

ElectraLink

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Laura Nell
Code Governance Remedies,
Ofgem,
9 Millbank
London, SW1P 3GE

1 February 2017

Dear Laura,

ElectraLink response to Ofgem's initial consultation on implementing the Competition and Markets Authority's recommendations

ElectraLink welcomes the opportunity to comment on Ofgem's initial consultation on implementing the Competition and Markets Authority's (CMA's) recommendations in respect of industry code governance, published on 9 November 2016. We are responding in our role as code administrator and provider of the DTS service.

We are wholly supportive of Ofgem's initial proposals on implementing the CMA's code governance remedies, namely the efforts to open the administration and management of central industry codes and systems to full market competition. Our responses to the consultation questions are detailed within Appendix 1. The key points of our response are:

- We have seen first-hand that competitively procuring code administration services ensures that costs to the industry and consumers are minimised; whilst ensuring the focus is on customer satisfaction and service delivery.
- We believe the benefits of competition should be extended to all of the CACoP codes, including NGET administered codes.
- We support Ofgem's proposals to licence code administration and central system delivery functions and agree with Ofgem's assessment that additional systems delivery functions, including the Data Transfer Service (DTS), should not be in scope of a licensing regime.
- We believe that strong benefits can be derived from the DTS being included within Ofgem's strategic direction and participating in the consultative board, all under the governance of the DTS User Group.
- The delivery of code administration services is significantly different to the delivery of IT systems and services, and as such we believe that they should be subject to separate licencing arrangements for code administration and central system delivery functions. This differentiation should maximise the number of bidders for each set of licences and so help to ensure that the competitive pressures on any procurement exercise are maximised.
- When procuring we believe that it is important to ensure that the model adopted is impartial and independent of existing incumbent providers. This will ensure a fully competitive procurement is undertaken for all codes, and the benefits are maximised.
- Ofgem should ensure the new governance arrangements, and resultant requirements placed upon code managers, should not comprise code managers' ability to provide excellent and low cost services to industry parties.

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ElectraLink is the operator of the industry DTS¹. Our role and experience in the transfer of data between market participants, including for the operation of the electricity settlement system, has enabled us to provide valuable input into Ofgem's recent consultation on mandating Half Hourly settlement. ElectraLink anticipates data volume growth over the DTS, if all MPANs were to be settled on a half hourly basis, of 2779% and work has already commenced to enhance the scalability of the DTS to accommodate this additional traffic.

Over the last 12 years ElectraLink has also grown successfully a commercial code administration business winning a number of contracts, all under competitive procurement. Our contracts are on a fixed price basis for the core service. Our costs are communicated transparently to code Parties via an annual budget process which requires budget approval by all code Parties. We currently provide code administration services to the Supply Point Administration Agreement (SPAA), Distribution Connection Use of System Agreement (DCUSA) and Smart Metering Installation Code of Practice (SMICoP) as well as providing administrative services to the Community of Meter Asset Providers (CMAP) and facilitating the Distribution Charging Methodologies Forum (DCMF) on behalf of the Energy Network Agency (ENA). All of our commercial contracts stipulate clear performance standards and metrics.

To date, ElectraLink has played an important role in supporting industry to implement a number of CMA remedies. In October 2016, in our capacity as a central code administrator², ElectraLink set up and chaired an industry Working Group³ under the SPAA. This Working Group was tasked to review the CMA's gas tariff remedy and incorporate the CMA's Undertaking drafting into SPAA governance. Over a series of meetings, the Working Group developed a SPAA Change Proposal⁴ which has been accepted by industry, ready for Authority consent. ElectraLink has also helped facilitate industry discussions in regards to the Debt Assignment Protocol for both gas and electricity, enabling a number of SPAA and Master Registration Agreement (MRA) Change Proposals to be developed and implemented in accordance to Ofgem prescribed timescales to date.

ElectraLink's experience in delivering code governance services has shown us the important role that well managed industry codes play in ensuring the effective and efficient operation of a competitive energy market. Codes are subject to significant volumes of change either to reflect new or developed policy (such as the role out of smart meters), to support new technology (such as electric vehicles and smart grids) or to deliver improvements to existing arrangements (such as the movement towards half hourly settlement). These changes can have a significant impact on the costs faced by market participants, impacting competition; or the experience of the energy consumer. For this reason, we believe competitive procurement of code administration services is required to ensure cost effective and high standard services. ElectraLink has experienced first-hand the benefits that competitive procurement has on code delivery i.e. by providing a downward pressure on costs and ensuring that the focus of code delivery is on customer satisfaction to ensure contract retention. As a result, we encourage Ofgem to consider all codes in scope of CACoP including those delivered by NGET, should be in scope of Ofgem's proposals.

Whilst industry codes set out the rules and responsibilities for market operation there are complex IT systems behind these to deliver the arrangements. We believe Ofgem has correctly identified the core IT systems which should be in scope of new arrangements. Although Ofgem has highlighted that it is open to industry views on whether the DTS should be considered in scope, we believe its inclusion in licensing arrangements may unnecessarily stifle innovation of the service and even drive up industry costs. ElectraLink procures the DTS on behalf of the UK energy industry following OJEU procurement rules. We provide the service to industry on a cost recovery basis ensuring that all market participants have equal and cost effective access to market data. ElectraLink works with industry to drive innovation with the DTS service provider deriving benefits through cost reduction and service flexibility e.g. the introduction of gas market data flows in 2016 regulated under the DTS Agreement. One of Ofgem's major considerations for which codes and systems should be included in scope for licencing is value for money. ElectraLink has managed its costs, and those of the DTS service provider, to drive down the cost of the service to industry. In July 2016 ElectraLink reduced traffic charges by 15% following on from two consecutive reductions at the start of 2016 and 2015 of 15% and 10% respectively. DTS data volumes are increasing at a year on year rate of 21% and scalability of the service means that as volume increases the DTS unit charges for users decrease.

¹ <https://www.electralink.co.uk/data-transfer-service/overview/>

² ElectraLink was awarded the Supply Point Administration Agreement (SPAA) in 2004 and Distribution Connection Use of System Agreement (DCUSA) in 2006 following competitive procurement

³ The SPAA CP 16/347 Working Group

⁴ SPAA CP 16/347

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Whilst there are similarities between the code administration and central system delivery, we believe that there are also fundamental differences. In particular, we note that code administration is resource and operationally focused, dependant on the skills and experience of the people providing the service. Conversely, central system delivery functions are IT focused and so capital intensive, requiring technical system knowledge. Licensing these disparate services together as a single service may therefore limit the size of the market that is prepared to tender to deliver these services; and potentially restrict this to the incumbent service provider. We therefore believe that code administration and central system delivery services should be subject to separate licence requirements. A single procurement exercise could still be undertaken, with multiple, separate licences; and so ensure that synergies can be realised (where present); whilst also ensuring that the market for these services is maximised along with the competitive pressures.

We strongly believe that any competitive procurement of code administration services must be impartial and independent of current code administrators. This will help to ensure that there is no competitive advantage to incumbent providers and so help to ensure that the full benefits of competition are realised. To this end we believe that there is merit in Ofgem being involved in whichever procurement model is chosen to ensure that it is applied consistently across the codes and systems, and assessments are impartial and based on agreed assessment criteria rather than previous working relationships. This should also include strict confidentiality clauses to ensure commercially confidential information is protected. We also recognise that code Panels (or code bodies) have a critical role to play in supporting Ofgem in any licencing model due to experiencing first-hand what is required by a code administrator or delivery body to deliver a high standard day to day service. Therefore, we encourage Ofgem to further explore the role code Panels must play when to date they have largely been excluded from Ofgem's proposals.

The introduction of new governance arrangements by Ofgem will introduce a direct relationship between all code and system service providers and Ofgem for the first time. Although we are supportive of the licencing measures, we believe a balance must be maintained with code managers being both accountable to Ofgem and responsible for providing a low cost and high standard service to code parties. For instance, code managers should be granted necessary vires, including the ability to raise modifications, in order to drive Ofgem's strategic direction forward. We also believe codes themselves will have to change, including the introduction of a new objective focused on delivering consumer benefits. The introduction of a new objective is crucial to align the functions of the code manager to code parties in directing the development and modification of the design of the code.

ElectraLink is responding in its capacity as a provider of code administration services and the operator of the Data Transfer Service (DTS). As such the views expressed in this response are those of ElectraLink Ltd.

ElectraLink would be pleased to engage with Ofgem to discuss this response in greater detail. Should you require any further information please in the first instance contact Stefan Leedham, at stefan.leedham@electralink.co.uk; 07921 292162.

Yours sincerely,



Stuart Lacey
Chief Executive Officer, ElectraLink

List of enclosures:

- Appendix 1 – ElectraLink response to Ofgem's 'Industry Code Governance: Initial consultation on implementing the Competition and Markets Authority's recommendations'

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Appendix 1 – ElectraLink response to Ofgem’s ‘Industry Code Governance: Initial consultation on implementing the Competition and Markets Authority’s recommendations’

Chapter 2: Question 1: Do you agree that the codes and functions we have identified (i.e. the codes within the scope of the CACoP and their associated central system delivery functions) should be within scope of the new regime?

ElectraLink supports the approach taken by Ofgem for identifying the codes and central systems to be considered within the scope of the new regime. We believe that all of the 11 codes identified, which fall under the scope of the Code Administrator Code of Practice (CACoP), contain pivotal industry rules and processes that operate the GB energy market. Although each code may differ in its role to deliver large-scale strategic market reform, each code has a significant potential to materially impact consumers; either directly by impacting their experiences, or indirectly by impacting the wholesale markets and so the costs that they face. As such we believe all of these codes should be the main focus of reform by Ofgem. Notwithstanding our support for opening central codes and systems to competition, we still encourage Ofgem to undertake an end-to-end impact assessment of the cost benefits to industry for expanding the roles of code managers through licensing. This will provide assurance to code parties of the benefits of licencing when code parties will be impacted by changing arrangements (i.e. with the possibility of service disruption and increased code/system costs brought about with new contractual requirements and the running procurement exercises etc.)

We are also of the view that if the arrangements were extended to all codes, agreements and standards i.e. including those that do not fall under the scope of CACoP (Group 3), this would consume unnecessary resource from industry at a time of unprecedented market change. Therefore, for the other codes, agreements or standards that are not within the scope of CACoP but where contracts are in place to deliver the service, relevant industry parties (under Ofgem’s guidance) should consider tendering or market testing on a semi-regular basis (i.e. every 3 years + 2-year extension) to drive innovative and cost effective service delivery.

Chapter 2: Question 2: Are there any other codes or systems that should be within scope and if so please give your reasons?

ElectraLink understands that Ofgem is open to industry views on whether wider delivery functions such as the DTS should be considered within scope of new arrangements. Unlike the central system delivery functions categorised under Group 4, the DTS is not governed under a central industry code, rather the DTS is governed under the DTS Agreement with the data flows that the service transports defined under a number of other industry codes including the Balancing and Settlement Code (BSC), MRA and SPAA. The governance of the service is managed by industry through this agreement which defines the role of the Service Controller and the DTS User Group. The DTS User Group is a representative body of all DTS Users on a constituency basis with no preference given to any particular constituency. The governance arrangements of the DTS are overseen by Ofgem. In the event of a major failure of the DTS, which is likely to impact all data flows supported by the service, Ofgem has the option to take enforcement action against Distribution Businesses under the Electricity Distribution Stand Licence Condition (SLC) 37. The governance of the DTS is designed to ensure that the service is operated under the direction of its users, not the shareholders of ElectraLink. This model has successfully delivered technological transformation, innovation and cost reduction to the benefit of all DTS Users.

Over the prior five-year period the total annual cost of the DTS to industry, spread evenly as an average cost across all Users, has fallen by 43% (see Chart 1 below). The cost of the DTS is recovered from Users over the life of the regulatory cycle, recognising that annual short-term surpluses and shortfalls are balanced over the longer term to a cost-neutral position while avoiding volatility in charges to Users (see Chart 2 below).

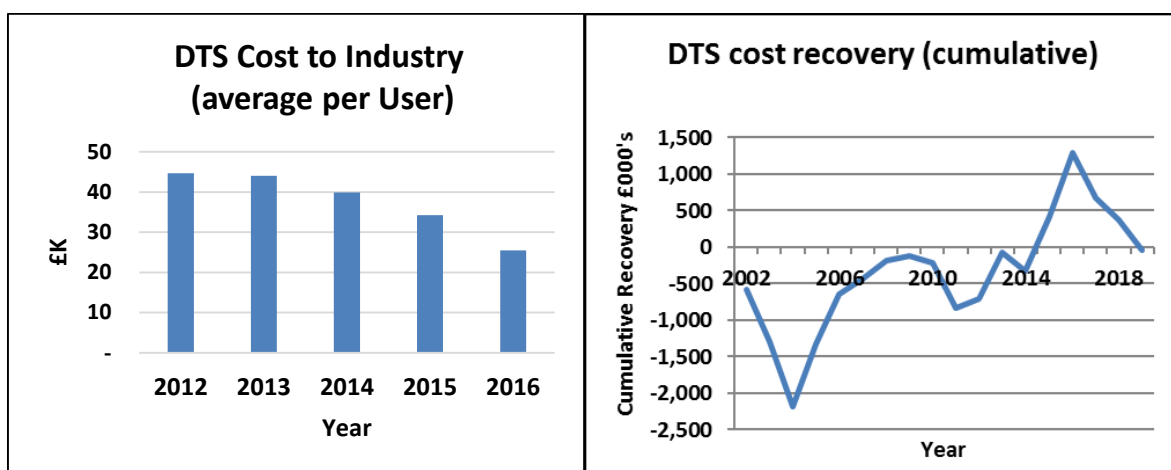


Chart 1: Annual DTS Cost (average per User)

Chart 2: DTS cost recovery (cumulative)

We would also like to highlight to Ofgem the challenges of the Theft Risk Assessment Service (TRAS) falling under the scope of a single licensed body when its governance is currently contained within two industry codes (DCUSA and SPAA). We recognise the possibility that one code manager could be appointed to undertake the role of two codes and that the code manager may appoint a third party to deliver the TRAS however, this may lead to complex legislative provisions being put in place to cover the TRAS obligations of the code manager over two codes. It is also worth noting that ElectraLink is separately contracted for its ongoing role in supporting the operation and governance of the TRAS, which is additional to the current contracts in place for administering the SPAA and DCUSA. As such we agree with Ofgem that greater accountability which will come from the introduction of a new licensing regime of code managers will provide added assurance to Ofgem in the efficient operation of TRAS without the need to follow a route of licensing a delivery body to undertake the end-to-end management of the service.

Chapter 2: Question 3: Are there any other factors you think we should consider when making this decision?

Firstly, although ElectraLink agrees with the approach taken by Ofgem to ascertain what code and systems should be considered within scope of the arrangements, we recommend Ofgem undertakes a comprehensive impact assessment of the cost benefits of a range of options. This will provide necessary confidence to industry who will be investing in the transformation of code governance arrangements. The impact assessment could for instance, look at the long term costs and benefits/consequences to industry (1) in maintaining existing arrangements, (2) in expanding the role/responsibilities of code administrators without licencing (through industry led market testing and tendering) or (3) full licencing of code managers with an Ofgem led competitive tender regime to award licences.

Finally, we encourage Ofgem to consider its approach for ensuring innovative delivery and economical costs of services is maintained in those codes or systems that are not considered within scope. ElectraLink sees great benefits in the industry using practices such as market testing but we also appreciate running such exercises can be costly and time consuming to industry. Accordingly, Ofgem may wish to consider developing guidance or criteria for reaching successful outputs of tender/ retender exercises where led or conducted by industry. The guidance will help ensure exercises are adopted pragmatically i.e. after a service has been in place for a number of consecutive years (for example 3+ years).

Chapter 3: Question 1: What are your views on our proposed approach of including the code manager and delivery body function in a single licence?

The requirement for maintaining industry codes is already contained within industry participant licences. Code administration can therefore already be argued as a licensable activity, albeit the approach is indirect with code administrators functioning independently from a licensed entity. We are therefore encouraged by Ofgem’s proposals to licence code manager and delivery body functions; however, we have concerns if a single licence approach was to be adopted. Code management and system delivery is intrinsically different, requiring diverse organisational expertise, experience and skill sets and bundling the functions together may hinder competition through restricting the types of organisations who wish to compete for an all-encompassing service.

In our experience, fundamentals of code administration revolve around the quality, professionalism and industry knowledge contained within a code delivery team. Customer satisfaction is therefore of utmost importance to code administrator organisations and where code parties are not satisfied with a service a contract may go out for tender. On the other hand, organisations who deliver central systems are driven by the ability to adapt to changing market conditions and providing innovative or transformational solutions. This is why, for instance, contracts for codes are for shorter timeframes than for delivering systems. In combining the two functions into a single licence this could stifle innovation of systems or lead to an increase in cost as investments are recovered more quickly, unless longer licences are awarded than the industry precedent of codes contracts for up to 3-5 years.

Chapter 3: Question 2: What are your views on strengthening the licence of NGET to include new code management requirements rather than holding a tender to identify an appropriate code manager?

The current licensing regime is structured in a way which may mean code administrators are owned by multiple licensees. This prevents a single organisation being directly accountable for service delivery. We acknowledge Ofgem's arguments for strengthening the licence of NGET however we strongly believe industry will benefit from the codes listed by Ofgem in Group 1 being subject to a single code manager licence in order that Ofgem can apply a common approach to monitor high standards of performance and take enforcement actions where necessary. A single approach for licensing, one which involves all central code and systems being open to tender, will increase transparency and reduce complexities in existing code arrangements.

Chapter 3: Question 3: What are your views on the merits and drawbacks of the four identified models for competitively licensing code management where applicable?

ElectraLink has assessed the pros and cons of each of the four models put forward by Ofgem and rather than selecting a preferred model, we believe Ofgem should follow a principle based approach to licensing. We believe the foundation of any licensing regime should not favour incumbent providers and should facilitate licences being awarded impartially and independently. We also recognise that there is benefit in including code Panels in the procurement exercise as they will be responsible for the management of the code administrator and delivery of services. As such we believe that a hybrid model may be beneficial, where the procurement is undertaken by Ofgem but with input from the existing code Panels.

We therefore encourage Ofgem to carefully consider the future role of code Panels who, largely, do not feature within this consultation. It is code Panels and code Parties who have the experience and understanding of what existing day to day code management comprises of thus such experiences should be considered in conjunction with Ofgem's vision for future roles and responsibilities of code managers.

Chapter 3: Question 4: What are your views regarding which model(s) may be appropriate for different codes, or types of codes?

In our view, a comprehensive licensing policy that is based on a consistent set of principles designed by Ofgem should be applied in awarding licences. This will ensure consistency in code governance management and should prevent Ofgem and industry participants playing differing roles from code to code. Although codes differ in size, scope and in the ability to impact customers, all central codes should be open to fair and equal term tenders to drive innovation and the economical costing services.

We also believe all code managers should be granted expanded vires to support Ofgem's visions i.e. through the ability to raise strategically important modifications. Alongside new tools being made available to code managers, codes themselves will have to change, including the introduction of a new objective focused on delivering consumer benefits. The introduction of a new objective is crucial to align the functions of the code manager to code Panels in directing the development and modification of the design of the code. We therefore encourage Ofgem to develop understanding of roles and responsibilities and would be pleased to share our ideas in this area.

Chapter 4: Question 1: Do you agree with the purpose of the strategic direction?

ElectraLink strongly supports the introduction of a strategic direction. We understand the strategic direction intends to set out expectations for the development of codes, aligned to code parties' objectives and Ofgem's focus on consumer interests. We believe its introduction will bring a number of welcomed benefits including code Panels and industry parties being able to make informed decisions around budgetary setting and in prioritising resourcing over the coming years.

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We also are encouraged by Ofgem's view that the strategic direction will inform the work to be carried out by the consultative board. By presenting the consultative board with a clear picture of future legislative or policy change, a holistic view of the market can inform code specific work plans which will help move away from how code administrators and code Panels can operate independently from one another. Nonetheless, it is worth highlighting that work is already being undertaken by existing code administrators in this areas. As an outcome of Ofgem's Code Governance Review Phase 3 (CGR3) a cross code work plan has been developed which considers priority reform projects identified by Ofgem within this consultation and any associated code modifications either already within code change processes or anticipated to be required over the next 5 years. This will act as a vital tool for the consultative board in understanding status of code change and we recommend code managers should be represented on the consultative board, as experts on code modification processes. The DTS is a critical dual fuel component of the retail market delivery model. Over the years the DTS has transformed and adapted to new policy and process. The continuing development of the DTS can be informed by Ofgem's strategic direction thereby ensuring the DTS continues to deliver innovative low cost solutions to meet the needs of the energy industry.

Chapter 4: Question 2: Do you have any views on how the strategic direction should be developed and implemented?

Ofgem's annual Forward Work Plan already provides useful insight into the industry's key priority projects and should therefore inform the initial development of the strategic direction. For the strategic direction to be of greatest use to industry, it should form a roadmap of how the sector can reach Ofgem's vision of the future energy market in the short, medium and long term.

As all market participants have a role in implementing market change we believe Ofgem should engage with industry throughout the setting process, ahead of the publishing of a draft strategic direction in autumn 2017.

Chapter 4: Question 3: How much detail do you consider should be included in the strategic direction?

We believe code Parties and, in some cases, code administrators are experts in the detail of required changes to codes. We would therefore encourage the strategic direction to focus on required outcomes of high-level policy decisions and leave industry and code managers to develop the specifics of consequential code change i.e. within cross code specific work plans.

ElectraLink also sees merit in Ofgem encompassing its longer term strategy within the direction i.e. beyond 3-5 years to aid longer term industry planning across industry participants.

Chapter 4: Question 4: Which specific projects do you consider should be included in the initial strategic direction?

ElectraLink agrees that the projects identified by Ofgem in its Forward Work Plan for 2016/17, provides a useful starting point for the strategic direction. We would also encourage joined up thinking by Ofgem between the setting of the strategic direction and the work that is being undertaken under the Ofgem 'Future Insights Programme'. Although the programme looks to explore the transformation of the energy system over forthcoming decades, we believe Ofgem's strategic direction is intrinsically connected to the evolution of the energy system and the issues the programme intends to explore.

Chapter 5: Question 1: What do you see as the core role and functions of the consultative board?

Very simply, codes are industry rule books that govern day to day operational processes and procedures of industry participants. For this reason, the industry should maintain a leading role in delivering small scale code change, which is facilitated by Ofgem and code managers. The consultative board should play a critical role in the delivery and overarching management of cross code change. The consultative board must take Ofgem's strategic direction and act as 'the eyes and ears' of industry to develop and maintain achievable code work plans that are mindful of the pressures and challenges industry participants and code managers are facing. It is, however, important that the activities of the consultative board dovetail with existing code change processes and the roles and responsibilities of industry players. For this reason, we believe the consultative board should only be attended by strategically minded individuals made up of code Panels, code managers, delivery body and Ofgem.

Chapter 6: Question 1: What are the main impacts of the proposed new arrangements on existing projects?

There are a number of industry reforms being undertaken in the industry which must be considered alongside implementing new code governance arrangements (i.e. Ofgem's Switching Programme, movement to HH settlement and

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mass smart meter roll out). Such industry projects should remain as Ofgem's priority to deliver due to the direct consumer benefits that they will put in place and which have also been heavily invested in to date by industry. Key milestones and the timelines of existing projects should be carefully scrutinised alongside understanding which central systems and codes will be consequently impacted, to ensure code modifications and system changes can be efficiently implemented before any competitive tender regime is introduced which could otherwise impact the priority of the code parties, code Panel or the code administrator.

Although we understand code consolidation is out of scope of Ofgem's proposed new code governance arrangements, our involvement to date in supporting the Ofgem Design Teams under the Switching Programme has highlighted the impacts the programme will have on existing governance arrangements i.e. the MRA and SPAA. One possible decision of the programme could be to create a new, dual fuel retail code to house switching arrangements in both the gas and electricity markets. As such, Ofgem may wish to consider the benefits of introducing new code manager licencing arrangements in accordance to the implementation of new codes brought about through existing projects.

Chapter 6: Question 2: Would Ofgem's enhanced powers over strategically important modification proposals mean that our Significant Code Review (SCR) powers will be obsolete, and will the new powers form an effective substitute? Please explain your reasoning.

In 2010 Ofgem introduced the Significant Code Review (SCR) process as a means to provide the regulator with a vehicle to step in to drive industry issues and change forward. Although the industry witnessed some incremental improvements, namely an overarching body to manage cross code change, the SCR has appeared at times to be a lengthy and cumbersome process.

We believe that Ofgem's proposals to licence code administrators will help to ensure that the code administrator should be responsible for delivering change to the codes and also engage with industry to develop the detailed solutions. From our experience of delivering the TRAS we understand that successful delivery of projects (i.e. on time and to budget) requires a careful mix between project management to drive through change and discussions; along with stakeholder engagement to ensure that the solution is developed to meet all industry requirements. Throughout this process we believe that there will be a role for Ofgem as project sponsor to provide guidance and direction on particular issues of strategic importance. In combination these reforms should help to ensure that change is delivered on time, multiple variants are avoided and overall customers will benefit.

At the same time, we also recognise that there may be rare circumstances where Ofgem will need to direct change. We are therefore supportive of the introduction of replacement provisional exceptional powers for Ofgem if the circumstances for such powers are clearly defined within legislation. Also where Ofgem maintains a high-level of industry involvement to ensure full impact assessments can be carried out by the parties impacted by any change.

We encourage Ofgem to provide further details on how the enhanced powers will be operated in practice i.e. how Ofgem's role will change if put in place to support the switching or mandatory half-hour programmes.

Chapter 6: Question 3: What are your views on staggering the implementation of competitive applications for licences?

To ensure the impacts to industry are minimised with implementing code manager licences, which may result in the transfer of services to new or existing organisations, we would strongly encourage Ofgem to adopt a staggered approach. The order in which code manager and delivery body licences should be implemented should be dependent on a number of critical factors, including:

- Existing strategically important industry programmes, their milestones and completion dates to prevent upheaval of services or systems at critically important stages;
- Existing contract terms and conditions between code Parties and code administrators'/service providers, including service renewal/end dates; and
- The opportunities existing industry programmes and projects may have for the creation of new industry codes i.e. the Switching Programme.

- End -