

Code Reform - Electricity Systems Team
Department for Business, Energy and Industrial Strategy
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To whom it may concern,

Reforming the Energy Industry Codes: Consultation Response

Scottish Renewables is the voice of Scotland's renewable energy industry, working to grow the sector and sustain its position at the forefront of the global clean energy transition. We represent around 260 organisations across the full range of renewable energy technologies in Scotland and around the world, ranging from energy suppliers, operators and manufacturers to small developers, installers and community groups, as well as companies throughout the supply chain.

Our energy system is experiencing a period of transformational change as we move away from centralised fossil-fuelled plants and embrace distributed low-carbon technologies. In order to meet the net-zero target it is critical that we have a governance framework in place that supports our transition to a smart and flexible energy system. The future regulatory landscape should be easy to navigate, forward-looking and responsive to change while also accommodating the diverse nature of the market players as the system continues to innovate to achieve the ambition of delivering net-zero by 2050.

We support BEIS and Ofgem in working towards creating a more agile governance framework. We are particularly interested in simplifying current arrangements to provide a clearer regulatory framework that will encourage more innovation to come forward. We agree with the future vision outlined within this consultation and welcome the references made towards the net-zero targets. We would emphasise, however, that it is critical that decarbonisation remains a central focus throughout any reforms to the energy industry codes. As such, we believe decarbonisation should be included within the key objectives of either the Strategic body or the Integrated rule-making body.

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In responding to the consultation, we would like to draw your attention to the following points:

- We agree with the view that existing regulatory arrangements are presenting a barrier to achieve the desired outcomes of the reform and there is need for Government vision to inform future energy code development.
- Ofgem and BEIS need to consider the role of industry, any changes to the current route to appeal in their future work under the reform and consult the industry prior to making final decision.
- Future analysis needs to consider the level that code managers should be accountable to code signatories in order to mitigate the risk of the conflict of interest present in the two models outlined.
- Ofgem and BEIS should set out clearer timelines, as well as outlining a vision on transitional arrangements.

Scottish Renewables would be keen to engage further with this agenda and would be happy to discuss our response in more detail.

Yours sincerely,



Cara Dalziel

Policy Manager

Scottish Renewables

Consultation Questions

1. Do you agree with our four desired outcomes for the code governance landscape by the mid-2020s? Yes/No/Don't know. Please explain. If you disagree, please explain what you consider the outcomes should be.

We agree with the desired outcomes of the reform and find them commendable.

We believe that the current arrangements create barriers to achieve these goals. The future regulatory landscape should be easy to navigate, forward-looking and responsive to change while at the same time able to accommodate the diverse nature of all market players as the system continues to innovate to achieve the ambition of delivering net-zero by 2050. Furthermore, future energy regulation will have a critical role in the decarbonisation of heat and transport – either through electrification or the development of green gas solutions.

Nevertheless, code changes should be able to be developed in a proper fashion with industry involvement and with some scrutiny to ensure workable solutions. The desired end-state should not compromise the purpose of the codes – serving as a contractual arrangement between parties. In commercial disputes such as those between generators and the counterparties, changes to the current framework can increase the likelihood that the terms of the contract will need to be updated and renegotiated later. The future regulatory framework needs to ensure the right incentives are put in place for code signatories to continue to innovate and support the development of codes.

2. Do you agree with the problems we have identified (in chapter 1 – Background – and in later chapters), and that they present a persuasive case for reform of the current framework for energy codes? Yes/No/Don't know. Please explain.

We agree. The problems identified present an accurate case for reform.

We disagree with the assertion in the consultation that the Significant Code Reviews (SCR) are *'ad hoc approaches to the problems that exist rather than a long-term solution. They are not a way to deliver wide-ranging, strategic reforms.'*

SCRs have worked well so far, driving issues which sit across multiples codes and encouraging wider industry involvement. We note that Ofgem's own guidance document on the drivers of a SCR¹ notes that it *"would consider whether to launch an SCR in response to various events including, for example... Government-led policy"*. Thus, the purpose of SCRs is not to solely

¹ Ofgem, 'SCR Guidance', June 2016 https://www.ofgem.gov.uk/system/files/docs/2016/06/scr_guidance.pdf

focus on remedying short-term issues, but also being able to drive forward overarching government objectives in a strategic manner on issues which cut across multiple codes.

We recognise that SCRs have so far been focused on single-fuel issues (e.g. solely electricity or gas). The reforms therefore need to realign current objectives with a whole system approach to delivery of net-zero ambitions to minimise the risk of unintended consequences. This will ensure changes are enforced with thorough consideration on their impact to achieve legally binding climate change targets.

Uncertainties arising from short-term changes to regulation, without a clear long-term strategy, have damaged investor confidence in the sector recently. To give an example, changes to embedded benefits were enacted where they were removed, without clarity about what would replace them. This undermined the ability for industry to plan. We believe that Ofgem's two electricity charging related SCRs in process would benefit from more clarity over the long-term strategic direction of the policy. A process must be developed for identifying and remediating situations where independent decisions by the regulator undermine or seem to contradict government policy. Currently this process is somewhat contingent on the role of the CMA (e.g. judicial review), but there is also a risk it could result in perverse outcomes.

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

Ambiguity and lack of clarity in the legal framework itself is preventing innovation. The desired outcomes need to assure that compliance with regulation is easy to achieve. This is not currently the case with the complexity and inaccessibility of energy codes proving a major barrier to new and innovative market entrants.

As new business models are being rolled out by the industry, the codes will need to evolve to incorporate these. However, this is likely to add to the complexity and length of the codes rather than reduce them. The future framework will have to be flexible enough to accommodate any new rules governing the role and use of structures which are not yet codified e.g. use of hydrogen and development of green gas solutions.

4. Do you agree with our proposed scope reform? Yes/No/Don't know. Please explain. If not, which additional codes or systems do you think should be included/excluded?

The proposed scope of the reform seems sensible.

5. Are there any codes or systems that we should only apply a limited set of reforms to? Yes/No/Don't know. Please explain.

We agree with the identified issues and support the need of reform. However, we would like to note the degree of governance complexity. Radical change and consolidation such as a merger of CUSC and BSC would likely be a very resource-intensive and complicated process.

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

We broadly agree.

We support strategic development of changes to the codes and independent decision-making aimed at achieving wider government outcomes. We believe that SCRs should continue to embody this function and serve as a viable tool to deliver long-term strategic solution to cross-code issues.

We support the creation of more active code administrators (code mangers) with incentives which are closely aligned with consumers' interest. Nevertheless, developing workable changes is contingent on the role of the industry and the preferred framework needs to ensure confidence in the role of empowered code mangers.

There is a missing function in the two options of reform, as there should be an appeal route for decisions of the independent body, whatever its nature, on code changes. Future energy investments are likely to be made on the basis of a known framework, thus making any changes to it very material indeed. There needs to be confidence in the process to ensure, in turn, investor confidence.

We note that progress is already being made, notably with the introduction of the critical friend concept in the CUSC which facilitates the development of new change proposals. However, there is no mechanism to ultimately prevent a change proposal being raised – a risk which becomes more prevalent if either of the two proposed models is adopted.

Code simplification and consolidation has merit once achieved, but it is also likely it will be prolonged, complex and highly resource intensive process. Careful consideration should be applied on who will undertake further assessment of options, and how new changes are handled whilst any consolidation and simplification are being undertaken.

7. Do you agree with the two broad models outlined? Please provide reasons for your position and evidence where possible. – further detail can be found on each model in the chapters that follow.

We believe that the two models as defined by the consultation do not cover a sufficiently wide range of high level potential functional structures. As presented in the consultation, it seems that the models do not take into consideration the interface between the industry, the code manager and strategic body functions. Not considering this interface will lead to several issues for future assessment work:

- Create conflict of interest potentially favouring a model where a single body is able to propose, approve and enforce modifications with no mechanism or accountability to its code signatories
- Misrepresentation of the different roles of the industry, without clear view on the changes to the current route to appeal
- Ignoring the important differences in function as well as interaction between the economic regulator, the strategic body and industry involvement
- Underestimating the potential complexity compared to the current arrangements

Nonetheless, we do believe it is necessary to consider a model for future governance arrangements where the role of the industry is better recognised, e.g. a hybrid model to the current arrangements where code managers are accountable to code signatories to a certain level. We believe that it is in the interests of both industry and consumers for Ofgem and BEIS to deliberate further on the preferred framework and consult the industry prior to making final decision.

8. Which model do you believe will best deliver on our desired outcomes? Please explain. NB: – further detail can be found on each model in the chapters that follow.

There is not enough detail in the outlined models and the accompanying assessment to be able to provide comment.

We are supportive of the approach to introduce a clear link between government ambition and future development of the codes. However, we strongly recommend that BEIS and Ofgem consult on the detail of the assessment approach as the current level of information provided does not allow enough scrutiny from industry. The desired outcomes outlined in the review are commendable, however, these must be further developed and discussed with industry before final decision under the reform. As previously noted, there is a missing function in the two options of reform, as there should be an appeal route for decisions of the independent body, whatever its nature, on code changes.

The assessment process, including the actual methodology for assessing each of the identified criteria, must be developed in detail and consulted on with industry. It is not clear how any of the criteria will be assessed, whether the assessment will be quantitative and qualitative and what evidence will be used to support the analysis. Future work should also set out the assessment methodology for evaluating progress on the proposed criteria, along with clearer timelines and milestones and a vision on transitional arrangements.

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

We note that if changes to the role of code signatories are made, code managers will no longer be accountable to code signatories. Possible conflict of interest potential would need to be considered regarding the possibility of an existing licensee being assigned the role of a powerful new code delivery body, making final decisions on changes.

The change in process will lead to code panels becoming redundant. If panels were abolished with no clarity on the route to appeal decision, the framework risks significantly undermining industry confidence at a time when very material new investments need to be made by the industry.

10. Do you agree there is a missing strategic function for codes development in the energy sector and introducing a strategic function with the responsibilities outlined in chapter 3 is the best way to address the lack of strategic direction? Yes/No/Don't know. Please explain. Who is best placed to fulfil the strategic function and why?

We agree strategic direction is needed in codes development. This should be wide-ranging, incorporating issues which might require new policies such as those tackling heat and transport decarbonisation as well as issues which do not traditionally fall under the remit of a single independent regulator such as cyber security.

It is not clear from the consultation document how the Strategic Policy Statement (SPS) and the strategic body might interface.

Further, we note that the purpose of SPS could be superseded by the addition of a new strategic layer between Government vision and code development.

It is important that commercial incentives and considerations are as distinctly separated from code management as possible. We would be more supportive if an independent body fulfils this role to mitigate any conflict of interest.

11. Do you agree with the objectives and responsibilities envisaged for the strategic function, and are there any additional objectives or responsibilities the strategic function should have?

We broadly agree.

However, there is nothing in the objectives and responsibilities to explicitly support decarbonisation of the electricity system and the delivery of net zero. In light of the legislation, the strategic body framework should set out how this goal will be explicitly supported and prioritised.

We support an explicit objective on decarbonisation and net zero as part of Ofgem's statutory duties, should Ofgem take on the new strategic body function. Such change will support long term objectives and would be more effective and impactful than through the Strategic Policy Statement.

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

Were an entirely new strategic body to be created, there would no doubt be different accountabilities and duties. It might bring additional cost, and risk introducing further fragmentation to the landscape creating siloes. Should Ofgem not take on the function of the strategic body, clarity needs to be provided to industry on the interaction between the new body and the economic regulator. Additionally, if a strategy board is set up to aid engagement, consideration should be given on the roles and responsibilities of parties which currently advise the direction of Government energy policy such as the Committee on Climate Change and the National Infrastructure Commission.

The new function will require a clear Government vision from BEIS and Ofgem on policy objectives and strategic code changes needed. This is likely to be a very challenging task and a strategy board could facilitate this process, but it would need to comprise a diverse set of skills and expertise.

Setting out a plan on licence and code modifications to be progressed within acceptable timelines for delivery would be helpful. Flexibility should be built into the framework to allow for such scenarios to be appropriately assessed and change proposals to be fairly treated in the prioritisation process.

13. What are your views on how the strategic direction should be developed and implemented (including the option of establishing a strategy board to aid engagement)?

Please refer to our answer to Q12.

14. Do you think that the scope of the strategic function should be limited to taking account of the Government's vision for the energy sector and translating it into a plan for the industry codes framework, or are there other areas it should address? (for example, impact on vulnerable consumers)? Yes/No/Don't know. Please explain.

The strategic function should have regard to the impact of policies on the consumer, both present and future.

Where plans for the industry codes framework are developed, the strategic body needs to ensure appropriate stakeholder engagement has been carried out so that the views of the industry are consulted on before publication of final plan. Industry should, in our view, retain the power and flexibility to propose code changes before a plan for the year ahead is set.

15. Do you agree that in addition to the current responsibilities that code administrators have, that a. the code manager function should also have the following responsibilities:

a. identifying, proposing and developing changes (analysis, legal drafting etc.), including understanding the impacts;

The current industry-led code modification process has given rise to a fragmentary and uncoordinated approach to reform. This can result in a lack of incentives on industry to make changes that are in the interests of consumers. This system also presents a high degree of risk of regulatory capture.

A central body could coordinate the reform agenda much more efficiently and effectively than the status quo, however in our view it makes sense for the modification coordination function to rest with the strategic body as distinct from the implementation body.

Industry should, in our view, retain the power and flexibility to propose code changes and to raise concerns with the code manager. However, it would make sense for the proposed strategic body to adjudicate on a case-by-case basis whether these modification proposals were in line with overarching policy objectives. If the strategic body recommended that a proposal should move forward, it would delegate it to the code manager to coordinate the analysis, legal drafting, impact modelling, and oversee the development process.

By delegating the responsibility for code development to a central authority, this process would be more inclusive of a diverse range of energy system stakeholders.

The functions of overseeing the change process; monitoring compliance with code obligations and deciding on appropriate measures in the event of non-compliance are distinct from the specific responsibilities for ensuring strategic alignment with Government policy. We would be more supportive of Ofgem retaining its enforcement powers as under the current arrangements.

b. making decisions on some changes, or making recommendations to the strategic body; and

c. prioritising which changes are progressed.

Yes/No/Don't know. Please explain.

The code manager should have oversight of this function and be able to determine correct sequencing of modification processes on a pure technical basis, however in terms of the overarching prioritisation of reform, this should rest with the strategic body and ultimately with Government.

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

Some existing code administrators such as Elexon and the ESO make their own system changes, to systems that they own or manage. This may have merit, as they can signal the change lead time needed and the costs involved well. However, were the ESO take on the role of the strategic body commercial incentives and considerations should be distinctly separated from code management as possible.

17. Should the approach differ on a case-by case basis (i.e. depending on the code or system in question)? Yes/No/Don't know. Please explain.

This would depend on how and to what extent consolidation of the existing codes were to move forward.

18. Do you agree that the code manager function should be accountable to the strategic body and that this should be via a licence or contract? Yes/No/Don't know. Please explain.

Please note questions 19- 26 only apply in respect of Model 1 (code manager function and a strategic body).

AND

19. Are there more effective ways that a code manager function's accountability to the strategic body could be enshrined other than in a licence or contract? Please explain.

It is critical that the code manager function should be accountable to the strategic body. The status quo self-governance model is predicated on the basis that licences are legally enforceable contracts, whereas legislative mandates are more likely to be changed by successive governments. It may therefore be appropriate for the strategic body to have more direct oversight via a legislative mandate to ensure an appropriate level of flexibility and accountability to overarching policy objectives.

20. Do you agree that we should not consider further a model whereby code managers are accountable to industry? Yes/No/Don't know. Please explain.

It is appropriate and necessary to separate code management/oversight and commercial functions as much as possible.

However, should the code manager function be paid through licence fees by code parties, it is reasonable to consider to what extent code managers should be accountable to those parties. An additional scenario should be included as part of future analysis.

21. Do you have views on whether the code manager function should be appointed following a competitive tender process or other competition? Yes/No/Don't know. Please explain.

We would be more supportive of competitive tender process.

22. Do you think the code manager function should be established by the strategic body creating a body or bodies? Yes/No/Don't know. Please explain. If the code managers were established in this way, would we need to consider any alternative approaches to funding or accountability? Yes/No/Don't know. Please explain.

Yes, it should be established anew.

It is essential in our view that this asymmetry of resourcing and expertise is proactively corrected. How to achieve this requires further thought. Simplification and code consolidation will provide a generally more navigable codes landscape for newer entrants.

Further, licensing for code manager roles may not be an effective way to achieve accountability in the first instance. Presumably where a code manager does not abide by the strategic

direction, they will incur a fine. Would the fine accrue to the code panel, who currently support code administrators, or to the company? Were it the latter, there would be a mismatch between those ultimately incurring the fine and the motivations of the offence, which may be committed in line with a company's individual commercial interest.

23. In terms of establishing/choosing the code manager function, do you agree that we should not consider further:

- a. requiring an existing licensee to become the code manager; and/or**
- b. requiring a licensee (or group of licensees) to create the code manager?**

Yes/No/Don't know. Please explain.

We do not have a preference.

24. What would be the most effective way to ensure the code manager function offers value for money (for example, through price controls or budget scrutiny)? More broadly, what is the right incentive framework to place on the code manager function? Please explain.

Please refer to our answer to Q20.

The code manager should be accountable to the strategic body and ultimately to Government itself.

25. Are there any factors that:

- a. would stop parties (including code administrators) from becoming a code manager**
- b. should prevent parties from becoming a code manager (e.g. do you agree that licensees should not be able to exercise control of the code managers).**

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

Licence fees paid by code parties would seem to be an appropriate funding mechanism for the code manager.

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

Digitalisation of codes and learning from best practice across code administrators seem to be the least regrets option to achieve the desired outcomes of the reform and make the codes more accessible. Adopting a common approach to governance of changes would aid code accessibility.

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

We do not have a preference.

The creation of a new strategic body should provide the necessary whole system oversight. We do not think the creation of a Unified Single Code for both gas and electricity would provide the most sustainable solution. Currently, there are separate operators for both gas and electricity networks, with separate settlement arrangements and limited interaction in operational timelines. Whole system issues could better be addressed by a new objective in each code manager to consider the impact across the industry or the efficient interaction of the markets.

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

Having more than one code manager would retain the ability to benchmark code manager performance. Full merger into a single code manager is thus unlikely to encourage competition and be the most optimal outcome.

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

Please refer to our answer to Q28.

31. Do you agree that the codes should be digitalised? Yes/No/Don't know. Please explain.

Please refer to our answer to Q27.

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

Industry can help identify a proportionate, transparent and fair approach to compliance where compliance is relative and in areas such as metering and supplier reconciliation issues. Non-compliance can be reported to Ofgem by code managers and system operators. As

compliance with codes is made mandatory via licence conditions, and as non-compliance is legally penalised, we recommend that compliance enforcement and the levying of fines remain with Ofgem – and not devolved to a code manager.

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

Please refer to our answer to Q32.

34. With Model 2 - integrated rule-making body - should the IRMB have responsibility for imposing measures (where a party is non-compliant with the code) or should this be for another organisation? Please explain. Please note this question only applies in respect of Model 2 (integrated rulemaking body).

There is no strong evidence presented within the consultation to suggest that changes to the current approach to compliance monitoring and enforcement are needed to address any failings. However, where possible common approach to monitoring party compliances should be applied across the codes.

We would be more supportive of Ofgem retaining its enforcement powers as under the current arrangements.