Gemserv

Competition and Market Authority
Victoria House
37 Southampton Row
London
WC1B 4AD

Dear Sir/Madam

ENERGY MARKET INVESTIGATION – UPDATED ISSUES STATEMENT AND CODES

Thank you for the opportunity to respond to the statement on your energy market investigative work.

The challenges faced by all market participants are heavily contextualised by the unprecedented energy market revolution now taking place, driven by policy initiatives such as the Green Deal, Smart Metering and the Energy Market Review. These market transformational initiatives have naturally led to a significant volume of change in market arrangements, as demonstrated by the introduction of two new Codes: Smart Energy Code (SEC), and the Green Deal Arrangements Agreement (GDAA), together with the consequential high volume of enabling modifications to existing codes. We note here that such changes are necessary to ensure that energy market participants (of which there are many, and in different forms) are able to continue to work effectively together, whilst at the same time, enabling these important Government driven, consumer focused, transformational initiatives to be implemented.

Gemserv's wide-ranging expertise over the past 15 years as a code administrator (see Appendix for the codes we govern), means we are involved in many of the major policy developments and industry initiatives in the energy sector. These include our role as code administrator for the Master Registration Agreement (MRA) which oversees electricity switching practices and supports the settlement processes under the Balancing and Settlement Code (BSC), and for the Smart Energy Code (SEC) which sits at the heart of the implementation of GB smart metering. We have also been instrumental in supporting the implementation of the UK Government's energy efficiency programme for the Green Deal. Consequently, we are at the forefront of addressing the day-to-day operational challenges and issues that all energy companies are wrestling with, be they large, medium or small.

It might help if we first explain Gemserv's market heritage. This stems from the inception of MRASCo Limited back in 1998, which was formed to deliver a central registration code (the MRA) to oversee customer transfers in the newly developing competitive electricity market. Gemserv, was subsequently born in 2002 when it became apparent that the knowledge, lessons and experience of managing the new MRA, provided an excellent platform to help other areas of the energy market and potentially beyond. Gemserv has 19 shareholders comprising of suppliers & electricity distributors, by virtue of those origins.

Today, Gemserv comprises of 115 employees, stretching across a number of sectors, jurisdictions and countries, providing expert advice, governance and consultancy services to industry participants, regulators and governments alike. Whilst this heritage brings many benefits in terms of that deep market experience, we are also fully cognisant that this might be perceived by some as having vested interests - this is simply not borne out in practice. We work hard to ensure that our approach is pro-competition, that we operate with absolute integrity in all that we do, and constantly drive competitive innovative practice. Indeed, all our work is solely secured based on a competitive tender basis and we are firmly of the view that, all codes should be open to competition. We have evidence that this brings about not just efficient cost practices, but also ensures that the pencil remains sharp when it comes to demonstrating value for all market participants, large, medium and small and that markets work for the benefit of everyone.

Central bodies embrace, in the governance of codes, the level playing field principle, facilitating fair play for all stakeholders in the delivery of code governance practice that is consistent and does not confer any undue advantage on one party over another. Without this approach framed by mandatory multiparty agreements and/or codes, it is our experience that effective market interoperability and fair market practices would be at risk. If the financial sector experience in recent years teaches us anything, it is that gaps or loop holes in market arrangements result in opportunistic practices that work against the greater good and incentivise a race to the bottom as far as compliance is concerned.

It is against this backdrop we welcome the CMA's focus on codes. Our response centres on the theory of harm 5: the broader regulatory framework, including the current system of code governance. In that regard, we believe that, central codes should centre upon three key objectives:

- Simplicity;
- Consistency; and
- Accessibility.

Deliver against these, and the issues identified by the CMA will be addressed. Our comments draw heavily from these objectives as we seek to address the two separate issues identified by the CMA:

- Whether the number of Codes in electricity add to barriers to entry and/or expansion; and
- Whether the current system of industry code governance acts as a barrier to pro-competitive innovation and change.

We come from the starting point that code governance needs to evolve and later on we highlight those aspects that we believe could be considered, with suggestions on where further innovation might support the above objectives.

We trust that our response provides helpful insight to the key questions posed by your investigation and would be keen to meet you to discuss further the comments we have made or to delve deeper into our market wide governance experience, covering electricity, gas, water and telecommunications.

Why do we have codes?

Fundamentally, the purpose of many forms of code is to translate regulatory obligations into documents that enact the licence duties that energy companies must follow. Each code is therefore designed to support particular constituents, their obligations and duties, as well as their rights (e.g. voting). The matter of 'rights' is an important one, codes are designed not simply to enforce obligations and defined duties, but also to ensure that those party to a code can exercise those rights – this can be sometimes forgotten; for example, timing of interactions between parties and access rights to centralised systems or a right to raise and challenge code modifications.

The important point to draw out here is that codes also form the 'contract' between the relevant market participants who have a role in that area of operations. This 'common contract' approach avoids a plethora of bi-laterals that would otherwise have to exist, such is in the water sector, where a switch needs to be a discrete contract for that site.

Codes also mitigate regulatory and market practice uncertainty, supporting market transparency (not hidden behind contractual bi-laterals), and ultimately by driving good industry practice (race to the bottom is avoided). Therefore, codes help new entrants get started, they support supplier organisations that might not have the capability or leverage to deliver a multitude of bi-lateral agreements (generally the smaller organisations), and when done right, provide an expert resource to draw from in terms of the central bodies that manage them.

Finally, empowering industry participants to be able to drive code change is an important one for it is they that are incentivised to drive effective, efficient and competitive working practices and to take action when as a consequence of working experience, further opportunities for improvement are identified.

Codes therefore need to be well managed to ensure good governance practices are followed. They are managed via a mixture of formal governance such as executive boards, committees or panels, and specialist working groups. Sometimes they signpost and support other significant 'Agreements' (such as the Green Deal Arrangements Agreement via the MRA). Ultimately, codes seek to engage via collaborative approaches with a wide range stakeholders (including suppliers, networks, metering organisations, communication providers, regulators, consumer bodies) in the support of market design and operational practices.

As such, codes are constructed in a manner that seek to ensure that, through the exercising of obligations, duties and rights, no one party has a conferred advantage - they seek to create a level playing field. In other words, codes lie at the heart of effective competitive market practice. However, we believe that code systems do need to change to reflect the changing energy market place.

Does the number of Codes in electricity add to barriers to entry and/or expansion?

The question of barriers may not simply be a question about the right number of codes (and by inference whether there are too many codes). We ask ourselves: what is the nature of the problem that we are trying to solve? For example, by reducing the number of codes, will this naturally lead to reducing the perceived barriers to entry and/or expansion posed by the CMA investigation? Will this make them more accessible?

The UNC represents a single gas network code, and we note here the CMA reference to Project Nexus and the challenge of moving this forward. Large and potentially unwieldy codes can become impenetrable for the uninitiated. Other examples include the BSC for electricity running in excess of 800 pages (excluding all the ancillary documents), and the SEC has evolved to become a fairly large complex technical code (currently over 700 pages) - one that is still developing. These large codes require dedicated personnel that are able to build up expertise. Indeed, training courses have now spawned designed to cater for those organisations that need to improve their understanding of such codes.

Notwithstanding that codes may, through necessity become large, certainly in the case of the MRA and BSC, some codes have evolved and provide a joined up approach across managing change and market assurance. So, whilst codes may be complex due to their contractual nature and the need to balance objectives, duties and rights, they manage a commercially competitive environment, whilst supporting consumer protection principles.

Fewer codes leads us to the concept of consolidation. We observe that the matter of 'code consolidation' as a concept can be open to interpretation, potentially detracting from the real issues. Indeed, the fear of code proliferation has on occasions led to Ofgem looking for a 'home' for new regulatory obligations that may not necessarily be a logical one. One example is the implementation of dual regulatory governance arrangements for the Theft Risk Assessment Service (TRAS), a single service provision which currently sits under two codes: The Distribution Connection and Use of System Agreement (DCUSA - for electricity) and the Supply Point Administration Agreement (SPAA - for gas). These codes were not originally designed with energy theft in mind and consequently had to undergo material change, particularly as some licencees are not obligated to be a party to TRAS, with the unintended consequence of generating more change.

Further, taking code consolidation to an ultimate conclusion could mean attempting to fit everything into one home, with the resultant code itself becoming almost impenetrable.

We believe it might be better to focus on codes being fit for purpose for the relevant market sector, e.g. Balancing and Settlement, wholesale charges, retail, metering and so forth. Also, we consider there is a case for codes to be differentiated between upstream and downstream market operations in order to avoid possible conflicts of interest between them during decision making, as well as supporting technical and inter-operational clarity for

participants. Codes that are focused on relevant areas of the overall market, has the advantage that smaller players are only required to take on obligations relevant to the area of the market in which they operate.

We appreciate that ultimately this could lead to some code consolidation, but this should be a natural outcome, based on good design and applying the three objectives as a starting point: simplicity, consistency and accessibility.

Does the current system of industry code governance act as a barrier to pro-competitive innovation and change?

Code complexity can arise for a number of reasons, and whilst we must avoid code complexity for its own sake, there are circumstances where it is a natural consequence of the highly technical aspects which the code is seeking to govern, e.g. the technical specifications pertaining to security of meters in the SEC are necessarily complex to meet the high standards required, and settlement matters under the BSC seek to manage complex network management and commercial risks. However, we have also observed that code drafting can come about as a consequence of legal drafting, usually driven by government policy seeking to strike a balance between the needs of a policy initiative and not wishing to unintentionally disrupt current market practices.

So, whether or not code complexity is a natural consequence of the above, it is very important to ensure that all market participants are not disadvantaged and that they can share equally in a pro-competitive energy market place. This is likely to require varied governance practices, tailored to ensure that all participants have an equal voice (e.g. via differentiated voting arrangements) and an opportunity to engage (e.g. via constituent design methods). Moreover, that they are able to enter and participate effectively in the market, including having a say in the governance and operation of that market.   Get that right, and we believe that it is questionable whether, just because a code is complex, this is necessarily a barrier to entry.

A good place to start is to ensure there are the right incentives placed on central code bodies to drive the right mind set. Not all code administration is open to competition, and we believe they should be. Competition will drive methods and approaches that do not simply drive efficient cost and efficient practices, but drive tailored governance and engagement approaches aligned to the client's needs. Under a competitive market framework for code body to do otherwise, is to risk losing the trust and engagement of code participants, who are of course ultimately the 'clients' of the central code body.

The CMA questions whether code modification processes are too slow. Gemserv administers the MRA and as part of its secretariat responsibilities, this includes regular reviews with industry participants on code modification practices. This has led to, for example, work being undertaken under the auspices of a Code Review Expert Group, which investigated a wide range of MRA code matters. This work led to simplification of procedural documentation, reinforcing alternative code modification practices, and perhaps of particular interest to the CMA, more recently improvements to the MRA Development Board constitution to better reflect views of smaller energy companies.   The MRA has always enshrined self-governance principles, and we note here that as part of Ofgem's Code Governance Review exercises, that other codes were moved towards similar self-governance models, demonstrating that there are lessons to be learnt. That said, what really exists is a form of co-governance across codes, reflecting the regulator's active role in code governance processes; for example, Ofgem is involved with approving material market code changes and delivering the appeal rights for code participants for decisions that are made.

Code review exercises are undertaken via wide ranging consultative process (with large and small energy companies). The MRA already has an extensive self-governance principle at its heart, and as a code has often been recognised as an example of good practice, demonstrating that the MRA has proven to be an efficient means of progressing industry change. For example, it was the first pre-existing central code to put in place changes to support smart metering and it developed the Electricity Central Online Enquiry Service (ECOES). ECOES is a supporting centralised system, providing services in support of registration processes, and also supports Feed-In-Tariff services. ECOES processes, more recently, have been acknowledged as a requirement for central registration services in a smart world.

Notwithstanding the above, we are aware that for some codes a change can take years to conclude. Whilst this feels intuitively unnecessary, and indeed sometimes questionable, some changes do take longer than others due to their technical nature. However, there is a balance to strike between allowing for effective engagement and speedy action.

Indeed, it is worth noting that Ofgem has recently decided to facilitate a wider 'change' window for DCUSA modifications that are of a technical and wide-reaching nature.

There are however challenges with code modification practices. They must be sufficiently robust to provide absolute clarity and certainty with regard to the practices and processes to be followed, i.e. the process for change modification consultation and the time allowed needs to accommodate the different energy company capabilities to implement change (for both large and small energy organisations). So there is clearly a tension – too quick and individual company customer systems could be compromised; too slow and urgent change that benefits consumers can be frustrated. Consequently, codes such as the MRA, have urgent code modification processes to help drive forward changes that warrant urgent treatment, e.g. to avoid the delay that can result in the realisation of consumer benefits or reduce consumer detriment. Furthermore, it is worth noting that CACoP helps drive cross code working.

How do we move forward?

Gemserv agrees there is a need to simplify codes and their practices. Indeed, we believe there is also a responsibility on Ofgem to ensure that new entrants are fully aware of their obligations at the time of licence application and that perhaps more could be done to help them understand what these entail either by Ofgem or the code bodies themselves.

However, we are very cognisant of the resource challenges smaller energy companies face. For example, we have noticed that resource constraints may mean that company representatives may not possess adequate knowledge to properly engage in discussion, even when they do resource governance groups and workshops.

We note the challenges faced by new entrants and smaller suppliers to help navigate codes to help them do business. Indeed, there is a growing case for central code bodies to accommodate the changing energy market dynamic they serve. With the growing prevalence and needs for smaller energy organisations, Gemserv believes that code bodies could do more to tailor their practices in order to cater for the varying needs of different types and sizes of energy companies and market participants and perhaps, by extension, to cater for the growth of non-traditional business models.

This is why Gemserv has instigated a smaller supplier engagement strategy, to complement the following services (free at the point of delivery) that we provide as a central code body:

- Code introductory and awareness training
- Published end-to-end process diagrams
- Market entry 'hand holding' practices
- Critical friend services
- Helpdesk services
- Code experts to advise and guide, supported by people drawn from the industry we serve
- Special small supplier 'only' days to listen and understand how we can help them further engage in market solutions
- Cross code working under a Cross Code Working Group

Furthermore, we are garnering views from energy companies on how to simplify and demystify codes. We are hearing that what is lacking is a strategic approach to future and existing code development. What they also seek is consistency and a design architecture approach to help manage change. Accordingly, there may be a

place for an overarching code roadmap, one that shows how all the codes fit together and where stakeholders can 'drill down' to the individual detail in each code.

Gemserv also believes there is value in having an overarching framework that could signpost code obligations in a holistic approach across all codes, perhaps enabled by search technology to help all participants engage more effectively e.g. smaller energy companies, consumer bodies, may find this capability particularly helpful.

This is leading us to consider further how to ensure that obligations and rights that exist within codes might be better harmonised and standardised – perhaps via a standard code model or contract. A standard code model could for example, seek to strike a balance across all codes with regard to self and co-governance principles, competition and consumer protection, reducing the need for Ofgem input, and thus enabling the regulator to concentrate and prioritise their limited resources on those aspects that have more significant market effects.

As we have commented in our response, there are merits in ensuring that codes are fit for purpose in terms of their boundaries (e.g. networks versus retail). The approach not only reduces code complexity, but ensures codes are well matched with competitive market practices. In that regard, a single registration code (covering both gas and electricity), one that embraces all governance practices to manage retail practices, might be a good way to go forward for retail services and for those new entrants wishing to get a stake in a competitive energy market place.

We have yet to test these ideas further, but they certainly play a part in helping to deal with the more fundamental questions of simplicity, consistency and accessibility.

I hope the above comments help to inform on your work. We would welcome the opportunity to discuss these matters further, to help answer any questions you may have with regard to industry code management practices, or indeed any points raised in this letter. For example, it might be helpful to elaborate upon the MRA, its philosophy, structure, and how it goes about managing the day-to-day interactions with all MRA participants.

Yours faithfully

Tony Thornton
Head of Transformation

Appendix - Central codes managed by Gemserv

	GAS	ELECTRICITY	ENVIRONMENT
RETAIL		MRA	GDAA
NETWORK	IGT UNC		
METERING	SEC	MOCOPA	
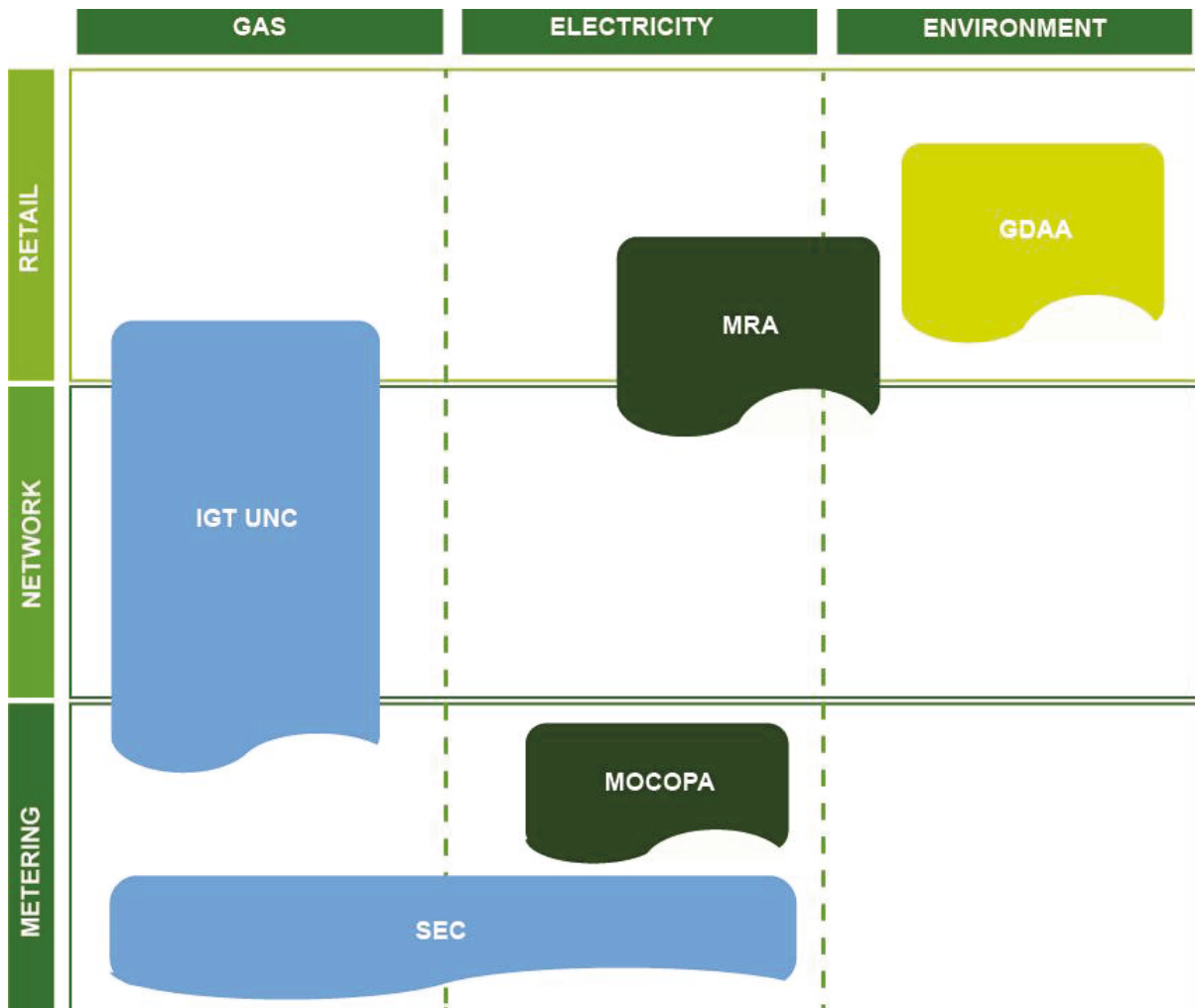
Key:

- GDAA (Green Deal Arrangements Agreement)
- iGT UNC (independent Gas Transporters Uniform Network Code)
- MOCOPA (Meter Operation Code of Practice Agreement)
- MRA (Master Registration Agreement)
- SEC (Smart Energy Code)