

By e-mail to: energymarket@cma.gsi.gov.uk

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Dear Will

ELEXON's comments on the CMA's Energy Market Investigation: provisional decision on remedies

We welcome the opportunity to comment on the CMA's energy market investigation provisional decision on remedies. As you are aware, ELEXON is the code administrator for the Balancing and Settlement Code (BSC). We are responsible for managing the electricity balancing and settlement arrangements as set out in the BSC. We are also the body responsible for the delivery of settlement systems and processes. We manage the development and implementation of changes to BSC Agent (central) systems and processes.

We are a wholly owned, arms-length subsidiary of National Grid. Our funding arrangements (which see our costs passed directly on to BSC Parties) enable us to operate independently from our shareholder (National Grid), who bears no liability or obligation to provide finance or financial support to ELEXON Ltd.

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.

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 are pleased that we have been able to support the work of the CMA to date, through our submissions, data provision and attendance at a hearing, and we are keen to assist further if required.

We believe that the overall outcome of the CMA should be to reduce complexity and costs to existing parties and new entrants, to facilitate competition and not to have the opposite effect. The recommendations and actions arising do need to be carefully tested against this requirement. With this in mind, we set out below a number of observations on those aspects of the CMA's provisional decision on remedies that are particularly relevant to the BSC and ELEXON. These areas are considered in further detail in the attached Appendix.

Transmission Losses

We are pleased that the CMA recognises the extensive analysis conducted previously under a series of BSC Modifications including, most recently, Modification Proposal P229 'Introduction of a seasonal Zonal Transmission Losses scheme'.¹

However, the proposed remedy contains some key differences from P229 and from any other BSC zonal losses scheme previously assessed by the industry. We believe further information is needed on these points of detail and we would be happy to discuss these elements of the solution to help ensure a successful implementation.

We also note that the remedy proposes to specify the full loss factor calculation in National Grid's Transmission licence, rather than just the principles behind the calculation. This means that Ofgem may need to make incremental changes to the licence if the calculation needs to evolve in the future, and these amendments would need to be co-ordinated with any consequential changes to industry codes such as the BSC. This two-part approach to defining and amending requirements appears to run counter to 'regulation through principles-based licences' and would seem to be less efficient than setting out and amending rules in industry codes only.

We expand on these points and provide additional commentary on the technical and implementation aspects of the remedy in the attached Appendix.

Settlement Reform

We strongly support the move towards half hourly settlement which builds on work ELEXON has led on for the past 6 years. We are pleased that the CMA has acknowledged the work ELEXON has pioneered with the industry via the Profiling and Settlement Review Group (PSRG)², the Settlement Reform Advisory Group (SRAG)³ and the expert support we are currently providing to Ofgem in its work on half hourly settlement. Our work has led to a number of proposed ways forward to implement half hourly settlement.

We support the production of a forward plan for implementing half hourly settlement that will provide clarity on the timing of any move to elective and/or mandatory arrangements.

We note the CMA's recommendation that Ofgem undertakes a cost-benefit analysis on the introduction of mandatory half hourly settlement as soon as possible. We believe we can build on our previous work in this area and help Ofgem develop its detailed thinking.

We also note that Ofgem, having considered the advice of the proposed consultative board, would have the power to appoint third parties to project manage programmes of change that deliver its strategic direction. Given our work on HH settlement reform we believe we are well placed to support and potentially run such a project and, subject to being awarded appropriate powers, see no reason why Ofgem couldn't appoint ELEXON in such a cross-cutting capacity.

¹ <https://www.elexon.co.uk/mod-proposal/p229-introduction-of-a-seasonal-zonal-transmission-losses-scheme/>

² <https://www.elexon.co.uk/group/profiling-and-settlement-review-group-psrg/>

³ <https://www.elexon.co.uk/group/settlement-advisory-reform-group-srag/>

Industry Code Governance

We welcome the CMA's wide considerations regarding industry governance. While we have some concerns over the checks and balances that should be part of the proposed governance (we comment on these in more detail elsewhere in this response), we can see merit in a re-set of responsibilities.

- We support the proposal for the development of an industry change programme (according to an Ofgem-determined strategic plan for industry codes) and the establishment of an expert group (the proposed consultative board) to consider cross-industry changes.
- We agree it is essential for code administrators and delivery bodies to be active members of the proposed consultative board.
- We agree that the independence and impartiality of code administrators is important.
- We support the proposal that code bodies should be given powers to raise changes to their respective industry codes.
- We are also encouraged by 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 administrators and industry code panels.

However, our position on the need for licensing code administration and delivery remains cautious, since it could create a fundamental shift in the accountability of such code bodies, has the potential to increase cost and complexity, and could inhibit innovation.

We note the CMA's view that 'Code administrators (and delivery bodies), as licensed bodies with better defined powers and responsibilities, and appropriate funding, would be able to step into the process where appropriate to support Ofgem and code panels in their respective functions.'

It will be important to ensure that code administrators can act autonomously for the benefit of industry code parties and consumers. Furthermore, that there is transparency in the interactions between code administrators and their various stakeholders.

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. We need greater clarity on the funding models that the CMA would consider appropriate in this respect, in particular, how such funding might support impartiality and the better delivery of Ofgem and code panel functions.

Overall, we are yet to be convinced that the above measures require a licensing regime to implement and we are concerned that the implementation of such a regime may introduce additional cost and complexity into the regulatory landscape. As we noted in our response to the CMA's provisional findings report and notice of possible remedies⁴, the BSC contains various provisions that afford Ofgem and the Gas and Electricity Markets Authority oversight of the BSC and its change processes. We believe these could be replicated across other industry codes and that the recommendations noted above could be delivered through amendments to existing industry codes without the need to develop a licensing regime.

⁴ <https://www.elexon.co.uk/wp-content/uploads/2015/08/31-Jul-2015-CMA-response-findings-and-remedies.pdf>

Additionally, if the main purpose of licencing is to create an accountability for delivering on government policy then, given the potentially infrequent nature of such requirements, it may be possible to achieve this in a much 'lighter touch' manner.

Simplification and Consolidation

We continue to support simplification in industry codes and we comment further on how this might be achieved in the appendix.

In particular, we believe there is merit in exploring the application of a principles-based approach to industry codes where possible. Such re-worked codes should be smaller, simpler and provide for easier innovation. This would facilitate any re-scoping exercise that might seek to consolidate codes.

Further, consolidation of code administration services would allow for industry parties to have a reduced number of interfaces for managing code activities and changes. Consolidation of service provision would offer further consistency in how similar (but currently separate) processes are delivered. We strongly believe it is essential to avoid further proliferation of code administrators and to act to reduce it. Any opportunities for consolidation should enable all existing code administrators to compete on equal terms and the existing restrictions on our own participation in any competitive process must be removed otherwise the benefits of such competition are lost.

Electricity Market Reform

Finally, as we observed in our response to the CMA's provisional findings report and notice of possible remedies⁵, we note the CMA's comments on the benefits of the competitive process in relation to Electricity Market Reform. Our subsidiary, EMR Settlement Ltd, will continue to support DECC, LCCC and ESC in delivery of these new provisions under the terms of our service agreement.

We would be happy to discuss our response and will continue to support the CMA in its work. If you would like to discuss any areas of our response please contact Adam Richardson, Design Authority, on 020 7380 4117, or by e-mail at adam.richardson@elexon.co.uk.

Yours sincerely,

Michael Gibbons CBE

Chairman, ELEXON

List of enclosures

Appendix A - Comments on the provisional decision on remedies

⁵ <https://www.elexon.co.uk/wp-content/uploads/2015/08/31-Jul-2015-CMA-response-findings-and-remedies.pdf>

ELEXON's comments on the CMA's Energy Market Investigation: provisional decision on remedies

Appendix A

Locational adjustments for transmission losses

ELEXON operates GB's electricity imbalance settlement processes under the Balancing and Settlement Code (BSC). These include:

- Collecting generators' and Suppliers' Metered Volumes;
- Scaling these Metered Volumes in order to allocate transmission losses;
- Comparing these scaled Metered Volumes with the contracts struck by generators and Suppliers, ahead of time, to sell and buy electricity;
- Calculating the price to apply to any imbalances (differences) between these scaled Metered Volumes and energy contracts; and
- Billing generators and Suppliers for these imbalance charges.

The CMA's proposed remedy for transmission losses will therefore require changes to the BSC's existing imbalance settlement rules, regardless of whether the primary delivery mechanism for the remedy is the BSC itself. We will support the development and assessment of these changes in the usual, impartial way.

To estimate the extent of the BSC changes, and their implementation costs and lead times, we require further clarification from the CMA on how it intends its proposed licence requirements on National Grid will be implemented practically. We expand upon these points further below.

Key differences between the CMA's proposed remedy and P229

Modification Proposal P229 'Introduction of a seasonal Zonal Transmission Losses scheme'⁶ sought to allocate transmission loss costs more cost reflectively across generators and demand customers on the GB transmission system.

Under the current BSC arrangements, losses are allocated to BSC Parties in proportion to their metered energy volumes, with a uniform allocation of 45% of losses to production accounts and 55% to consumption accounts. The current BSC losses arrangements do not consider the geographic location of generators and customers. Modification P229 proposed to change the Transmission Losses arrangements in the BSC to require that a Transmission Loss Factor (TLF) for each BSC Season be calculated for each 'TLF Zone'. TLFs would be calculated annually for the following year using historical data.

The CMA's proposed remedy contains the following key differences from P229 and from any other BSC zonal losses scheme assessed by the industry previously:

- It obliges National Grid to create the load flow model and calculate the loss factors, rather than assigning these activities to a third-party agent;

⁶ <https://www.elexon.co.uk/mod-proposal/p229-introduction-of-a-seasonal-zonal-transmission-losses-scheme/>

- It obliges National Grid to appoint third-party agents to collect metered volume data, rather than using the existing BSC Metered Volume data held by ELEXON and used in the BSC's imbalance settlement calculations; and
- It applies only to generators, rather than to both generators and Suppliers.

Collection of Metered Volume data

We believe that requiring National Grid to obtain metered data, when such data already exists through the BSC Settlement process, would be inefficient and would result in unnecessary additional implementation costs and lead times for the industry.

Change to existing 45:55 split in loss allocation

We note the CMA's intention to apply its proposed remedy solely to generators, amending the BSC's existing 45:55 split in the allocation of transmission losses. We welcome further clarity from the CMA as to whether its intention is to apply all transmission losses on a locational basis, or only those losses which vary with the distance that the energy travels (what P229 referred to as 'variable losses', also sometimes called heating losses). P229 sought only to apply these 'variable' losses by location, continuing to allocate the remaining 'fixed' losses to all parties on a uniform basis.

The loss allocation proposed previously by P229 can be summarised as:

'Delivery' receives: 45% of the total (fixed and variable) transmission losses overall, comprising a locational allocation of variable losses and a uniform allocation of fixed losses

'Offtake' receives: 55% of the total (fixed and variable) transmission losses overall, comprising a locational allocation of variable losses and a uniform allocation of fixed losses

We need further clarity from the CMA as to how it intends to define 'generator' and 'Supplier' for the purposes of the remedy. In general terms, the existing BSC rules allocate transmission losses by scaling generators' output down and Suppliers' consumption up. This means that generators have to produce more (and Suppliers buy more) electricity to meet their contracts or they will pay imbalance charges on the difference.

However, in practice, the BSC scales Metered Volumes at the BM Unit level and a single generator or Supplier may have multiple BM Units.⁷ For each BM Unit, the BSC uses the net Metered Volume of its Trading Unit⁸ (the Trading Unit's 'delivery/offtake' status) to determine what allocation of transmission losses it should receive:

- Where the Trading Unit is a net Exporter, all BM Units in that Trading Unit receive the 'delivering' allocation of transmission losses and have their Metered Volumes scaled down
- Where the Trading Unit is a net Importer, all BM Units in that Trading Unit receive the 'offtaking' allocation of transmission losses and have their Metered Volumes scaled up

The BSC determines this delivery/offtake status for each half-hourly imbalance Settlement Period and so it can change over time. A single generator or Supplier can have multiple BM Units in multiple Trading Units, and so that generator or Supplier can have a mix of 'delivering' and 'offtaking' BM Units at any point.

⁷ A BM Unit is a grouping of a generator's Plant/Apparatus or a Supplier's customers.

⁸ A Trading Unit is a grouping of BM Units, which may belong to the same company or to different companies.

The existing BSC rules can result in generators receiving the 'offtaking' allocation of transmission losses, and in Suppliers receiving the 'delivering' allocation. An example Trading Unit could be a Power Station with a Generating Unit and a demand unit. When generating, its net Metered Volume will be 'delivery'. But if the Power Station goes on outage while still consuming station load, its net Metered Volume will be 'offtake'.

Another example is what the BSC calls a Base Trading Unit. This, for a particular geographic region of GB, comprises all Suppliers customers' consumption and microgeneration. It also, by default, comprises licence-exempt 'embedded' (distribution-connected) generation in that region. Normally, a Base Trading Unit's net Metered Volume will be offtaking. This means that the licence-exempt generators get an 'embedded benefit' by receiving the offtaking allocation of losses, effectively treating them as negative demand. However, if the level of embedded generation exceeds consumption, then at certain times (e.g. in summer) the Trading Unit can become net delivery. This happens in the North of Scotland and means that all BM Units in the Base Trading Unit for that region, including those belonging to Suppliers, receive the delivering allocation of losses.

We suggest that the principles behind a 100:0 'generator/Supplier' loss allocation therefore require detailed consideration. We note that previous BSC Modifications sought to retain the existing 45:55 split and so the industry has not assessed such a change previously. As explained above, retaining the existing delivery/offtake definition, but only allocating transmission losses to delivery, would not necessarily result in a 'generator only' allocation. We note that NERA modelled a scenario for the CMA's cost-benefit analysis in which it allocated 100% of losses to generators; however its report does not clarify how it distinguished 'generation' for this purpose.

Practicalities of, and governance for, National Grid's licence obligations

We note the CMA's intention to enact its transmission losses remedy by imposing an order and licence conditions on National Grid as the System Operator.

These licence conditions will introduce new, high-level, obligations on National Grid to undertake certain key activities supporting the calculation of zonal loss factors. However, the proposed remedy does not explain how these will be implemented and governed in practice.

Clarity of solution and impacts, and feasibility of implementation timescales

The proposed remedy states that the order and licence conditions will set out the formula to calculate the transmission loss factors. However, it is unclear what this formula will be, how it may differ from P229, and therefore what other consequential changes will be needed to the existing industry codes such as the BSC.⁹

Indeed it is not entirely clear whether the CMA intends the BSC to still be the allocation mechanism for these loss factors. This is because the proposed remedy puts obligations on National Grid, outside the BSC and under its licence, to deliver key transmission losses activities that P229 would have implemented through BSC systems, processes and agents. If transmission losses are to sit entirely outside the BSC in the future, we highlight that a BSC Modification will still be needed to (as a minimum) remove the BSC's existing allocation. If the allocation of transmission losses continues to

⁹ E.g. footnote 72 in the CMA's report states that the proposed remedy would involve the calculation of 'annual loss factors'. We are unclear whether this means loss factors calculated annually, but which could apply to more granular time periods within a year, or one single loss factor per zone per year. P229 sought to introduce an annual calculation of seasonal zonal loss factors, to reflect that the North of Scotland can switch between delivery and offtake depending on the time of year.

fall under BSC governance, then a more substantive BSC Modification will be needed to deliver the detailed processes underpinning National Grid's new licence obligations. Enacting the remedy through an order and licence conditions does not remove the need for BSC Modifications, but simply alters what consequential BSC Modifications are needed.

Before any BSC Modifications can be progressed, the technical solution and applicable governance arrangements therefore need to be clearly defined. It is unclear what process and timescales will be followed, and by who, to do so. The CMA's report notes that previous BSC Modifications had implementation timelines of around 12 months. However, this 12-month window started from the point that the technical solution and governance arrangements had been both fully defined and approved. We believe that the time needed to define this outstanding detail, in addition to that involved in finalising the CMA's report in June 2016, and then enacting the order and amending the licences, is likely to jeopardise the CMA's proposed implementation date of 1 October 2017.

Practical implications of placing the solution within licence conditions

We note that the remedy proposes to specify the full loss factor calculation in National Grid's licence, rather than just the principles behind the calculation. We note that this means that Ofgem may need to make small incremental changes to the licence if the calculation needs to evolve in the future, and that these would need to be co-ordinated with any consequential changes to industry codes such as the BSC. This two-part approach to defining and amending requirements appears to run counter to regulation through principles-based licences and would seem to be less efficient than setting out and amending rules in industry codes only.

Further, key transmission losses activities would sit in National Grid's licence and potentially outside the industry codes. Depending on how these are implemented, this could mean that the industry has less oversight and assurance of the systems, processes and data involved. For example, under P229 an independent BSC Agent would have undertaken the calculation of zonal transmission loss factors, and the performance of this agent would be subject to scrutiny and audit under the BSC. The load flow model itself would also have been subject to a technical audit by a separate independent expert. The BSC Panel, as the body responsible for ensuring that Settlement is conducted in accordance with the BSC (including the performance of BSC Agents, processes and systems), would have overseen these activities to give assurance on behalf of the industry. Similarly, the P229 calculation would have used the BSC's existing Metered Volume data, which is subject to a considerable assurance regime to ensure its accuracy.

We wonder if the wording of the remedy reflects some confusion over the different roles of National Grid and ELEXON. For example, the CMA's report talks in places about National Grid calculating imbalance prices, or imbalance charges, that include transmission losses. Although National Grid provides data to ELEXON on the energy balancing actions it takes as System Operator, and this data then feeds into the BSC's imbalance price calculation, National Grid itself does not calculate imbalance prices or charges. Instead ELEXON undertakes these calculations, including the allocation of transmission losses, in our role as GB's imbalance settlement operator. In addition, while transmission losses form part of imbalance charges, they are not part of the prices applied to imbalances. Instead (and as described above) they are applied as scaling factors to generators' and Suppliers' Metered Volumes. The BSC then applies the imbalance price to the difference between this scaled volume and the party's energy contracts. We would therefore welcome clarity from the CMA as to whether it intends National Grid to calculate and allocate loss factors itself outside of the BSC, or to calculate them but pass them as a data feed to be allocated under the BSC, or to delegate the full calculation and allocation to BSC Agents.

A BSC Modification would be required to implement any of these options fully.

The proposed remedy refers to National Grid directing ELEXON, we would highlight that the only existing mechanism by which National Grid can do so is by raising a BSC Modification.

Half Hourly Settlement Reform

We support the move towards half hourly settlement. We welcome the CMA's acknowledgement of the work that ELEXON has pioneered with industry via the Settlement Reform Advisory Group (SRAG) and the expert support we are providing to Ofgem in its work on half hourly settlement. We support the production of a forward plan for implementing half hourly settlement that will provide clarity on the timing of any move to elective and/or mandatory arrangements.

We note the stated principle that smart meters should remove the need for profiling in electricity. However, we believe that some backstop profiling and data estimation will be necessary to address circumstances where metering data is not available through technical faults or as a result of consumers choosing not to have a smart meter.

We also note the CMA's support of the powers for Ofgem to implement switching and settlement reforms in a timely and cost effective manner as contemplated by DECC in its draft legislation¹⁰. However, we are concerned that the legislation does not include code administrators in the list of parties who Ofgem is required to consult in relation to proposed modifications (where valuable expert input could be missed). We are also concerned at the diminished capacity for industry parties to appeal decisions of the Authority in relation to modifications made under this legislation. We comment further on these proposed powers in the context of our wider considerations regarding the remedies concerning industry code governance.

Industry Governance

Amendments to industry codes can have significant commercial implications for parties that are obliged to sign up to them. Additionally there are impacts on service providers to these signatories and downstream customers who may see savings or additional costs arising from changes to the codes. We therefore continue to believe that it is important for all stakeholders to have the opportunity to take part in the processes that underpin the evolution of these multi-party agreements. We believe that effective industry code governance must provide for such inclusivity while delivering an efficient process founded on common principles that enable changes to be assessed impartially.

This is a significant challenge in the face of the unprecedented level of change currently facing industry parties. This includes the roll-out of smart metering, introduction of new low-carbon technologies, demand side flexibility and the evolution of European regulations.

Ofgem Independence

We support the proposed requirement for Ofgem to publicly comment on draft legislation and policy proposals which are relevant to its statutory objectives and which are likely to have a material impact

¹⁰ <https://www.gov.uk/government/publications/draft-legislation-on-energy>

on the GB energy markets. We agree that this will increase transparency in policy making and help to underpin Ofgem's independence.

We note that the CMA expects this commentary to include the interaction between the proposed legislation and the existing regulatory framework of licences and industry codes. We would encourage Ofgem to, wherever possible, engage with industry code bodies' expertise when considering such interactions.

Code Adjudicator

We are pleased that CMA has moved away from its provisional recommendation to appoint an independent code adjudicator. We believe that such a body may have adversely impacted coordination between industry code change governance, licence modifications and legislation. However, we believe that it remains important that industry code changes are able to be appealed to the CMA, where the Gas and Electricity Markets Authority (the Authority) has approved a change that was recommended for rejection by the relevant industry code panel.

Ofgem Publication of a Strategic Direction

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 DECC's Strategy and Policy Statement into appropriate signals as to how Ofgem expects high-level policy decisions to be implemented via code changes. We believe this strategy should focus on required outcomes, rather than dictating the details of required changes. We would also encourage Ofgem to consider a time horizon of 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.

Development of Code-Specific Work Plans

As we noted in our response to the CMA's provisional findings report and notice of possible remedies¹¹, 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. We therefore agree that all code administrators should develop work-plans illustrating how their respective industry codes will need to develop to deliver Ofgem's stated strategic direction.

We note that the CMA remedy makes Ofgem responsible for the development of these industry code work plans but leaves the mechanism by which they will be prepared more open. We agree with the CMA's recommendation that Ofgem should make use of the expertise of industry code panels and code administrators in preparing these plans and that consideration should be given to producing a consolidated cross-code strategic work plan.

We look forward to working with industry code panels, and other industry bodies, including DECC and Ofgem to develop a strategic work plan that encompasses cross-code change. We believe this would enable more efficient planning and allocation of industry resources. Such a change programme should also encompass a longer term strategy and take account of the various domestic and European policy and change initiatives.

¹¹ <https://www.elxon.co.uk/wp-content/uploads/2015/08/31-Jul-2015-CMA-response-findings-and-remedies.pdf>

Together, Ofgem's strategic direction and the industry code work-plans will enable industry parties, code panels, administrators 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 proposed three-tier change process (i.e. self-governance, nominal code panel oversight, or Ofgem-led strategic change). We comment on this change process in further detail below.

The Consultative Board

We believe the proposed consultative board shares many of the features of the cross-code expert group we suggested in our response to the CMA's provisional findings report and notice of possible remedies. That is: a cross-code group, comprising experts on the various arrangements with a desire to work together to make things better, able to provide expert design advice on issues relating to all industry codes. We see this as a mechanism for the industry to provide input on solutions to policy proposals at an early stage and develop a strategy for (or facilitate the design of) cross-code change.

We also support the intention of this remedy to provide a forum to ensure Ofgem's early engagement on change. Early engagement in the consideration of industry code changes by Ofgem can help ensure that assessment work meets the Authority's needs, thereby reducing the risk that subsequent work needs to be undertaken.

We therefore support the concept of a consultative board and agree that it is right that Ofgem should be responsible for establishing this group. We agree that Ofgem must be an active participant in overseeing this group. However, it is less clear that Ofgem should be required to administer its work, so long as the governance and responsibilities of the board (and its members) are clearly defined.

Responsibilities of the consultative board

We note that the proposed remedy places a number of explicit (or implicit) responsibilities on the consultative board. It is clear that this advisory group has a particularly wide remit and its deliberations could lead to assessment or implementation costs on industry parties that may not have been considered by the relevant industry code panels. Its responsibilities include:

- **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 (eg. by harmonising certain processes) (para 10.408);
- **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 (para 10.406);
- **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 (para 10.404);
- **Operational input and support:** provide additional oversight of (strategically important) modification proposals by:
 - providing a formal venue for Ofgem to contribute its initial views on the terms of reference of work groups (para 10.407(a));
 - ensuring that work groups are composed of members with the relevant expertise and, where appropriate, making additional resources available for the purpose of obtaining such expertise (e.g. commissioning third parties to carry out additional analysis) (para 10.407(b));

- reviewing discrete pieces of analysis performed during the development stage (following a request by the relevant code administrator) (para 10.407(b));
- identifying cross-code impacts (para 10.407(c)); and
- **Performance Monitoring:** reviewing the performance of code administrators (and, we assume industry code panels) in relation to the delivery of end to end project management plans relating to changes that deliver Ofgem's strategic direction (para 10.418); and
- **Direct control:** discuss the commissioning of third parties (we assume by Ofgem) to manage the implementation of changes (para 10.443).

Careful consideration will need to be given to the mechanisms by which this group would deliver its operational support, monitoring and control activities to ensure these dovetail with the standard industry change processes and responsibilities. In particular, the standards and measures of success for performance monitoring will need to be clearly articulated and subject to an appropriate decision-making process.

We therefore agree it is essential for code administrators and delivery bodies to be active members of this consultative board.

Ofgem Oversight of Change

We note the CMA's characterisation of Ofgem's dual role in industry change, that is: Ofgem as a gatekeeper (or approver) of Modifications to industry codes and Ofgem as a 'gap-filler', addressing the need for change where this is not forthcoming or where co-ordination across codes is needed (for example, by exercising the Significant Code Review (SCR) provisions).

A three-tier change process

We believe that the remedies proposed by the CMA in relation to Ofgem's powers and responsibilities will, in aggregate, lead to a three-tier industry change process:

- **Tier 1:** Changes that relate to Ofgem's strategic direction. These changes would be subject to wide-ranging, enhanced Ofgem oversight and control which may preclude consideration by the relevant industry code panel(s).
- **Tier 2:** Material changes that, while not related to Ofgem's strategic direction, still merit being subject to approval by the Authority following a recommendation from the relevant industry code panel.
- **Tier 3:** Changes that are relatively self-contained and can be considered by the relevant industry code panel under the 'self-governance' provisions without reference to the Authority.

Ofgem control of strategically important change

The remedy includes substantive and wide-ranging provisions that afford Ofgem unilateral control over strategically important changes. Ofgem will have the power to raise such modifications directly, instruct licensees (including code administrators) to raise such modifications or subsume modifications raised by any stakeholder into a category of 'strategically important status'. This latter power echoes the current ability for Ofgem to subsume Modifications into any ongoing SCR. An important difference here is that this new power would be ongoing, emphasising the importance of clarity and transparency in Ofgem's stated strategic direction.

Changes that are categorised as 'strategically important' will be monitored closely by Ofgem either directly or via the consultative board. It is also proposed that Ofgem be able to 'call-in' modifications and manage these themselves or commission an independent third party to manage the relevant

assessment and implementation processes themselves. Further, it is proposed that the costs Ofgem incurs in managing called-in modifications be charged back to industry.

We understand the stated intent that code administrators and code panels should manage these strategically important changes according to their respective industry code work plans. Furthermore, we believe that the powers noted above are intended to act as an incentive to ensure timely assessment and implementation of changes in a co-ordinated fashion.

We believe such an approach could be effective in reducing the risk of duplicated effort and avoiding extended timescales for introducing wide-scale change. However, it is essential that Ofgem works closely with industry parties in order to ensure these processes operate effectively and do not become a disincentive for industry parties to engage in the overall process. We agree that clear and transparent guidance must be published by Ofgem indicating the factors that it would take into account when determining whether to utilise its call-in power.

Engaging Industry Expertise in Directed Modifications

We believe it is essential that industry experts work closely with Ofgem in developing code modifications. We welcome the inclusive approach taken by Ofgem in relation to its work on Half Hourly Settlement and faster, more reliable switching. However, we are concerned that draft legislation¹² produced by DECC in relation to Ofgem powers to direct modifications is silent on the steps that Ofgem should take to engage with industry experts prior to publishing proposed modifications. We assume the CMA anticipates that any prior engagement would take place through the proposed consultative board.

This is important since ELEXON is responsible for maintaining the Balancing and Settlement Code. We assume that the practical implementation of modifications to this code made by Ofgem would therefore fall to us in line with existing provisions¹³.

We are also the body responsible for the delivery of settlement systems and processes. We manage the development and implementation of changes to BSC Agent (central) systems and processes. We work closely with our service providers in translating code modifications into the relevant detailed requirement documents.

We also note that our delivery of change is measured by Ofgem (through monitoring defined in the Code Administration Code or Practice). This is set to be extended under the CMA's remedies by monitoring via the proposed consultative board under the terms of a licence. Consequently, we would be concerned if we were not consulted in the development of changes proposed by Ofgem.

Given our responsibilities, and those of other code administrators, we believe it is essential that code administrators and delivery bodies be fully engaged in the development of all modifications to their respective codes. We are concerned that the successful delivery of proposed changes could be subject to otherwise unforeseen risk, cost and delay if code administrators are not consulted such that the impact on central systems and processes can be taken into account. We therefore believe Ofgem should be obliged to consult with code administrators prior to directing a modification.

¹² <https://www.gov.uk/government/publications/draft-legislation-on-energy>

¹³ Where BSC modifications are approved by the Authority, we are directed to make such modifications to the BSC by the Transmission Company in accordance with its responsibilities under the Transmission Licence.

Appropriate use of Checks and Balances

We believe that industry code panels must continue to have a role in voting on recommendations associated with all Modifications. This is an important check and balance in the existing industry code governance. We are concerned at the diminished capacity for industry parties to appeal decisions of the Authority in relation to modifications made under the legislation recently proposed by DECC.

We believe it is feasible to require that, following the 28 day consultation period set out in the draft legislation, Ofgem submit its proposed modification (including consultation responses) to the relevant industry code panel (or equivalent) for review. The relevant industry code panel would be required to submit its recommendation to Ofgem in light of the information provided (i.e. without a further panel-led consultation).

This approach preserves the important check and balance in the existing industry code governance. It provides for a second body (the code panel) to review the benefits of any solution developed by Ofgem. It also preserves the (limited) capability for industry parties to seek a second opinion from a subsequent body (the CMA)¹⁴. This helps to mitigate the risk that a single body (in this case Ofgem) develops and implements its own solutions without due reference to the views of impacted parties. This additional check and balance would result in only a modest increase in the time taken to reach a decision on a proposed modification.

Taking account of consumers

Consistent with our response to the CMA's provisional findings report and notice of possible remedies, we believe there is merit in providing for consistency across the relevant applicable industry code objectives and also between industry codes objectives and those of Ofgem. Such consistency would reduce the risk that complementary changes arising under different codes are not progressed as a result of being assessed against different sets of principles. This is particularly relevant in the case of modifications progressed as self-governance provisions since these changes are only subject to the consideration of industry code panels.

We are encouraged that the CMA has recommended that the proposed licensing regime for code administrators and delivery bodies should ensure 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 administrators and industry code panels. This would ensure that industry code panels would need to consider the impacts on consumers arising from code changes in addition to the parties to their respective industry code.

Licensing code administrators and delivery bodies

We agree that the independence and impartiality of code administrators is important. We note the CMA's reference to the quasi-independent status of code administrators.

Since the governance of industry codes varies, we believe that the CMA should publish a clear and consistent definition of the functions to be licenced.

We understand the purpose of licensing code administration and code delivery to be twofold:

¹⁴ For example, the provisions of the Electricity Act offer the opportunity for Authority decisions to be appealed to the CMA in the event that the Authority approves a modification which was recommended for rejection by the BSC Panel.

1. To ensure that code administrators act independently of industry parties in the interests of competition and consumers; and
2. 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.

Licensing to ensure independent focus on competition and consumers

In respect of the first consideration, we would note, that the BSC and ELEXON are founded on principles of impartiality. For example, under the BSC, all BSC Panel and Panel Committee members and chairs are required to be impartial. They must not act as representatives of the body or person by whom they were appointed. All members are required to provide a written undertaking to this effect prior to taking office.

Further, while ELEXON Ltd. is a wholly owned, arms-length subsidiary of National Grid, our funding arrangements (which see our costs 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).

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. We strongly support the principle of critical friend (as set out in the Code Administration Code of Practice) and agree that code administrators play a vital role in ensuring that the voice of all industry parties can be heard and that they have the opportunity to participate in industry code processes.

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. We note the CMA's view that 'Code administrators (and delivery bodies), as licensed bodies with better defined powers and responsibilities, and appropriate funding, would be able to step into the process where appropriate to support Ofgem and code panels in their respective functions.' We would therefore welcome greater clarity on the funding models that the CMA would consider appropriate in this respect and, in particular, how such funding might support impartiality and the better delivery of Ofgem and code panel functions.

Licensing to enable Ofgem oversight and control

Separately, in relation to the second consideration, the BSC already affords the Gas and Electricity Markets Authority particular control over the BSC change process:

- These provisions mean that (unless the Authority is satisfied that variation is required due to the complexity, importance or urgency of the change) the BSC Panel must make its final determinations regarding a BSC Modification between 2-8 months from the date on which the Modification was raised. The Authority can, at any time, request that the Panel re-prioritise Modifications, and amend timetables for the development, assessment and implementation of changes.
- The BSC also enables the Authority 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.

We support consistency between the governance of code bodies, including their objectives, obligations, impartiality and funding. With these considerations in mind we understand the attraction of a licence regime for code administration and delivery. We believe that licensing these functions creates a fundamental shift in the accountability of such code bodies.

Under the CMA's proposals code administrators and delivery bodies will be required to support industry code panels (which are unlicensed creatures of their respective codes) while operating under the terms of a licence under the oversight of Ofgem's consultative board and the Authority in developing, assessing and delivering changes on behalf of industry parties for the benefit of consumers. It will therefore be important to ensure that code administrators can act autonomously for the benefit of industry code parties and consumers. Furthermore, that there is transparency in the interactions between code administrators and their various stakeholders.

New Powers for Code Administrators

In our response to the CMA's provisional findings report and notice of possible remedies we also expressed concern that code administrators do not possess the powers required to better progress and co-ordinate change and that the absence of such powers would make it impossible to deliver benefits associated with licensing code bodies. We are therefore pleased that the CMA has recommended new powers for code bodies.

We support the proposal that code bodies should be given the capability to raise changes to their respective industry codes. A further extension of these powers might enable code administrators 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.

Implementation considerations and future reviews

We note that the changes to industry code governance recommended by the CMA will require changes to legislation and the implementation of a licensing regime. We believe that industry codes themselves will also need to be amended to reflect these proposals. Amended governance and funding arrangements and harmonised processes should be set out in the relevant codes or, alternatively, where relevant removed from industry codes and embedded in an enhanced Code Administration Code of Practice. We believe these consequential changes should be considered when implementing the licensing regime (they could, for example, be directed by the Secretary of State to ensure consistent and timely implementation).

We also note the CMA's recommendation that Ofgem (directly or via the proposed consultative board) keeps industry code governance under review. In this regard, the CMA highlights a need for further consideration of industry code simplification, consolidation and competition in the delivery of code services. We offer the following comments in respect of these aspirations:

Simplification of industry codes

The direction of travel for many years has been to provide for certainty in industry code requirements by capturing prescriptive detail. This is understandable since industry codes are (in one way or another) multilateral agreements. Some are seen as commercial codes, others as purely technical. However, they all have commercial impacts on the parties to those codes which are ultimately felt by consumers.

Given their commercial implications, industry codes attempt to find a balance between certainty, size and complexity. However, capturing detailed rules and requirements increases the size and complexity of codes, which then become less readable by those without specialist technical knowledge. Some areas of industry codes, particularly those that support interoperability, need detailed prescription.

Nevertheless, we believe there is merit in exploring the application of a principles-based approach to industry codes where possible. Such re-worked codes should be smaller, simpler and provide for easier innovation.

Another approach could be to harmonise existing processes where they exist across codes. For example, each code has a change process. These processes could be removed from their respective codes and consolidated in a separate 'code administration code', perhaps by evolving the Code Administration Code of Practice. Any harmonisation work should avoid undue complexity and seek to deliver processes that are simple in design and flexible enough to be pragmatic in application.

Consolidation of industry codes and services

Reviewing the scope of industry codes would be a major exercise. However, there may be benefits in re-casting the landscape of codes over the mid to long term and we believe this would be facilitated by first simplifying and harmonising codes as noted above.

We believe that consolidation of code administration services might, in the medium term, bring more benefits. It would allow for industry parties to have a reduced number of interfaces for managing code activities and changes. 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 before any organisation (including ELEXON) could provide (or seek to provide) any code administration services in addition to the administration of 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 compete on equal terms and the existing restrictions on our participation in any competitive process must be removed otherwise the benefits of such competition are lost.