to be clearly articulated and understood. All parties will have slightly different perspectives of the world based upon their organisations commercial model and interest.

As we have suggested that this Strategic Direction be owned by Ofgem and as the scope of this review is industry code governance we believe that changes impacting upon 'industry codes' is a good basis for the scope.

The Strategic Direction could be a useful tool for Ofgem to include in their own annual Forward Work Planning activity and also in their dialogue with Government regarding future policy initiatives in the energy sector.

### **Consultative Board**

Of the three recommendations from the CMA regarding code governance the proposal for a Consultative Board seems to have the least clarity as to its role and value.

It is clear to us what it shouldn't be, an additional level of industry governance bureaucracy, as this will frustrate and slow change and add unnecessary costs to the process.

The role and purpose of the Consultative Board first needs to be defined and the logic and value of this articulated and justified. Our initial view is that the Consultative Board could perhaps be more of a Consultative Forum.

It could be used as a sounding board for Ofgem to engage with all stakeholders regarding the Strategic Direction. Its key task could be to test assumptions and to hear feedback regarding policy areas and the impacts of these for stakeholders. If framed as such it might be a useful addition to the current arrangements and complement the development of the Strategic Direction.

### **Licencing**

Perhaps the most controversial aspect of the CMA recommendation, we believe that this consultation missed some of the issues which should be first considered.

A key question that should be answered is how many code administrators should there be?

Should there be one administrator for all codes?

From experience of the existing arrangements where a specific code administrator looks after multiple codes they tend to harmonise the administrative processes across them (documentation, website, helpdesk and stakeholder engagement). This outcome could be



seen to address many of the concerns raised by stakeholders to the CMA which were similar to those highlighted in the recent Ofgem 'Code Governance Review' initiatives.

Expanding this logic might see code administration activities for all codes, or for logical subsets of codes (retail, wholesale etc), provided by a single service provider.

Counter to this is an argument that competition between Code Administrators provides an incentive for innovation and provides for improvements in service. This aspect of the code governance arrangements should be examined as part of this review by Ofgem.

Something that is clear from the current arrangements is that competition is a preferable outcome to ensure that services are provided to the highest standard. This can be achieved either via direct commercial arrangements (e.g. as seen in the provision of code administration services for the MRA or SPAA industry codes) or via the competitive award of a licence (e.g. as seen with DCC licence for smart metering services).

The winner of the competitive tenders for services may have a variety of different business models and may potentially be a non-profit organisation. Individual business models are less relevant than ensuring that incumbent providers do not become complacent via a monopoly provision of services.

The scope of what is being described for a potential licence regime also needs to be considered and set out clearly. The current code governance arrangements have evolved in a haphazard manner with no clear planning or blueprint as to what they should look like. Each new code has looked at existing arrangements and picked parts that were perceived to work well or has tried new approaches to issues.

The Code Governance Reviews by Ofgem have failed to reverse or amend any existing arrangements, mostly as a result of opposition from the incumbent code administrators who have a vested interest in maintaining the status quo.

It would be useful for Ofgem to clearly define what an appropriate model for industry code governance should look like. The consultation seemed to confuse code administration and code delivery and created a new role of code manager.

The benefit of licencing code administration was not clear to us from the consultation (smaller commercial value and less impact upon the market and consumers).



The benefit of licencing code delivery bodies is clearer. This role includes the provision of central IT and services to the market (e.g. wholesale settlement, green deal administration, smart metering communication services and customer switching arrangements).

These have significant impacts upon market participants and the costs and service that consumer's experience. Recent evidence from Project Nexus shows how a lack of accountability and control can have negative consequences for the market.

Unlike the suggestion in the consultation we therefore see the Smart Energy Code (SEC) as the logical model that should be applied to all industry codes.

The pure code administration function (e.g. SECAS in the remit of the SEC) should be a service that is procured by the code panel on a commercial basis whilst the central delivery bodies should be licenced. The award of these licences and the consequential price control and regulatory oversight should be managed by Ofgem.

This model would provide clarity and would help facilitate the potential drafting of a new licence where the prohibition of code delivery services that provide monopoly central services to the energy sector would be simpler to achieve.

Concerns around how strategic change could be better co-ordinated and implemented should rely on the existing Significant Code Review (SCR) powers from Ofgem and an enhancement to the existing Code Administration Code of Practice (CACoP) arrangements. These are not particularly effective at the moment but could be improved by greater enforcement and competitive provision of all code administration services with links to CACoP deliverables.

The implications of moving to a new common model for all industry codes would be potentially bold, would affect different codes to varying amounts (e.g. the BSC would be particularly affected, whilst the SEC would not) and would need to take place over a period of time to avoid unnecessary disruption.

There does not seem to be logic to assume that the National Grid administered codes (CUSC, GC and STC) should not follow a similar set of arrangements with a competitively procured code administrator providing services for them.

The recent announcement by Government and Ofgem regarding changes to the system operator function reinforce the suggestion that independence and the removal of conflicts of interest is useful in this area. Utilising an independent code administrator is therefore consistent with this outcome.



The establishment of a new licencing regime will require parliamentary time to approve new regulation. This might be challenging for the remainder of this parliament and so present a risk to this project.

A potential option may be to explore whether existing licence arrangements could be used. For example the DCC Licence could be extended to include other functions that provide central services to the energy industry. It has recently been extended to include central registration services and theoretically it could be extended to other services as well.

### **Consultation Question:**

#### **CHAPTER: Two Scope of the new arrangements**

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

Yes, the logic for choosing the relevant codes (breadth of scope and materiality of impact) is sound.

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

The Green Deal Arrangements Agreement (GDAA) is a potential candidate but there is work currently underway merge this with the MRA.

The SMICoP and DTSA are also potential candidates; both are narrow in their scope and have specific issues regarding their governance arrangements that need addressing.

They both have implications for consumers and the market and therefore logically should be included within the scope of this review.

Our preference would be for both of these Codes to be subsumed into other codes. SMICoP should be part of the SEC and the DTSA service should form part of the MRA. Moving these arrangements would address the current governance issues and ensure that they were in line with the improvements that will be introduced for all industry codes.



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

The potential impact that a code has on consumers may be another factor that should be considered when making a decision.

For example SMICoP is a very narrow piece of industry governance but its administration and change process have required considerable effort over the past few years as a result of the potential impacts to customers.

**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 do not think that this is a good idea and alternatives need further consideration.

We agree that the end to end delivery of central system changes is the reasoning behind the CMA AEC but believe that this can be addressed by licencing only the entities that actually deliver these services.

Licensing pure code administration services (as for example undertaken by Electralink for the DCUSA code) does not seem to have any potential value or merit. The scope of the activity would be difficult to define in a prohibition order needed for the new licence. It isn't also clear that it would be an efficient use of Ofgem's time to be procuring such services for the large number of industry codes.

The role of delivery body and code administrator should be kept separate with only the former licenced. Whether the delivery body is termed a code manager or something else is less material, it would be helpful if it were termed something which is obvious and clear to industry participants.

**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 believe that the code administration for the NGET codes should be procured from an independent entity in a similar way to that used by other existing codes. It isn't clear to us that there would be any value in licencing this activity.



If there was a strategic change that Ofgem wanted implementing on these codes then they could rely on the existing SCR and consultation process. Facilitation of any amendments to the relevant codes could be made by the new independent code administrator.

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

The scope of the relevant activity will help define which model is best for appointing the new licensees.

If our preferred model of only licencing code delivery bodies is adopted then Model 3 would seem to be the best route. This model was used by Government when the DCC licence was awarded and will be the same process that Ofgem uses to find a new Licence holder when the current DCC licence term comes to an end.

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

If a common model for all codes was chosen then the approach would be logical and follow a defined route.

If there is to be no defined blueprint for industry governance and existing arrangements are to be individually reviewed then it isn't clear whether one model would be preferable.

The current divergent arrangements in the codes would probably result in different models suiting specific codes. Individual assessment would need to be undertaken to understand which would be the best.

This seems inefficient and time consuming and we would prefer to concentrate on developing a preferred model that all codes could adopt.

**CHAPTER: Four Strategic Direction**

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

Yes, ensuring that the scope is well defined will be crucial to ensuring that it is a success.

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

The Strategic Direction should be developed in a collaborative manner by Ofgem with input for all relevant stakeholders.



There are a number of options as to how this could be achieved; it could be via consultation (e.g. the Ofgem Forward Workplan), via engagement seminars and workshops or via bilateral dialogue.

There may be a place for the proposed Consultative Board in helping with the establishing and reviewing the Strategic Direction. It may also be useful to consider the support that relevant industry trade associations may be able to provide.

What is important is for Ofgem to consult as widely as possible to ensure that the process for setting the strategic direction is both transparent and as inclusive as possible.

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

Clear milestones from each policy initiative will be needed to be included in the strategic direction.

To provide value to the industry it will need to highlight what activity is being undertaken and what can be expected from stakeholders (e.g. engaging with Ofgem/Government regarding policy development or building and implementing new IT systems).

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

The projects listed in table 4 of the consultation were a reasonable start for those that should be included in the Strategic Direction.

Assessment of Ofgem's forward work plan, BEIS planned activity for the remainder of the parliamentary term would also be useful.

Engagement with the current industry code panels would also be useful as each of these undertakes reviews of potential industry impacts to them in near future.

**CHAPTER: Five Consultative Board**

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

This is unclear to us at the moment.



We did not believe it would be possible for it to 'coordinate and facilitate delivery of strategic change' and to 'identify and remove obstacles' as suggested in the consultation without providing it with new regulatory powers.

This seems to risk it becoming an additional layer of industry bureaucracy, overseeing the industry codes and somehow interacting with Ofgem regarding decisions on industry change.

Who would be on this Consultative Board is also not clear as their individual responsibilities may be onerous. Another contentious area would be how the individuals would be appointed, whether they would be independent or be expected to represent constituencies.

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

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

It isn't clear whether there would be an immediate impact upon any of the existing industry projects from implementing these new arrangements.

There would potentially be risks to the delivery of some of these projects should amendments to the governance arrangements undermine the smooth implementation of industry changes.

There would be implications for the current governance arrangements and the commercial contracts that are in place with existing industry code service providers. These would need to be managed in the transition from the old arrangements. None of these are insurmountable but a clear plan of how and when the transitions are needed to occur would be needed.

### **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?**

No, the proposals set out here might improve the governance arrangements around industry codes and if implemented correctly may bring better accountability and increase the likelihood of future industry projects being delivered successfully.

They would not however remove the situations where the use of an SCR would be necessary. These are scenarios where Ofgem wish to implement a strategic objective and want to dictate control over how the process will operate.



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

This is a sensible and pragmatic approach.