ESO

Energy Code Reform – MAC pre-read

Steering questions

Exec Summary

- The code change process governs the way in which changes to the industry regulations work. In the case of the codes managed by the ESO they are intrinsic to how an organisation connects to, operates with and is charged for use of the transmission system. Code change is slow and complex and requires reform to support and enable the industry to meet net zero rather than the current framework which struggles to deliver overall policy outcomes.
- Code Reform has been an on-going piece of work within government and Ofgem since 2019. Although delayed compared to the original timescales the ESO is fully supportive of the need for reform to the way the industry codes are changed and are sharing our thinking with Ofgem on this crucial topic.
- A consultation is expected from Ofgem and the Department in Winter 2023. We will continue to engage with our stakeholders to support development of proposals for reform and ensure we can meet expectation outlined in Ofgem's role guidance.

What is the current process?

The ESO is currently the code administrator for four codes:

1) Grid Code – details the technical requirements for connecting to and using the National Electricity Transmission System (NETS).
2) STC - defines the relationship between the transmission system owners and the system operator.
3) SQSS - sets out the criteria and methodology for planning and operating the National Electricity Transmission System (NETS).
4) CUSC – is the contractual framework for connecting to and using the National Electricity Transmission System (NETS).

The code change process uses an open governance approach meaning that any organisation who is a party to the particular code can raise a modification proposal, and in some cases external parties can raise change as well. Once formally raised, a modification proposal must go through the governance process which can take significant time (multiple years in some cases), which is not an efficient use of industry time. In addition, although some prioritisation is applied in some codes

The code change process currently entails the activities in the below table. Note that there are opportunities to flex the process for an "urgent modification, or self-governance if appropriate.

Stage	Industry Representation	Format	Input	Output
Panel	Independently elected industry members and some appointed parties (eg ESO, Consumer reps etc)	Monthly meeting (generally 4hours)	Governance session to agree the next stage of the process for each change and some ancillary business	Approval of modification proposal progression through the process
Workgroup	Interested organisations that are a party to the code or nominated by a party (this is broadly representative, but does differ slightly between codes).	Depends on the complexity of the modification. Ranges from 1hour session once, through to many multiple sessions lasting 4hours+ each	Challenge and review sessions from impacted parties ranging from developing analysis to outlining the impact of the change on different parties	Development of modification solutions, legal text and workgroup consultation
Consultation	Open to any interested party	1 x workgroup consultation during the workgroup process x 15days 1 x code administration consultation for at least 15days	Organisational impacts of a specific code modification	View of the impact of the change from across the industry
Decision	Ofgem	Decision document from Ofgem outlining the reasons behind their decision. Can include an impact assessment and take many months to complete	Consolidated process and governance documentation detailing the change, impact of the change	Approval of implementation, send back for further information or clarity, or rejection of implementation

Why are we looking at strategic code reform now?

Ofgem and the Department for Energy Security and Net Zero have been developing policy on Energy Code Reform since 2019[1]. The aim is to "ensure that the energy codes can respond to the significantly changing sector, enabling change to be delivered more efficiently and effectively in the interests of consumers, and to support the transition to net zero." This was borne out of findings from a CMA investigation[2] that "found the existing code governance framework resulted in adverse impacts on competition arising from code parties conflicting interests… and that there are limited incentives to deliver policy change in the interests of consumers."

Reforms have now been included in the Energy Security Bill to provide Ofgem with additional powers, setting out the intention to create Code Managers who will be responsible for the governance of the codes and setting out a framework to develop a new governance process. Note that Code Managers are different from the current set up of Code Administrators, as Code Managers will be responsible for strategic development and governance, taking on more responsibility than the current Code Administrators.

[1] https://www.ofgem.gov.uk/energy-policy-and-regulation/policy-and-regulatory-programmes/energy-code-reform

[2] https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf

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Ofgem and the Department have recently run a number of industry workshops, following on from a call for input in January 2023, and a consultation in 2019. A further consultation is likely to be released in winter 2023.

Why is it important?

Energy code reform is an important enabling step towards net zero. The current code change process is slow, cumbersome, inefficient and can be subject to influence from narrower commercial interests, hampering the progress towards strategic objectives including achieving net zero.

Current issues

- Cross code working - there is an increasing number of modifications that have an impact across the codes. This prolongs the modification process as the modification needs to go through multiple governance routes in order for a decision to be made.
- Speed - if a modification requires a Workgroup, on average in the last 2 years it takes over a year to progress through the relevant stages and be submitted to Ofgem for approval. Across the same period of time the average number of workgroups required has been 8. The average value however disguises the number of workgroups and time taken to progress more complex modifications. Some examples are CUSC modification CMP315/375 which has had 17 workgroups and Grid Code GC0117 that has had 18 workgroups and neither of these modifications has yet concluded. These are not outliers, there are other multiple modifications that have a similar number of workgroups.
- Complexity - for new entrants to the market, the codes and code change process is complex and difficult to understand and engage with in a meaningful way. There are multiple governance routes, urgency criteria and processes that differ across the codes.
- Competing objectives – across the industry, there are different objectives driving strategic change and each organisation's direction. This feeds through into the code process and makes managing change challenging for all concerned. This can lead to instances where multiple solutions are offered up, or progress is delayed due to lack of alignment across industry.
- Lack of overall strategic direction for each code - given that any party can present a proposed modification at any time, there is a distinct lack of control and ownership over the long-term strategic direction of each individual code. This is then compounded with the above point around different objectives driving the code process in different directions.
- Commerciality and risk incentivisation - organisations represented within code panels and workgroups will look to remove any commercial disadvantage or legal risk from code development. While understandable, this can increase the complexity of solutions and the time that it takes to achieve them, while not necessarily achieving the best outcome for consumers.
- Lack of agility in governance - there is a lack of flexibility within the current process which means industry is not able to engage proportionately to the proposals to ensure efficiency. Much time is spent on multiple consultations when in many modifications few responses are received outside of views already recorded within the workgroup report.

The code change process is absolutely integral to how the industry performs as it dictates the rules for how organisations connect to, pay for and interact with the network. A wrong decision on a code modification can mean higher consumer costs, the wrong incentives for organisations and ultimately mean missing net zero.

What are the next steps?

Ofgem and the Department have commented publicly that they expect to run a consultation in Winter 2023 on the next steps. There is no information on the content of this consultation.

ESO has been developing a workstream on detailing our thoughts on how Code Managers and a new governance process could work to better facilitate enabling net zero. Some of our initial thoughts are below:

- Ability for Code Managers to prioritise changes that will drive net zero.
- Ability for industry to understand the strategic direction of the code and raise changes related to this.
- Reduce timescales and need for unnecessary multiple consultations.
- Increase engagement across smaller parties who may be more impacted by changes to the code.