

CMA Codes

Summary

1. Citizens Advice is the statutory consumer representative for the codes. It has membership and voting rights on a number of modification panels. It has the right to raise modification proposals on most codes, though this right is heavily restricted on the main gas code, the Uniform Network Code (UNC). Given their materiality for consumers when compared to other codes, and the constraint to engagement caused by the sheer number of codes, we are most active on the Balancing and Settlement Code (BSC) and UNC panels.
2. As we stated in previous evidence, we believe the industry code governance system is relevant to the CMA investigation and we welcome it being included under theory of harm 5.
3. While we believe we play an important and useful role in codes, the proliferation of codes and the complexity and resource intensiveness of the respective change processes does limit the effectiveness of our engagement in the governance of the energy market. It also follows that this would be the experience of smaller firms and new entrants. It is clear that the current code arrangements do not facilitate major change in a timely way.¹ The CMA is right therefore to home-in on electricity code complexity, and accessibility and timeliness of the modification process, as the focus of its investigation.²
4. One area that is not explicitly addressed in the working paper that we believe is core to the operation of the codes is the misalignment between the specification of code 'objectives' and Ofgem's statutory duties. We believe this inconsistency should be resolved to make for a more open and accessible modification process for all stakeholders, and help align commercial and wider economic and consumer interests. We expand on this point later in this submission.
5. If the CMA finds that the codes are having an adverse effect on competition, the failure of the Code Governance Review (CGR) to fix the codes suggests that radical change may be needed. This may mean consolidating the electricity codes and/or, if what we are really experiencing are the limits of industry self-

¹ We note that subsequent to this paper being drafted, the BSC Panel issued a consultation on whether the implementation of BSC P272 should be further delayed. https://www.elexon.co.uk/wp-content/uploads/2014/10/235_04_P272_Implementation_Delay_1.0-1.pdf

² The Energy and Climate Change Committee (ECCC) identified the length (960 pages) and complexity of the Smart Energy Code as an issue at paragraph 21 of its recent report, *Smart Meters: progress or delay*, . <http://www.publications.parliament.uk/pa/cm201415/cmselect/cmenergy/665/665.pdf>

regulation, creating a separate process led by Ofgem and with it as the decision-maker, for making major 'public policy' changes.

6. An Ofgem process for initiating major code projects does exist, in the form of Significant Code Reviews ('SCRs'). These were introduced following Ofgem's first CGR but have arguably not worked as a process due to a lack of timely progression of issues and policy u-turns. The gas security of supply SCR, launched in January 2011, is yet to be implemented but this should take place in October 2015 – four years and nine months after inception. The electricity transmission charging SCR, launched in July 2011, is due to be implemented in April 2016 – also four years and nine months after inception – and is currently subject to a judicial review challenge. The electricity balancing SCR, launched in August 2012, has still not been implemented – and has seen Ofgem reject proposals that it itself effectively instigated (P304 and P314). While the SCR process appears to have been intended to allow the regulator to grab important issues by the scruff of the neck and drag them forward, its practical effect increasingly appears to be the opposite – that these projects conspicuously lack momentum, and make very slow progress. It is hard to make a case that the SCR model is fit for purpose – and the CMA may wish to consider whether there is a better means for delivering reform to key areas of the industry rules that are governed by the codes.
7. Ultimately, the challenge for the CMA is not so much to identify the problems with the current arrangements. That the codes are complex and that change is a protracted business is a statement of fact. The challenge is rather to gauge the extent to which that complexity distorts competition or hinders innovation and recommend proportionate and enduring solutions.
8. We are conscious that a CMA finding that incumbents are using the codes to inhibit innovation or stifle competition may point to deeper problems of market structure that might need to be attacked directly, in addition to the more obvious problems with the rules themselves. Incumbents with market power may well be able to use whatever governance arrangements that are put in front of them, no matter how simple or elegant, to their advantage given their superior resources.
9. To help delineate 'rule' and 'structural' effects - i.e. those effects due to the complexity of the codes rather than those with deeper causes - it might be useful for the CMA to identify reforms that, in a competitive market, might have been expected to have emerged organically from the codes process but have not. Why, for example, modifications to substantially reduce the time it takes for

consumers to switch only came forward as a result of pressure from Ofgem and the Government to streamline the process?³ It appears to us that a plausible explanation is that the complexity and resource intensiveness of the process hinders the ability of ‘challenger’ firms to progress modifications that would presumably be to their benefit.

10. The codes vary in the extent to which policy is discussed by the governing panel or by workgroups, and in whether the governing panel acts with genuine independence or not. For example, in the case of the BSC Panel, considerable time is spent in critically appraising the modification assessments brought forward by industry working groups. Conversely, in the case of the UNC Panel, discussions are often more focussed on procedural matters, with the discussion of the benefits of (or problems with) a proposal largely conducted by the industry working groups. While members of both panels are obligated to act independently of the interests of their day-job employers, it is particularly unusual for members of the UNC Panel to vote against the interests of their employers. We would have greater confidence in code processes to bring forward coherent, fully assessed proposals if there was an onus on all panels to adequately justify policy recommendations and clearer safeguards to ensure genuine independence. It is possible smaller market participants would also take confidence from this; we note that your small supplier case studies paper suggests several lack confidence in the integrity of panels.
11. Aside from consolidating the codes, the CMA may wish to consider whether it should consolidate the underlying settlement systems behind them. In the retail market, dual fuel is the principal product, but the central industry systems for settlement and meter point registration in electricity and gas operate wholly separately. This appears inefficient.

Aligning Code Objectives

12. We believe the lack of alignment between the code ‘objectives’ and Ofgem’s statutory duties is contributing to the issues the CMA identifies in the codes working paper.
13. As it stands, code objectives are based on more confined ‘competition’ and ‘efficiency’ criteria compared to Ofgem broader duties to “protect the interests of

³ See for example, <https://www.ofgem.gov.uk/ofgem-publications/93224/fastandreliableswitchingdecisionfinal.pdf> and <http://www.gasgovernance.co.uk/sites/default/files/UNC477D.pdf>

current and future consumers”.⁴ While we understand the intent is for modifications to be assessed against an objective and simple set of criteria that are familiar to industry, in practice the lack of a direct link to outcomes contributes to an unhelpful abstraction of the debate from the real world impacts of the proposals. This was evident in a recent modification, UNC501, ‘*Treatment of Existing Entry Capacity Rights at the Bacton ASEP to comply with EU Capacity Regulations*’, a complex modification to alter the way capacity was allocated at one of the main entry points for gas from the North Sea and Europe to meet new EU rules, where only one of the 15 submissions by market participants sought to identify the possible impacts for consumers, or even how these impacts might be transmitted.⁵ The lack of a consumer objective to ground the debate also contributes to a situation where arguments about procedure often take the place of discussions about the substance of the modification itself.⁶

14. While we acknowledge that Ofgem checks the modifications against its broader statutory duties as part of its role as the ultimate decision maker, this happens at the end of the process, by which time assumptions have become entrenched and momentum built up behind solutions. There is also a limit to the check that the panel consumer representative can provide at an early stage – in part because it is not possible to attend the work group meetings where the detailed discussions about modification take place (as the working paper notes at paragraph 28). By the time the modification comes before the panel, the debate is often limited to an introduction and vote along industry lines.⁷ The introduction of a consumer objective would mean modifications would be presented and assessed in a less complex way – because it would need to explicitly describe consumer impacts from the outset – providing a ‘point of entry’ into debate for consumer representatives and other stakeholders.⁸ Modification that better considered consumer impacts would also streamline the Ofgem stage of the process, reducing the need for it to conduct its own assessment late in the process – a point that the Brattle Group made in its report for the CGR.⁹

⁴ Section 4AA, Utilities Act 2000 <http://www.legislation.gov.uk/ukpga/2000/27/section/9>

⁵ <http://www.gasgovernance.co.uk/0501>

⁶ See for example UNC 0522 – a modification to make a simple change to the code to substitute email for fax communications that has become bogged down <http://www.gasgovernance.co.uk/0522>

⁷ This is partly a function of heavy panel meeting agendas limiting the time that can be spent on any one modification. This is a particular problem in the UNC – see this recent agenda where 16 modifications were listed <http://www.gasgovernance.co.uk/sites/default/files/Panel%20Agenda%2019Feb15%20v2.0.pdf>

⁸ Basic information about consumer impacts is often missing from modification reports, information such as the classes of consumers that might be affected – see for example UNC 523S, where the modification proposal does not identify the classes of consumers that utilise shared supply points (domestic or industrial and commercial) <http://www.gasgovernance.co.uk/0523>.

⁹ The Brattle Group Report for the CGR identified duplication as a problem – see page 88 http://www.brattle.com/system/publications/pdfs/000/004/861/original/Critique_of_the_Industry_Codes_Governance_Arrangements_Hesmondhalgh_Jun_2008.pdf?1378772135

15. We note that Ofgem considered and rejected proposals to align the code objectives with Ofgem's statutory duties as part of the CGR. The view at the time was that it would ask industry to enter the realm of 'public policy' – something they did not have the resources, expertise or incentive to do. We disagree with this view for four reasons.

16. Firstly, the industry, supported by the code secretariats, has demonstrated that it is capable of conducting basic consumer impact analysis. Cost benefit analysis incorporating consumer impacts was, for example, conducted for the faster switching modification UNC 0477 '*Supply Point Registration – Facilitation of Faster Switching*'.¹⁰ The problem is that while this analysis is undertaken from time to time, it is not a default, and is rarely done for modifications that do not have a direct and obvious consumer impact, even if they are likely to have material indirect impacts.

17. Secondly, whether it is recognised or not, the industry is already operating in a public policy space under the current self-regulatory arrangements. Fundamental issues about the future of the energy market – switching, smart grids, cash out reform, and European market integration, locational pricing – are being advanced through the standard code modification process. That some of these issues are now informed by SCRs is important but does not mean that the industry is left dealing with a residual set of commercial issues. The timing and final design of the cash-out reforms will for example, be heavily influenced by its progression through the BSC modification process and have real implications for security of supply – an issue where the Government itself has recognised that commercial and public interests might not align and has sought to address with the Capacity Mechanism.

18. Thirdly, the buffer that exists between the commercial/engineering work of the codes and domestic consumers in the old centralised energy market is being eroded by the advent of distributed generation, smart grids and DSR. Transmission system operators (TSO) will soon be able (at least technically) to reach into the home via smart infrastructure to dial down or switch off smart appliances to maintain the stability of the network and codes will need to be amended to govern these interactions and protect consumer rights. This has become apparent in the development of the new European Network Codes, where the TSOs have sought to use them to impose direct obligations on some

¹⁰ <http://www.gasgovernance.co.uk/0477>

domestic consumers to maintain uninterruptible communications links and compliance test their equipment (e.g. solar panels) - obligations that are not at all well adapted for non-industry actors and are not matched by rights for consumers to be consulted about their design or implementation.¹¹ It follows that documents like these that impact consumers in this way should at the very least be explicitly aligned with their interests through the specification of the objectives.

19. Finally, Ofgem's reluctance to align code objectives with its broader statutory duties runs against the grain of other regulatory decisions that seek to shift the focus of industry assessment from processes to outcomes. As part of its recently introduced RIIO price control processes, Ofgem has sought to encourage the monopoly networks to engage directly with consumers and other users of their networks in order to develop the policy proposals – price controls – that they will be subsequently be subject to. The intention was to force the networks to become more consumer-centric. A key part of Ofgem's rationale for introducing the Standards of Conduct regulations via the Retail Market Review process was to ensure that consumers were treated fairly, with a new onus on suppliers to ensure they thought carefully about the consumer impacts of their policies and processes. More broadly, part of the underlying lack of public confidence in the supply sector is founded on so many consumers having had poor interactions with the industry, whether in sales methods or in complaint handling. Encouraging the industry to think through what changes to the industry codes mean to the customer experience of their services could help to improve quality of service, and a consumer code objective could drive this consideration.

¹¹ See for example, the Draft Emergency and Restoration Code, Article 30(1) <https://www.entsoe.eu/major-projects/network-code-development/emergency-and-restoration/Pages/default.aspx>