ESO Response to Ofgem's consultation on the future of local energy institutions and governance

Who we are

As the Electricity System Operator (ESO) for Great Britain, we are in a privileged position at the heart of the energy system, balancing electricity supply and demand second by second.

As the UK moves towards its 2050 net zero target, our mission is to drive the transformation to a fully decarbonised electricity system by 2035, one which is reliable, affordable, and fair for all. We play a central role in driving Great Britain's path to net zero and use our unique perspective and independent position to facilitate market-based solutions to the challenges posed by the trilemma.

Our transformation to a Future System Operator (FSO) is set to build on the ESO's position at the heart of the energy industry, acting as an enabler for greater industry collaboration and alignment. This will unlock value for current and future consumers through more effective strategic planning, management, and coordination across the whole energy system.

About this response

This response provides a summary view of our proposals relating to Ofgem's consultation on the future of local energy institutions and governance and is in addition to the points made in the covering letter. Detailed replies to the specific consultation questions asked can be found in Appendix 1. We look forward to engaging with you further as these proposals develop. In the interim, should you require further information on any of the points raised in our response please contact us. Our response is not confidential.

Our overall views on the proposals:

The scale of change needed to deliver a decarbonised energy system, demands urgent and collaborative action. This action includes a need for a shared, industry-wide vision of what is required both in terms of networks and markets to deliver net zero. We believe Ofgem's proposed governance reforms are a key element of this change and strongly support the consultation's conclusions and recommendations.

The creation of Regional System Planner (RSP) and market facilitator roles presents an unrivalled opportunity to accelerate GB's transition to net zero. The FSO is the primary candidate for these critical roles given its national presence, expertise and impartial and independent role within the sector. We recognise that our existing skills and capabilities will need to grow to successfully fulfil these roles.

It is vital that the needs of consumers and local communities are considered in the development of these roles. They need to work for all parts of GB and leverage the democratic mandates (i.e., the aims and needs) of the regions – particularly for the RSP role.

These new entities of RSP and market facilitator also need to complement existing roles and responsibilities within the industry. Both the market facilitator and RSP can help accelerate the growth of flexibility markets and the decarbonisation of the sector. To that end, it is important that the roles and responsibilities of all stakeholders are clearly defined and understood to inform RIIO-ED3 and other strategic developments.

We understand and support the need to thoroughly assess the costs and benefits of Ofgem's proposals for local energy institutions and governance reform via its proposed Impact Assessment. However, we believe the case for change to be sufficiently strong that the counterfactuals examined as part of this assessment should focus on a comparison of options for implementation (rather than seeking to quantify the change case against the status quo and other in-flight policy developments), for example by examining the appropriate model in terms of depth and sizing for the proposed RSP role.

We also agree with the recognition of the interactions with other areas of policy reform. In particular we would like to highlight the close relationship between the RSP role and Ofgem's consultation on frameworks for future systems and network regulation (FSNR) in relation to accelerating investment planning processes[1]. It is

[1] Consultation on frameworks for future systems and network regulation: enabling an energy system for the future | Ofgem

important that the current programme of reforms is appropriately co-ordinated, ensuring a holistic outcome that will promote certainty and clarity on the pathway to net zero.

Below we provide further context on our specific views on the proposed RSP and market facilitator roles along with our thoughts on the proposed treatment of real time operations.

Our views on the proposed governance reform: energy system planning

There is a clear gap in the current industry structure for an independent organisation that can look holistically across the whole energy system to help local and regional stakeholders, as well as government, achieve net zero aspirations. We see 'local' stakeholders in this context as dealing with individual local groups, such as local authorities or community groups. We view 'regional' as a broader area which brings together wider groups of stakeholders. We believe that the RSP model can fulfil this critical need for stakeholders. In fact, we believe the RSP will be essential in addressing current inefficiencies associated with not taking a whole energy system view[2] and supporting GB consumers and communities in accelerating their journey to net zero at lowest cost.

It is critical that the RSP model is built with and for local and regional stakeholder needs. Their support and buy-in in developing the model will be integral to its success. The RSP should have a regional presence with physical locations to build and maintain close relationships with local and regional stakeholders. Regional engagement is likely to be structured around investment planning processes, advisory functions for governmental organisations and fielding stakeholder enquiries. We would engage through a phased process working with initially with regional stakeholders, and exploring specific issues as required with other stakeholder groups to ensure democratic accountability.

A successful RSP can help to deliver optimum decisions through the investment planning process faster than current mechanisms, by improved clarity and cross-cutting expertise, and unlocking best practices that are currently developed in silos across GB. To do this, the RSP will need to connect democratic mandates to the national strategy, ultimately ensuring that net zero is developed in a way that works for all. We see the RSP working alongside regional and local stakeholders to enhance and deliver for the regions the activities and developments currently undertaken at transmission level, such as the ESO's Central Strategic Network Plan (CSNP). The clarity and consistency provided via an independent, impartial body (the FSO), means investment planning decisions can be expedited to accelerate GB's course to net zero.

The FSO is the only entity able to undertake this role. There are a number of key attributes that lead us to this conclusion:

- As a **body with national reach and applicable expertise** in energy strategy and planning, the FSO will be able to ensure there are consistent investment planning processes and assumptions across GB network organisations, and is best placed to coordinate and align local and regional strategies with overall national requirements. This will also encourage best practice sharing between regions and support for regions with limited resources.
- The FSO is being set-up as a **neutral independent organisation** and therefore can reflect consumer impacts and democratic mandates, rather than being biased towards a particular technological or sector-based solution.
- The FSO has the **ability to analyse data and undertake scenario planning, and develop strategic energy plans**. Our critical roles in areas such as Future Energy Scenarios (FES), Network Options Assessment (NOA), Holistic Network Design (HND) and Accelerated Strategic Transmission Investment (ASTI) processes demonstrate both the benefit of an independent entity accelerating network investments and also our experience in developing and delivering such processes.
- As the ESO, we have **established relationships with key stakeholders** across a range of energy issues and recognise the importance of continuing to develop these in the RSP role. However, we recognise the need for us to work with, and learn from, existing organisations who work more closely

[2] As cited in Ofgem's consultation document, Energy Systems Catapult state that coordinated local energy system planning discounted cost savings (compared to an uncoordinated approach) could total £252 bn between 2025 and 2050.

with local stakeholders, including community groups and democratic institutions. This will ensure the RSP can expand and build on these relationships at a regional level.

We understand the importance of ensuring that the RSP model builds on and complements existing activities currently undertaken. Once established, the RSP will continue to hone skills and capabilities, increasing trust with regional and local stakeholders as the role develops.

We wish to work closely with local and regional stakeholders to understand how we can establish the RSP at speed in time to influence RIIO-ED3 (2028) and without any perception of a hiatus in our transition to net zero.

We believe the RSP role complements other FSO activities, including the proposed advisory role in which it is intended that the FSO will have a statutory duty to provide expert advice, analysis and information to Ofgem and government to inform policy decisions. This synergy could help to leverage skills, systems, and the legislative framework to help accelerate the introduction of the RSP within the FSO.

The expectation that the FSO will take on a whole energy system role, which will be aided by the RSP approach, is also noted in the response to the FSO consultation from BEIS (as was) and Ofgem *'as a newly independent body, the FSO will take an increasingly significant role in shaping the energy system and driving forward competition. The FSO should be taking a whole system approach while doing so, which means considering the interactions across electricity, gas and other emerging markets (such as hydrogen and Carbon Capture, Usage and Storage), both on and offshore, and between transmission and distribution systems. This was endorsed and considered a priority by consultation respondents.'*

Our views on the proposed governance reform: market facilitation of flexible resources

Significant growth in distributed flexibility is critical to balance our decarbonising and decentralising electricity system. However, providers of facilitated flexibility face significant challenges to developing secure business models including a lack of sector vision, barriers to entry and an unstable market environment. Specifically, their participation at the local level has been held back by a lack of standardisation and alignment of approach. We acknowledge that Open Networks has made some progress in achieving alignment among the network companies, and has reflected stakeholder feedback in its new targets in its 2023 plan. Whilst this is moving in the right direction, progress needs to be accelerated to achieve the required growth, particularly in distributed flexibility.

We believe that a single, neutral entity should take on the central market facilitation role. A single point of accountability is needed to drive alignment at pace across transmission and distribution flexibility markets, to achieve coherency with wider markets, and to remove the barriers to scalability of markets in a timely manner. Whilst standardisation of local markets will contribute towards the business case of distributed flexibility, this alone will not unlock the level of distributed flexibility required to meet our net zero targets. The market facilitator must also have a role in facilitating wider market and policy alignment.

We believe that the FSO is the only body to take on this role for the following reasons:

- The ESO has **many years of experience in designing and operating flexibility markets** that are coherent with one another as well as with wider markets. We use our market design framework to constantly reform our market designs, adapting to changing system needs as well as to an evolving landscape of flexibility providers.
- As an ESO **we work in close collaboration with industry**, and our long-term reform strategy is published annually in our Markets Roadmap.
- The FSO is being set up with new **'whole energy system' responsibilities.** This, coupled with our experience in strategic market reform, makes us a natural fit for the role of market facilitator.

We recommend that Ofgem delivers the proposed changes in a timely fashion to avoid any hiatus in market development and alignment. It will be crucial to implement appropriate and clear interim governance arrangements, i.e. between now and Day 1 of the market facilitator, to ensure markets continue to develop and align at pace.

To ensure the right outcomes, and to avoid the same issues that have been experienced to date reoccurring, it will be critical that the governance framework is established correctly and that the market facilitator is given the appropriate powers to ensure all parties comply with the framework. Otherwise, progress could be easily stalled,

or sub-optimal outcomes achieved, if a minority of parties were not to engage properly. It will be important that Ofgem provides the appropriate support for this new framework.

We broadly agree with the proposed allocation of roles as it is important that one entity is accountable for each role, but there will of course need to be significant input from all parties into each stage of the process, e.g. in product design and managing market rules. Whilst the market facilitator should be ultimately accountable, DNO input into the design of these products and rules will be critical if they are to be fit for purpose and implementable on the distribution networks and in DNO control rooms.

DNOs should continue to have direct relationships with distributed energy resources (DER), consumers, and market participants. This is critical for the success of many parts of the market development and operation process, from sales and marketing through to operations, and feedback from these relationships will be important to drive continuous market development and innovation.

Our views on the proposed governance reform: real time operations

We agree with Ofgem's proposal that the DNOs retain accountability for real time operations. They have the expertise to deliver the continued reliability and safety of the distribution system. We recognise the need for close collaboration and data interchange with the DNOs to ensure actions taken across distribution and transmission networks are coordinated. We agree that effective operational coordination is a must-have rather than a 'nice to have'.

Real-time operations rely upon, and are affected by, market outcomes to maintain a safe and secure network. We acknowledge therefore, the critical role of a neutral market facilitator, to enable the inclusion of increasing numbers of participants, including distributed flexibility and demand side response providers. A regional whole energy system strategic plan would also be a key input for market participants' decisions, giving markets clear signals on system requirements and where flexibility will be of most value.

Appendix 1 – Consultation Question Responses

Q1. Do you agree with our proposal to introduce Regional System Planners as described, who would be accountable for regional energy system planning activities? If not, why not?

We believe that the RSP model is a fundamental requirement to transition GB to net zero quickly and at lowest cost to the consumer, filling an existing gap to achieve whole energy system outcomes. Without RSPs, existing inefficiencies associated with not taking a whole energy system view in energy planning will deepen as we transition towards the 2035 decarbonised electricity system and 2050 net zero GB targets. To that end, we strongly support Ofgem's proposal.

The RSP needs to give a voice to local communities, promoting democratic mandates and buy-in from local and regional stakeholders. It needs to act as a link between local and regional entities ensuring that whole energy system outcomes can be achieved and optimised and provide a bridge between local plans and the national strategy for decarbonisation. The RSP can help society efficiently plan and deliver the investments needed to move to a decarbonised sector. It can also ensure that best practice techniques are shared, thereby accelerating decarbonisation whilst also stimulating regional investment.

In the table below we have considered the qualitative value the RSP role could bring to the energy system, centred around Ofgem's strategic planning activities from the consultation document:

Ofgem RSP activity area	Value each activity brings
Develop and own the critical planning assumptions	• Enables efficient whole energy system decarbonisation plan proposals. • Provides a consistent approach and optimisation at a regional level for decarbonisation across GB.
Coordinate, facilitate and ensure effective local stakeholder participation	• Allows local views to be understood and considered. • Bridges local requirements with national strategy through neutral facilitation. • Independent facilitator who can bring local stakeholders together to make change happen.
Develop and own a regional whole energy system strategic plan that is coherent with national and local net zero ambitions and energy security priorities	• Facilitates a longer-term strategic view of regional decarbonisation; informs future requirements such as policy development and supply chain impacts. • Provides stability for net zero transition; minimising disruption for communities and futureproofing arrangements.
Provide independent technical analysis and advice to support decision making	• Minimises cost of transition to net zero caused by inefficient funding of individual requirements. • Facilitates sharing of best practice and innovative pathways to decarbonisation. • Provision of tools, data and framework to accelerate decarbonisation transition. • Accelerates process for investment decisions through application of cross-vector expertise and best practice plus a stronger overarching direction.

Q2. What are your views on the detailed design choice considerations described?

The RSP needs to be independent, impartial and able to look cross vector, joining up and aligning regional and national plans. These characteristics will ensure the RSP has the necessary credibility when creating strategic regional plans that effectively and impartially weigh up all the components and options associated with the whole energy system. The RSP also needs to have foresight of longer-term planning (i.e. the net zero by 2050 target) in its remit, looking beyond regulatory cycles. In summary, we believe that the detailed design choice considerations set out in Ofgem's consultation document are informed and reasonable.

In terms of high-level structural design, we believe there are two key elements:

1. **A central team undertaking planning and analytical functions**

This team will build on existing ESO capabilities to form coordinated and cross-vector strategic plans, planning assumptions and scenarios. We see that its primary responsibilities would be to develop and own planning assumptions, co-ordinating the overall process of strategic plan development, and providing technical analysis and support in decision making.

An annual RSP process would be coordinated with the FSO's Central Strategic Network Plans (CSNP) to ensure a joined-up approach between national and regional plans with timescales harmonised in line with the CSNP process. Once the RSP has set the direction through planning assumptions and the appropriate context for regional plans, annual replanning cycles would be less onerous delivering much needed stability and allowing progressive optimisation and efficiencies.

Leveraging the strategic regional plans, the central team could also help to accelerate investment decisions similar to the ESO's HND process for Offshore networks at transmission level. This would be through acceleration of the regulatory approvals process (and therefore investment) if a 'plan and deliver' regulatory archetype is introduced, which involves a central planner defining the needs case, what will be delivered and when.

2. **Regional planning hubs to engage with local and regional stakeholders and develop regional strategic plans**

The RSP will need regional planning hubs to be both the vehicle to engage with local and regional stakeholders and also to develop the specific regional strategic plans working closely and drawing on information from the central team.

Strategic plans would detail the broad infrastructure needs for a region that the RSP has assessed as optimal, having engaged and worked with local communities and organisations throughout the process. This would also provide certainty to regional parties to take the relevant elements forwards into their own revised detailed plans for specific investments down to street level.

Regional engagement would encompass non-energy stakeholders including democratic organisations and network organisations, to ensure proactive participation and accountability. Whilst a region could cover a wider geography, engagement leads could focus on smaller areas enabling the development of key relationships. RSP stakeholder engagement would likely involve a range of activities including:

- Investment planning processes: an annual process, encouraging challenge, review and acceptance of strategic regional plans which would feed into the development of regional strategies and their alignment with network operator plans, building a better understanding of economic, environmental and community impacts.
- Advisory functions: seeking input to inform FSO and government policy direction and decisions.
- Stakeholder enquiries: engagement at the request of stakeholders and facilitating the sharing of best practice techniques and processes across GB, which will improve overall engagement
- Where decisions are particularly contentious, we are exploring with regional stakeholders how democratic accountability and buy-in can be supported through different means such as participatory budgeting (as has been used in Scotland drawing on wider best practice in Rio de Janeiro) and Citizens Assemblies which have been used to great effect in infrastructure decision making in New York City for example.

When developing detailed design recommendations it will be important to work with existing actors who already engage with local authorities and devolved Governments . Through taking on the additional skills and capabilities to run studies of DNO and Gas Distribution Network (GDN) planning models, as well as carrying out the required modelling and analysis to challenge these, the RSP would be able to assure consumer value in the validation of these plans.

We recognise that Ofgem's role will remain vital in providing regulatory oversight of existing and new activities in the regional sphere. Clarity on the accountabilities for investment planning will be critical to understand from the outset. We also recognise the interlinkages to the ongoing policy decisions and consultations, such as the 'Future Systems and Network Regulation' consultation. This is particularly pertinent with regards to

understanding the right level of access to data and stakeholders to ensure that informed investment decisions are taken.

We welcome working with Ofgem and other industry stakeholders to gain an understanding of the timeline for delivery options, recognising the suggested pace outlined in the consultation (in time to influence RIIO-ED3 – 2028), and noting the need for further work on the detailed design as part of the planned impact assessment. We are aware of industry concerns regarding the impact of a potential hiatus whilst the RSP is established, and subsequently understand the importance of transparency and certainty in the next steps after a final decision has been made by Ofgem.

Q3. Do you have views on the appropriate regional boundaries for the RSP?

It is critical that the RSP enables and empowers local and regional stakeholders in the transition to net zero. Therefore, RSP regions must be appropriately sized to meet their needs. Consideration should focus on numerous factors, including proximity to hydrogen networks, local electric vehicle (EV) and heat pump uptake rates, rural to urban ratio and demographics. We would also highlight the political appetite that different regions will have to accelerate achieving net zero and the different conclusions and priorities that they may propose. Whichever regional boundaries are identified need to be fair and equitable, with the ability to take into consideration the views of consumers and all relevant parties to achieve net zero, and to be cognisant of the number of regional RSP teams that will result.

The appropriate size of regional boundaries should be further considered during the detailed design phase and impact assessment of the RSP proposal. After this has been determined an in depth understanding of the optimum RSP organisational model in terms of number of offices, number of full-time employees (FTEs), costs and capabilities is a necessary part of addressing the structural arrangements, including regional boundaries.

Q4. Do you agree that the FSO has the characteristics to deliver the RSPs role? If not, what alternative entities would be suitable?

We believe that the FSO is the only credible candidate to deliver the RSP role. In the preface to our response we have articulated why we believe this is the case. In summary the FSO, building on the position of the ESO, will be a national independent entity with a remit, expertise and experience to look strategically across energy vectors. The FSO is already being established to undertake a number of roles, such as Advisory, which can be leveraged to facilitate rapid deployment of the RSP.

Whilst the ESO has deep stakeholder relationships and expertise in the energy sector already, we recognise that the RSP role would require the FSO to significantly grow this expertise and develop new relationships with local and regional entities. We are keen to learn from existing organisations that perform similar roles and want to hear from local stakeholders to understand how the RSP needs to work for them, and how we can help them achieve their goals.

Q5. Do you agree with our proposal for a single, neutral expert entity to take on a central market facilitation role? If not, why not?

Yes, we agree with the proposal to create a single, neutral market facilitator.

We continue to hear from distributed and consumer energy resources (including demand-side response (DSR)) that their business case is challenging because of the fragmentation of market processes, designs and signals. The business case for distributed flexibility projects relies on the stacking of multiple revenue streams (across system operator (SO) services, as well as wholesale, retail and network signals). However, DSO markets across regions are not standardised, and there exist conflicts or incoherencies with ESO markets and wider market signals. This increases complexity for providers, both in terms of making decisions around which markets to enter, but also logistically in the cumbersome processes they need to go through to access the different markets. It means that markets revenues cannot easily be stacked. The lack of a clear industry-wide strategy and roadmap means that it is difficult for developers to create a clear business case to attract investment as scale, leading to underinvestment or higher cost of capital for distributed flexibility projects. It is

important we address these issues urgently, to unlock the significant level of distributed flexibility required to meet the net zero challenge.

While Open Networks has played a role in achieving some coordination over the past few years, this is not progressing at the pace required to achieve our net zero targets. This is evidenced by the lack of full standardisation of DSO services, participation processes or contracts, and a lack of progress to resolve stacking issues. We believe it has been and will be difficult for Open Networks to set ambitious, long-term plans and hold all SOs accountable to deliver due to its lack of mandate and decision-making authority.

Given the urgency of the challenge, we believe there is a case for change to create a single entity, with the right capabilities, incentives and mandate, is assigned the role to facilitate market coordination across ESO and DSO services.

Q6. Do you agree with the allocation of roles and responsibilities set out in Table 2? If not, why not?

Our assumption is that Table 2 refers to the development and operation of flexibility markets at distribution level only. However, it is important to note that there is significant potential value available from coordination and standardisation of markets and products across transmission and distribution, as well as from ensuring coherency with wider market designs and reforms.

We broadly agree with the allocation of roles, with regards to the accountability of activities. However, while we understand that Table 2 is not proposing sole responsibility of certain roles to one actor, we want to emphasise the importance of giving both the market facilitator and local entities (DNOs, local authorities etc) appropriate responsibilities in the process of developing and operating flexibility markets across transmission and distribution.

For example, we outline the importance of DNO involvement in the following activities:

- Product development & standardisation: while we agree that accountability should sit with the market facilitator, it alone cannot design and standardise products without significant input from the DNOs. We see the design of ESO markets as analogous: when we design ESO markets or products, we require significant input from ESO National Control engineers to ensure the products a) meet the needs of the control room to securely operate the transmission system and b) can be implemented in the control room IT environment. The same can be said for development and standardisation of distribution market products – the input of the relevant DNO engineering and IT experts will be critical.
- Managing market rules: when creating market rules, it is important the market facilitator is guided by a robust framework that maximises whole electricity system and consumer benefits. This framework can also be used to communicate and justify decisions made in a transparent manner. The ESO has developed a market design framework for just this purpose, and this can be adapted for a whole electricity system purpose. The DNOs would need to contribute to the ongoing development of this new framework to ensure that product designs and market rules are created fairly.
- Engaging with market participants: this is a very broad term and should be further broken down with responsibilities clearly set out. There are multiple touchpoints with market participants throughout the market development, design and operation journey, and the engagement role will be best suited to different organisations at different stages.
    - We believe the market facilitator should have a strategic role in convening distributed flexibility providers to identify challenges, resolve market issues and advocate for wider market and policy changes. However, there are other engagement activities such as the marketing of DNO products to local providers, contracting and customer support that should remain with the DNOs that will dispatch these services directly.
    - DNOs will need to maintain strong relationships with local parties – it would not be feasible for a central market facilitator to take on accountability for this engagement.

We recommend that each activity in Table 2 is broken down to the next level of detail, and a full RACI is created for each activity and sub-activity.

Q7. Are there other activities that are not listed in Table 2 that should be allocated to the market facilitator or other actors?

While we agree that the primary purpose of the market facilitator is to deliver alignment of SO markets across transmission and distribution, this alone is not sufficient to achieve the market environment required for distributed flexibility to develop at scale.

Market participants face a broader coordination challenge across wholesale, retail and network charging signals, in addition to ESO and DSO markets, which prevents them from developing scalable business cases for distributed flexibility. To facilitate the level of distributed level flexibility required for net zero, it is important that the market facilitator will consider DSO/ESO market design and coordination in the context of wider market and policy development, and influence reforms across the landscape where appropriate.

We would also like to emphasise on the importance of autonomy to enable the market facilitator to unlock greater value for consumers. It is important that the governance structure is set up in a way that ensures Market Facilitator is empowered to take action to remove any conflict or barriers during the process and the market players cooperate in a consistent way. Clarity and accountability in the governance structure will be a necessary step to ensure there is equity in engagement. We recommend using the learning from code modifications process and the ongoing energy code reform regarding allocation of responsibilities and stakeholders engagement. We are currently working on our response and believe the response can be valuable to this consultation as well.

Q8. What are your views on our options for allocating the market facilitator role?

We believe that FSO would be the only suitable organisation that will be able to successfully deliver the market facilitator role.

The market facilitator must have the following characteristics to be successful in delivering the system and consumer benefits set out in this consultation:

1. **Having consumer interest at heart.** The market facilitator must have delivering consumer benefits as its main objective in the way they design and coordinate SO services. This objective is also a key driver for the establishment and design of the FSO, which will act as a trusted advisor to government to deliver consumer benefits.
2. **Independence in decision-making.** It is important that the market facilitator does not favour individual system operators, and makes decisions in the best interests of the whole GB system and all consumers. We recognise the concerns of neutrality in market design and market rules across transmission and distribution levels given ESO's current capabilities and responsibilities. It is vital this concern is fully addressed through the transition from the ESO to the FSO. This include the way the FSO (and specifically the market facilitator function) is regulated and incentivised to ensure it prioritises whole electricity system benefits instead of just transmission level needs. The FSO will also need to grow their capabilities and understanding of distributional level issues to ensure DSO needs can be appropriated accounted for. In addition, a clear and transparent market design framework, with a 'coherency' principle will enable the FSO to act as impartial decision maker as market facilitator.
3. **The ability to plan strategically and optimise for overall system benefits.** For the market facilitator to design effective services and rules that will deliver the best overall outcome, it needs to have the strategic understanding of the whole energy systems, including transmission, distribution as well as the wider market, policy and regulation frameworks. The FSO's new responsibilities goes beyond this to whole energy system optimisation, not only across transmission and distribution but across vectors such as gas and hydrogen. The FSO will have sufficient capabilities and frameworks to take on the responsibility of ensuring transmission and distribution coordination.
4. **An understanding of how to design and coordinate multiple services to efficiently manage the energy system.** To ensure the market facilitator can add value as soon as possible, we must build on existing capabilities and expertise in market design and coordination. Over many years, the ESO has designed and operated competitive and liquid markets for balancing and ancillary services. We are

also familiar with and experienced in coordinating market design and reforms across multiple ancillary services. The market facilitator will be able to draw on such expertise from within the organisation.

5. **An understanding of different types of flexibility providers, and how to incentivise and facilitate them to participate in markets.** Through Power Responsive and many of our markets, the ESO is familiar with DER and demand side flexibility solutions. ESO markets, particularly frequency response, remain the main revenue streams for distributed batteries, while larger DSR providers have been participating in short term operating reserve (STOR) for many years. Our recent Demand Flexibility Service is accessing residential demand flexibility directly. We recognise there are still gaps in market access for distributed flexibility, this is why we are developing a Distributed Flexibility Strategy to set out our actions to facilitate the growth of distributed flexibility.

Q9. Are there other options for allocating the market facilitator role you think we should consider? If so, what advantages do they offer relative the options presented?

As explained in our response to Q8, we strongly believe FSO is the only suitable option for the role of market facilitator.

We recognise that the establishment of the market facilitator may take some time, which could result in a hiatus in DSO markets development and ESO/DSO market coordination if not carefully managed. It is therefore important that Ofgem and the selected market facilitator put measures in place to ensure the delivery of interim deliverables until the regulatory framework can be put in place.

Q10. Do you agree that DNOs should retain responsibility for real-time operations? If not, why not?

Yes, we agree that DNOs should retain responsibility for real time operations. It essential that there is clarity on the party responsible for operating distribution networks. The DNOs have the appropriate skills, knowledge and experience to competently undertake this role and should continue to do so.

However, we wish to emphasise continued enhancement in the cooperation, collaboration and standardisation between DSOs and with the ESO to ensure a secure transition to a smart, flexible energy system that reaches the government's 2035 decarbonisation target for the electricity system. As described in the consultation document, the proposals for regional system planner and market facilitator roles also interact with real time operations, it is therefore critical that development of these new roles is co-ordinated with operational requirements, processes and systems.

Q11. What is your view on our proposed approach to the undertaking of an impact assessment as outlined in Appendix 1?

We support Ofgem's overall approach to its impact assessment. Framing this in the context of the benefits, costs and the counterfactual seem reasonable. However we emphasise that the impact assessment needs to be proportionate, given the strength of the current case for change and the timeframe that may be required to undertake a full evidence-based review.

To that end, we do have concerns over the need to establish a counterfactual as a baseline. We believe that the cases for market facilitator and RSP roles are compelling and are met with general industry support. We would suggest an impact assessment focusing on the different options for implementing these roles may be of greater benefit. Framing this in the context of the benefits, costs and the counterfactual seems reasonable.

We would like to continue working with Ofgem and industry throughout the impact assessment process to provide any further detail that may be necessary and to continue to assess the available options.

Q12. What is your view on the most appropriate measure of benefits against the counterfactual?

The benefits associated with Ofgem's reform packages fundamentally address inefficiencies and gaps in the energy system and the associated risks that comes with this to achieving net zero. However, we highlight the difficulty in providing the most appropriate counterfactual(s) to understand the impacts of such benefits, and as such refer to our response to Q11.

Ofgem's benefits listed in the consultation seem appropriate to measure the case associated with RSP and market facilitator proposals. Further clarity could be provided in some of those listed, along with an appreciation of areas which have more of an impact on one role area over another, as highlighted below:

Benefit listed by Ofgem	Points for Ofgem's consideration
Flexibility provision	Further clarity on this could be provided; if this is the amount of flexibility that enters into transmission and distribution markets this can be measured. Whilst inevitably this benefit will focus on the market facilitator role, the role of the RSP in providing clarity on investment decisions will be an important consideration here.
Data quality improvements	Standardisation will be key to this benefit which will then enable decision making at a faster pace. This benefit will be difficult to measure quantitatively against the counterfactual proposed by Ofgem.
Improved market participation of flexible resources	This benefit may be overly similar to that of flexibility provision. We suggest measuring the cost of entry to market.
Deferred reinforcement/decarbonisation synergies	Whilst we agree that the percentage of deferred reinforcement is a sensible benefit, again this may be difficult to understand in relation to Ofgem's proposed counterfactual. Decarbonisation synergies needs further clarification.
Transparency of decision making	Clear roles and responsibilities are also heavily linked to this benefit.
Increased stakeholder confidence	Stakeholder feedback, as a measure of the benefits included in Ofgem's impact assessment, will be integral to the success of the RSP and market facilitator.
Whole system benefits	Clarity on what is meant by whole system is needed; this will also help in finding appropriate measures. In our Future Energy Scenarios (FES), we define this as: *A collective term that is used to cover all interdependent systems associated with provision of energy and the emission of greenhouse gases; including systems such as transport, water, waste, hydrogen.*

Other benefits that could be considered are:

- Increase in pace of decarbonisation
- Increased consumer engagement
- Ensuring a fair and equitable energy system transition
- Provision of solutions that cater to the needs of local communities
- Addressing security of supply during the energy transition.
- Clarity on market signals and subsequent investor confidence.
- A forward view on the impact of supply chains.
- Facilitates alignment of local plans with regional strategies
- Ability to deliver consistent outputs and sharing of best practice
- Better overall choice of options for delivery enabling efficient investment decisions

In terms of quantitative benefits, there are various examples of the benefits bought by regional approaches; for example[3] , the West Midlands Combined Authority have said there could be a benefit of [4] to a regional approach over 30 years.

Q13. How should we attribute those benefits between the governance changes in the proposed option, and other changes required to achieve benefits? We particularly welcome analysis from bodies that have undertaken an assessment of benefits, specifically how those benefits might be attributed to different policy reforms that are required to achieve those benefits.

The calculation of the benefits for the regional system planners and market facilitators is very complex. Many policy reforms listed in Ofgem's consultation have interactions with these benefits to an extent. We note that other policy areas may also interact with the proposals; for the market facilitator, this includes:

- Market wide half-hourly settlement[5]
- The smart meter rollout[6]
- Retail market reform[7]
- The wider economy (energy prices, interest rates, supply chain costs)

From an RSP perspective interactions with the following policy developments should also be considered:

- Data best practice changes including open data proposals[8]
- Holistic Network Design[9]

Whilst we recognise the importance of being able to disentangle the benefits of such from wider policy reforms that are taking place (where possible) for the purposes of this impact assessment, it is critical that the development of these new roles considers and coordinates with inflight policy and upcoming policy decisions. For example, the market facilitator must consider any potential changes resulting from REMA. Reforms to the wholesale market, the balancing market (BM) or other operability markets would have a fundamental impact on transmission and distribution flexibility markets. The need to understand the interactions between markets, policies and regulation across the whole energy system strengthens the case for the FSO to take on the market facilitator and RSP roles.

Q14. What additional costs might arise from our governance proposals? We welcome views both on the activities that may arise and cause additional costs to be incurred, as well as the best way to estimate the size of the costs associated with those activities.

The costs associated with the governance proposals outlined in this consultation need to be considered in relation to other ongoing policy developments, e.g. there is very clear overlap between the RSP proposal and the future systems and network regulation consultation. Furthermore, clarity on the precise roles and structures for these new functions – for example the number of RSP offices - with be vital in understanding the costs that will arise.

[4] Coventry EIZ | Energy Capital (arcgis.com)

[5] Electricity settlement reform | Ofgem

[6] Smart Meter Rollout: Energy supplier Rollout Delivery Open Letter April 2023 | Ofgem

[7] Review of electricity market arrangements - GOV.UK (www.gov.uk)

[8] Energy data and digitalisation | Ofgem

[9] The Pathway to 2030 Holistic Network Design | ESO (nationalgrideso.com)

We believe that the following areas need to be considered in calculating the costs arising from the proposed governance proposals:

- Number of FTEs
- IT infrastructure (including cyber security requirements) and systems to support data and digitalisation that accompanies role developments
- Office locations for RSP regional presence

Q15. What additional costs may arise from sharing functions with several interacting organisations? We welcome views on set up cost, lost synergies, and implementation barriers.

It is important that the proposed new roles in this consultation complement rather than duplicate existing activities. However, there may be changes to the roles and activities of some existing actors as a result of these proposals and there will be areas of overlap, for example where the RSP needs to validate proposals for future investments received from network companies. These costs need to be considered and it is important that all parties have sufficient funding to realise the benefits of the proposed changes.

Given that both the market facilitator and RSP roles are new requirements, we would see lost synergies as being minimal. This is because there are currently no entities undertaking these roles so there are no synergies to be lost.

Implementation barriers need to include the maturity of relevant processes and capabilities within all affected organisations. The underlying legal and regulatory requirements should also be assessed to understand the changes needed and therefore the impact on the overall timeline to delivery.