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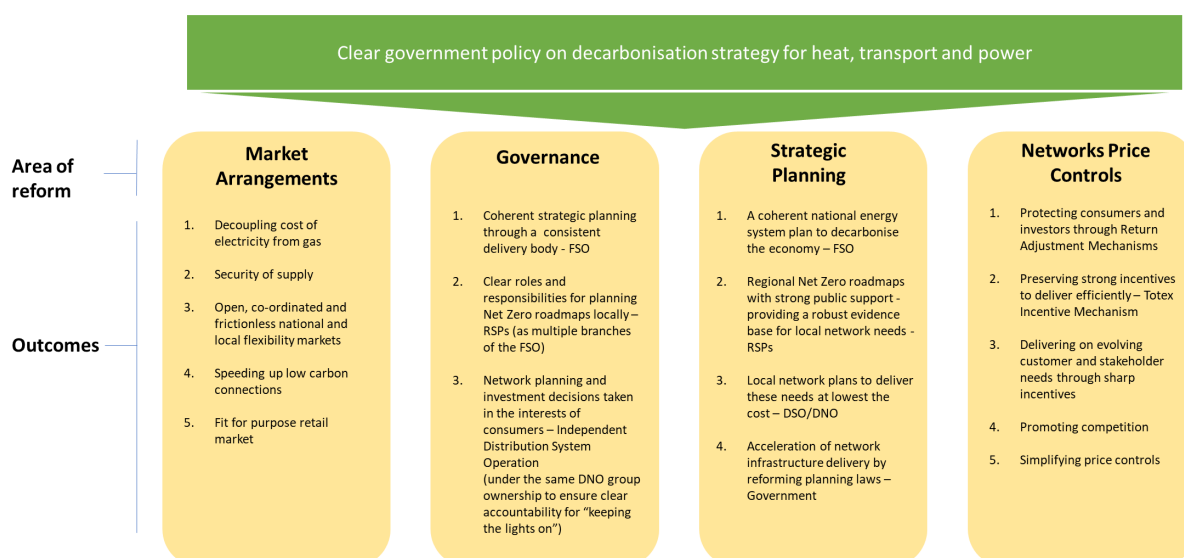
Dear Jonathan

## Future of local energy institutions and governance

Thank you for the opportunity to provide feedback on the future of local energy institutions and governance. We are encouraged to see Ofgem making progress on setting institutional arrangements that establish clear accountabilities for the delivery of energy networks which support the Net Zero transition.

**We believe that decisions on institutional arrangements should be considered in the context of the overall suite of reforms being proposed by Ofgem (e.g. Future Systems & Network Regulation). This is required to understand potential interlinkages and avoid any unintended consequences.**

To enable this, we have developed the framework below which articulates our understanding of the outcomes that Ofgem is seeking from the overall suite of reforms it proposes. This image is reproduced with larger font size in Appendix Two.



**We have stepped back and assessed the reforms holistically and have drawn five key conclusions relevant to local energy institutions and governance:**

- 1. Planning the Net Zero transition is broader than energy system planning.** The reality today is that most households do not understand the changes required and associated costs, especially for decarbonised heating. Therefore local/sub-national decision making on how the Net Zero transition should occur requires a democratic

mandate coupled with strong engagement with the electorate to maintain public support for Net Zero. It will require trade-offs to be made including on how costs are allocated across wider needs – housing, jobs, transport, improving air quality etc.

**2. The establishment of Regional System Planners (RSPs) to assist local government in determining the optimal pathway to Net Zero for the local region is crucial.**

Practically, this means:

- Supporting local government with technical analysis to determine what decarbonisation technologies should be deployed, how many, where and when;
- Ensuring that the pathway takes a whole systems approach to understand and incorporate dependencies on transport, housing, and other societal needs;
- Assessing the economic costs impartially and doing so across energy vectors to provide local government high quality information to base local policy decisions on; and
- Identifying the quantum of funding needed to realise the plans, recognising that this will be much broader than network investment costs alone.

Consistency in how the RSP role is delivered would be better achieved under the responsibility of a single entity such as the FSO, provided that the entity is resourced appropriately. If the FSO is chosen, its capabilities will need to be significantly enhanced from what is currently the case under the Electricity System Operator (ESO). The level of change required should not be underestimated.

**3. However, a regional system plan is not a substitute for an electricity network development plan.** Distribution System Operators (DSOs) have a crucial role in taking this regional plan and advising on how the electricity distribution network needs to be enhanced to deliver the needs at lowest cost. The DSO ensures that network investment decisions are taken in the interests of consumers i.e. the lowest cost options are always taken free from any asset-based bias. For DSOs to perform this task meaningfully, they require a thorough understanding of the condition and loading on the asset base. Independence of DSOs is critical to address any information asymmetry between network companies and Ofgem. They provide an effective layer of independent review, in addition to Ofgem's scrutiny, to ensure network capacity is required and delivered cost efficiently.

**4. Retaining DSOs under the same ownership group as the DNO maintains the healthy tension of keeping costs down of network investment whilst not jeopardising security of supply.** Responsibility for keeping the lights on remains with the DNO and under a single ownership group. In the event of major incidents and severe weather events, single ownership provides single point accountability to customers, Ofgem and government for security of supply. For the DNO to continue to assume responsibility for keeping the lights on meaningfully, it must have full confidence in load forecasts, network planning procedures, and in the availability of flexibility services. This is what has led UK Power Networks to a joint sign-off approach for our proposed DSO model; our view is that this is a pragmatic approach which delivers customer benefits whilst avoiding excessive cost duplication.

5. **Evolution of price controls for electricity distribution should be targeted in the areas where change is needed rather than wholesale reforms that create unnecessary uncertainty and distraction.** The reality is that less than 15 percent of DNOs' totex allowances are related to building new capacity in response to the Net Zero transition. Upending an incentive based regulatory regime which is world-leading and still relevant to the vast majority of totex allowances makes little sense. When we examine other regulatory regimes internationally in the US, Europe, or Australia, we do not conclude that their models are more advanced than the GB RIIO approach. Nor are they better prepared for the energy transition. Rather, we see these jurisdictions replicating elements of Great Britain's regulatory model in areas such as reliability and customer service incentives, stakeholder engagement focus and developing distribution level flexibility markets.

We describe our detailed views on networks price controls in our response to the Future Systems and Networks Regulation consultation. In summary these are:

- (i) **The introduction of Return Adjustment Mechanisms (RAMs), if calibrated correctly, provide a way to hugely simplify price controls** if network company returns are significantly higher than anticipated at the time of setting price controls. Rather than regulating for a myriad of inputs, Ofgem could utilise RAMs to provide an upper return expectation that the very best companies can earn if they deliver efficiently and in line with customer expectations enshrined in stretching, but realistic targets.
- (ii) **Ex-ante regulation and the totex incentive mechanism remain paramount to drive the private sector to deliver greater efficiencies using innovative solutions.** Taking a cost-plus approach or ex-post assessment of delivery significantly dilutes the focus of network companies to strain every sinew of efficiency from their operations utilising the latest technologies and solutions from the market. Given the quantum of future investment needed in the networks, we should be replicating the dynamics of competitive markets to incentivise and reward high performance, not moving in the opposite direction.
- (iii) **We strongly believe that RIIO incentives should continue to evolve to reflect the outcomes and changing needs of consumers as they decarbonise their lifestyles.** For networks to not be a blocker to decarbonisation, we believe that the customer service incentives should specifically measure low carbon technology connections and enquiries. This measurement should be underpinned by rewards or penalties. Similarly, as electricity will power more of our lives, the reliability incentives should be adapted to measure and reward reductions in momentary interruptions (less than three minutes). Ofgem should also be sharpening the incentive properties for the DSO to find and deliver the lowest cost solutions given the huge customer savings potential from a smarter and flexible energy system.
- (iv) Lastly, we recognise that there are a lot of voices from the industry calling for large scale strategic anticipatory investment to be allowed by networks. The reality is that most investment by its very nature is in anticipation of demand, otherwise we would experience far more unplanned power cuts. Therefore, we rationalise that commentators asking for large scale anticipatory investment are seeking the ability to make more speculative decisions about future network needs. The issue we have with this is that **new demand from decarbonisation will not be spread evenly and there is no guarantee on when and where network constraints will occur.** DNOs collectively have

hundreds of thousands of substations and hundreds of thousands of kilometres of linear assets. Encouraging system-wide reinforcement without being demand-led would be catastrophic for customers' bills, it would jeopardise the benefits of a smart and flexible energy system (estimated to be up to £16 billion per annum) and would exacerbate already stretched global supply chains unnecessarily. Future price controls therefore must:

- a. Protect customers from unnecessary network investment by having robust and independent network needs identified by RSPs in conjunction with other local stakeholders.
- b. Deliver network capacity at the lowest cost by having independent DSOs determining the optimal solutions for capacity free of any asset bias.
- c. Ensure that large scale strategic network investment, when it is required, is delivered efficiently by DNOs and monitored by Ofgem using price control deliverables.

**With respect to Ofgem's position on the three key areas in its consultation:**

### **1. Introduction of Regional System Planners**

- We support the introduction of Regional System Planners (RSP) which advise on regional decarbonisation pathways whilst electricity network planning remains within the remit of DSOs and DNOs.
- We believe that for the FSO to assume RSP responsibilities as described by Ofgem, there needs to be a quantum shift in capabilities and capacity of the current ESO. Our experience of working with the ESO to address the current connections and transmission/distribution interface issues is that the ESO has capable and committed people, but it requires:
  - Greater expertise and focus on distribution customer issues given that the decarbonisation of heat and transport will be transformative for the local distribution networks. Distribution networks cannot be an afterthought for the FSO.
  - Resources and funding to deliver change at a faster pace needed to meet distribution customer connection needs which are smaller scale and shorter duration relative to transmission. The backlash caused by extensive lead times to connect distribution level generation and storage and the time taken to respond with urgency is a case in point.
  - The depth of knowledge and strength of relationships at a local level to develop effective decarbonisation pathways. UK Power Networks' licence areas alone have over 127 local authorities each with differing levels of net zero ambitions. The FSO will need to step up to take on this significant engagement and planning activity whilst also dealing with transmission level issues, including connections reform without delaying progress in these critical areas too.
- We also considered alternative entities to deliver the RSP role given the challenges described above. For example, extending the role of the Climate Change Commission (CCC) to produce regional roadmaps for Net Zero alongside its national work. The CCC could franchise in regional task forces led by leading figures in each region, including academics and other public figures to leverage cross-disciplinary expertise and help exercise quality control centrally over the regional work. It could also effectively hold national and local government to account for delivery against published long term regional plans.

- Any proposal is likely to have different trade-offs; there is no perfect answer. If additional RSP responsibilities are placed under the stewardship of the FSO, there needs to be a clear strategy, underpinned by targets and accountability placed on the FSO's management to ensure that progress in existing critical areas does not slow down.

## **2. Market facilitation of flexible resources**

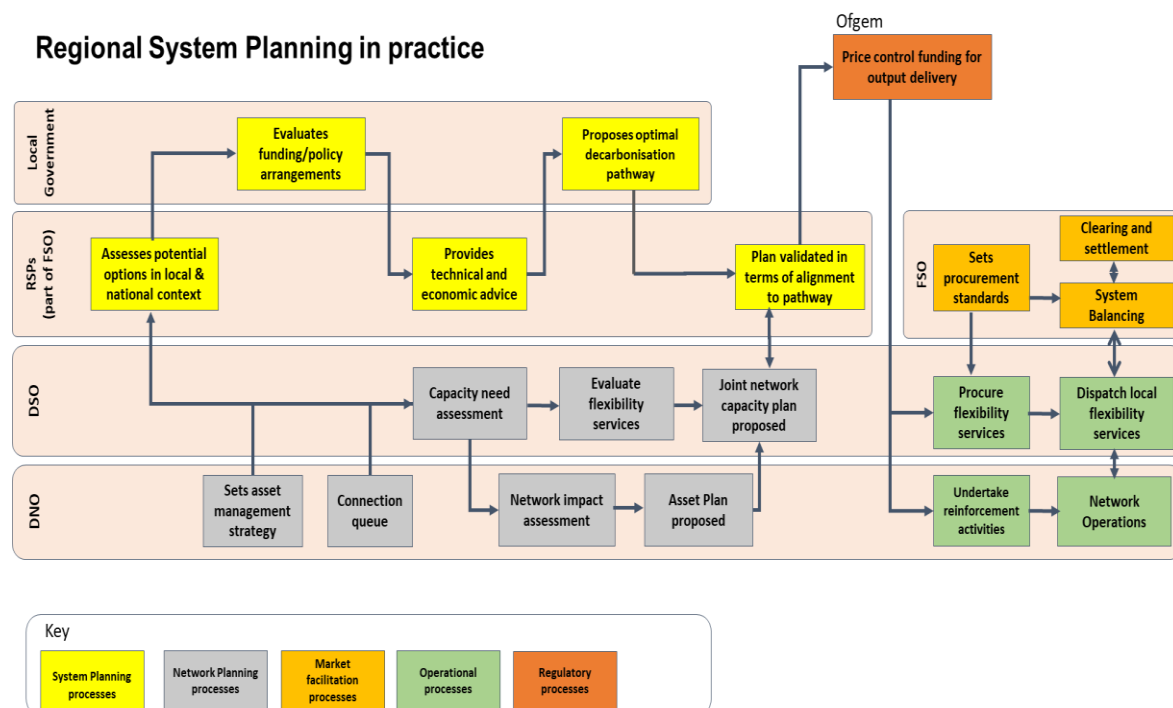
- We agree that the FSO should take a key role in market facilitation aligned to the roles and responsibilities that Ofgem sets out in its consultation. However, we believe that there should be a formal way in which DSOs can influence the design of future flexibility products by the FSO such that they are fit for purpose for distribution level needs. It would be a mistake for the FSO to drive flexibility product development without a strong voice from the DSOs to ensure their needs are met. Similarly, DSOs will need to continue to engage with flexibility providers if they are to successfully contract with them and rely on their services. Ofgem's current RIIO-ED2 DSO incentive recognises this important point by measuring this area specifically. The FSO does not have the expertise to understand distribution level issues and distribution level flexibility markets are not at a level of maturity yet where DSOs can be restricted to simply identifying network needs and submitting requirements on a market platform. Reform in this area must reflect the realities on the ground today to drive successful change rather than slow down progress.

## **3. Real-time operations**

- We welcome Ofgem's proposal that DNOs will remain responsible for real time operations and keeping the lights on. This will enable UK Power Networks to build on its strong track record, which has involved reducing the number of customer interruptions by 18% and their length by 23% over RIIO-ED1. Nevertheless, as set out in our RIIO-ED2 Business Plan we still see a need for oversight from the DSO on DNO control activities to ensure that flexibility dispatch decisions are undertaken on an open and transparent basis and that contracted flexibility is used to its fullest extent.

**Before any final decisions are made on institutional arrangements, we believe that Ofgem's high level vision must be translated into a workable operating model that reliably delivers intended outcomes and does so at pace.**

UK Power Networks has been developing a model based on its experience summarised below. In our response to Ofgem's detailed questions this model is reproduced with larger font size and we provide more details of how this model would work in practice.



**The reform of local energy institutions must not slow down progress; the energy sector needs to continue to perform whilst it transforms.**

Through our recent engagement with key stakeholders spanning flexibility providers, market platform developers, local and combined authorities, as well as Citizens Advice, we have overwhelmingly heard that they want to work more closely with us to address today's challenges as quickly as possible. Not doing so would create a real risk of delaying much needed expertise being shared with local and combined authorities in the short-medium term to help them get plans off the ground and getting on with the investment in networks required to meet the government's targets to ban new petrol and diesel vehicles from 2030 and facilitate connection of 600,000 heat pumps per year by 2028.

To ensure that the energy industry accelerates its pace whilst reforms are designed, we believe that:

- Industry and Ofgem should work together to reform the Open Networks Programme in a targeted way in advance of the FSO being established.** Open Networks should have clear targets to deliver improvements in high priority areas such as network primacy rules, there should be increased involvement of non-network parties and its Steering Group should be reformed to enhance its independence, powers, and transparency. We are committed to work with Ofgem to make this happen quickly given the need to make progress on critical issues.
- Ofgem should utilise the new DSO incentive and associated DSO KPIs to compare and drive network company performance.** Its Performance Panel should ensure network companies make significant progress on their DSO commitments by rewarding the best and penalising the laggard performers. Doing so will enable Ofgem to gather a rich set of real-world insights to inform future policy design in this area. Ofgem should be confident that high powered incentives work based on

evidence of how customer service and reliability have dramatically improved over RIIO-ED1.

- **Ofgem and industry should work together to develop an integrated roadmap to 2030** that shows how the various reform programmes combine to deliver improvements that benefit consumers. This will help industry to prioritise its support to Ofgem, as well as provide transparency about commitments and progress made against them to government and wider stakeholders.

We look forward to engaging with Ofgem on shaping the detailed governance reforms that will unlock the full benefits of a smart and flexible system for consumers and local communities.

Yours sincerely



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## Appendix One – UK Power Networks’ responses to questions

### . 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 support the introduction of Regional System Planners (RSPs) which advise on regional decarbonisation pathways whilst electricity network planning remains within the remit of DSOs and DNOs.

We believe the RSP adds greatest value as an organisation that advises the public sector on how to deliver decarbonisation and how to address the associated key challenges facing local and regional government to make progress. Our concern is that Ofgem’s focus on RSPs in the energy sector alone is too narrow for the needs of regional and local (and national) government and that energy-only RSPs risk in part duplicating activities that we are already doing today as a DSO.

If the RSP simply comes up with an optimal pathway for a region, but cannot resolve the barriers to realising it, such as funding requirements and policy levers, it is unclear how the RSP will achieve a step change in progress. In fact, there is a risk, especially in the context of Ofgem’s FSNR proposals, that licensees are put under pressure to strategically invest in line with these pathways even though they may be unlikely to be delivered, which would lead to stranding at customers’ expense. RSPs must therefore be integrated into government decision-making at local, regional and national level on how to deliver Net Zero in each region, including which networks are needed and when.

We welcome Ofgem’s proposal to retain network planning within the DNO’s remit, but we recommend clearer delineation between these network planning requirements around the delivery of network capacity, from the responsibilities of a new RSP function which aims to advise on regional decarbonisation pathways. Decarbonisation planning needs to consider the trade-offs between how costs are allocated fairly across society and across energy vectors. In contrast the trade-offs between network reinforcement and flexibility solutions for energy system planning are of second order importance in this societal context, and they are already dealt with through Ofgem’s regulatory framework.

Any institutional settlement has to be judged against a number of criteria. We agree that the key ones are as set out in the consultation, but there are challenges in respect of each one.

- **Clear Accountability** – this means that responsibilities are assigned to a single body. The proposed RSP function could be interpreted as significantly overlapping with or even subsuming DSO functions of electricity network planning. Clear delineation is required between the two. If the RSP takes over any significant part of electricity network planning, moreover, this has implications for clarity of accountability for DNOs over network reliability and safety.
- **Organisational credibility** – this comes from experience of undertaking activities, the organisation’s current culture and how trusted it is to deliver. FSO is a new



organisation and any inherited track record acquired by subsuming ESO into the new body would need to be supplemented by significant new expertise on regional and local planning for Net Zero and on distribution network responses.

- **Speed of response** – any future model must avoid slowing down progress. The ban on the sale of petrol and diesel vehicles is less than seven years away and the target to have a fully decarbonised power system is less than twelve years away. Any new organisation will take time to achieve full operational efficiency and the wider the spread and the greater the volume and depth of new functions, the more time it will take. This suggests, to our minds, a prioritisation of functions which add to current capabilities overall, rather than disrupting existing activity by foreseeing institutional shifts in existing functions. An RSP focused on helping plan for Net Zero at regional and local level would add to existing capabilities, one which takes over existing and planned DSO functions would put short- and medium-term progress at risk.
- **Continuous innovation** – both uncertainty and a lack of incentives can deter innovation, which is evidently needed due to the nature of the challenges being faced. The RSP will need to engage significant resource in understanding the diversity of regional and local environments and aspirations for Net Zero as well as network capacity and potential to respond. There is a risk that solutions are perceived as top-down impositions, especially if the RSP lacks the capacity to engage in depth at local level. If network planning responses are imposed on DNOs, meanwhile, their ability to innovate in meeting demand efficiently will be curtailed.
- **Implementation cost** – creating new bodies and/or systems is hugely time-consuming and costly, which means the benefits of doing so must be clear and sufficient.

Set out below on pages 13 – 16 we offer an assessment of the extent to which the main criteria are met in respect of some of the key local and regional Net Zero and distribution network challenges we are facing today. We do this for two very different RSP models:

- one where the FSO leads on facilitating local flexibility and distribution network planning, thereby replacing the need for separate DSOs, rather than focusing on supporting local and regional authorities on Net Zero pathways more broadly,
- the other where the new RSP is dedicated to supporting local and regional government with Net Zero planning. DSOs focus on determining network planning and capacity needs and delivering local flexibility and have legal separation from DNOs.

The reasoning behind our preference for the latter model is clear from the charts.

No solution will be perfect, and it is possible that the FSO can be equipped to deal with all the above challenges, but the scale of them has led us to consider priorities and alternative means of delivering them. Our preferred model would therefore deliver the following:

- **Establishment of an RSP function** with a sharp focus on assisting local government in determining the optimal pathway to Net Zero for different regions. This would ensure that the pathway adopts a truly whole systems approach to understand and incorporate dependencies on transport, housing, and other societal needs. The RSP would advise on how policies and funding could be best leveraged to ensure

delivery in a way that aligns to the UK's overall Net Zero target and what is being sought by sub-national leaders with a democratic mandate.

Due to the size of the resource gap, the complexity involved in setting regional and local area decarbonisation plans and the urgency of action, we believe that the RSP needs to build on what our DSO is doing today in advising local government and focus on complementing rather than duplicating existing DSO functions.

- **Establishment of an independent and legally separate DSO business unit within all DNO groups.** The DSO advises on what network capacity is needed to facilitate pre-agreed local and regional plans and ensures this is delivered cost efficiently. As part of this the DSO maximises existing network capacity and takes a flexibility first approach. This arrangement means there is an effective layer of independent review without significantly duplicating functions or diluting accountability for network reliability. In contrast if the FSO did this instead of the DSO, the incentive to procure and use flex for distribution needs would be greatly reduced and the DNO would put a higher risk premium on flexibility options.
- **DSOs continuing to take a central role in increasing the participation of local flexibility.** We now have over five years of experience of tendering flexibility across our networks. Our first flex tender secured flex at a handful of sites, whereas in our latest 2023 tender we have just offered £14m of contracts spread across 1,000 sites. As a result, we have built up a deeper understanding of how flex can solve our networks' needs, and how we can better support flex providers overcome the commercial and technical obstacles they face due to the innovative nature of their offerings. On the other hand, the FSO, which will be borne out of the ESO, has experience in dealing with well-established and large flexibility players for national balancing. This is a very different to managing local constraints, which typically involves tapping into the flex that EVs can provide as well as using network optimisation tools.

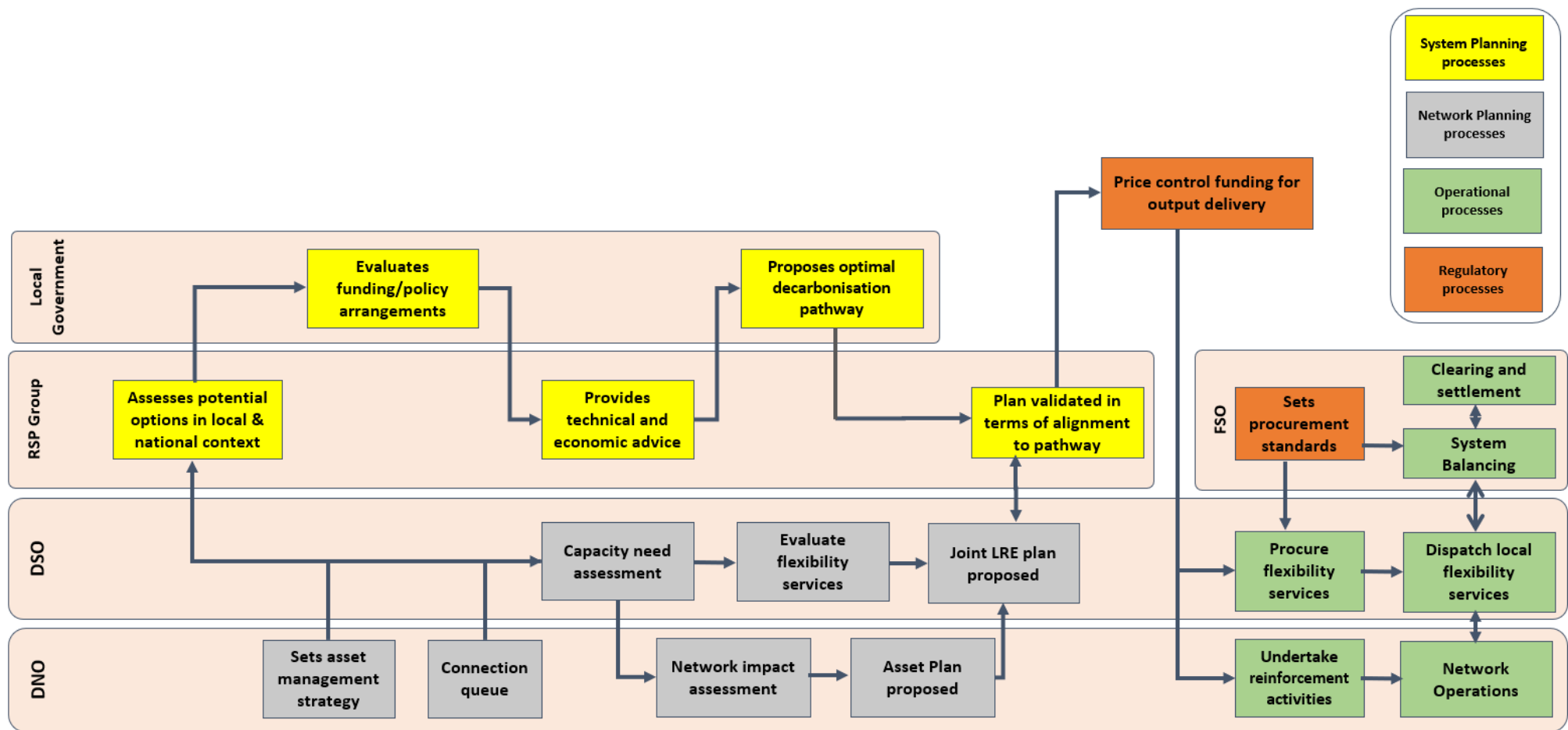
The process map on the next page is an overview of our recommended model that describes the key interactions between different parties. Essentially it shows the critical path between setting decarbonisation pathways and delivering the associated network capacity. Local government, with support from the RSP, sets a regional decarbonisation pathway. The RSP helps to ensure regional pathways align to a common national scenario.

Under this arrangement the DNO jointly develops a load related expenditure plan with the DSO that can respond to regional decarbonisation plan needs, and which helps ensure cost efficiency by minimising any bias between flexibility and reinforcement, as well as focusing on forecasting accuracy. In this model accountabilities are clear across network boundaries, and it avoids a situation where the FSO duplicates DSO responsibilities.

To help shape Ofgem's thinking it is useful to ask two key questions with regards to the proposed reform package:

1. Does it accelerate DSO and RSP related capabilities in a way that delivers better customer outcomes, for example does it ensure that there is strong accountability for delivering the commitments made in RIIO-ED2?
2. Which parties will be able to best prioritise the challenges being discussed in the consultation? In particular, can the FSO realistically rapidly develop the depth and range of high-level capabilities it needs to be responsible for developing flexibility markets at distribution level, for advising local and regional governments across the

country on Net Zero, for planning distribution network pathways in each locality as well as all the other wide ranging areas they will already be covering in place of the ESO. If certain functions have to be prioritised, which ones add most value to the current institutional set-up?



An interpretation of Ofgem's proposal whereby the RSP, embedded in the FSO, leads on facilitating local flexibility and distribution network planning, thereby replacing the need for separate DSOs, rather than focusing on supporting local and regional authorities on Net Zero pathways more broadly				
Today's key challenges	Clear Accountability	Organisational credibility	Speed of response	Continuous innovation
Engagement with communities on Net Zero i.e. providing expertise to support their needs	<ul style="list-style-type: none"> <li>FSO would be expected to engage with local government to understand their requirements, but as would licensees to effectively plan their networks and to facilitate connections</li> </ul>	<ul style="list-style-type: none"> <li>Unclear how the FSO would be able to take account of local views and meaningfully support at the very local level – risk of national imposition or a perception of national imposition</li> </ul>	<ul style="list-style-type: none"> <li>Would take many years to build resource in FSO to achieve this level of engagement</li> <li>Unclear that FSO could secure necessary public funding to develop this expertise at the necessary scale</li> </ul>	<ul style="list-style-type: none"> <li>Misaligned to DSO incentive that is already encouraging new and enhanced ways to support LAs and community groups</li> <li>Unclear what happens if FSO does not make sufficient progress</li> </ul>
Defining the optimal regional decarbonisation pathway i.e. making cross vector recommendations	<ul style="list-style-type: none"> <li>FSO would not have a democratic mandate to make these decisions.</li> <li>Decisions go beyond energy networks into spatial/transport planning – no framework for government decision-making</li> <li>FSO could have accountability for DFES, but unclear consequences if this does not align to what LAs or the DSO defines over a certain area – unclear hierarchy</li> </ul>	<ul style="list-style-type: none"> <li>FSO has credibility on forecasting but doubts over its ability to take full account of local variations. DNOs already doing this so added risk of duplication</li> <li>ESO has no knowledge of local trade-offs to inform setting an optimal pathway</li> <li>Unclear regional boundaries could make local government engagement very difficult</li> </ul>	<ul style="list-style-type: none"> <li>Would take time for FSO to do this properly and likely to be low down their list of priorities – it goes far beyond the remit of the ESO today</li> </ul>	<ul style="list-style-type: none"> <li>A risk that plans will be too top-down if led by the FSO and there is less emphasis on localised collaboration</li> <li>Risk of less innovation from DSOs in ensuring agility to respond to changing need, especially if DSO local engagement is downgraded</li> </ul>
Turning local ambition into an action plan i.e. addressing the funding and other barriers to local decarbonisation	<ul style="list-style-type: none"> <li>FSO likely to dictate parts of the plan and offer no support for other parts, potentially removing LA control. Mixed accountability and unclear democratic legitimacy</li> </ul>	<ul style="list-style-type: none"> <li>FSO has strong knowledge of the national system but not of the local system and local trade-offs</li> </ul>	<ul style="list-style-type: none"> <li>RSP team within the FSO will take years to establish and get up to speed. Likely to lead to delay in resourcing LAs properly to give them the support they need</li> </ul>	<ul style="list-style-type: none"> <li>Standard approach by FSO could eliminate diversity of methods of support and innovation. North of Scotland has different characteristics to Central London</li> </ul>

An interpretation of Ofgem's proposal whereby the RSP, embedded in the FSO, leads on facilitating local flexibility and distribution network planning, thereby replacing the need for separate DSOs, rather than focusing on supporting local and regional authorities on Net Zero pathways more broadly				
Today's key challenges	Clear Accountability	Organisational credibility	Speed of response	Continuous innovation
Distribution Network Planning to facilitate demand changes i.e. deciding needs and solutions	<ul style="list-style-type: none"> <li>Unclear where FSO responsibility would end and DNO accountability begins. Likely to create duplication and real risk of disputes and unclear how these would be resolved</li> </ul>	<ul style="list-style-type: none"> <li>FSO has credibility around EHV/132kV network planning but not at LV/HV level, which is where the majority of change is happening/forecasted</li> <li>Would not reduce the need for licensees to continue to do what they do today as per licence conditions</li> </ul>	<ul style="list-style-type: none"> <li>Will take years for FSO to get a deep understanding of distribution network requirements and unclear what it would do differently</li> <li>Risk of rushing decisions based on inaccurate assumptions to the detriment of consumers</li> </ul>	<ul style="list-style-type: none"> <li>A thick FSO that makes decisions at the distribution level will use standardised assumptions that fail to recognise local factors and lead to inefficiency</li> <li>A greater risk that politically motivated decisions override evidence based decision making</li> </ul>
Facilitating timely connections at distribution i.e. queue management	<ul style="list-style-type: none"> <li>Split accountability between DNO and FSO. Possibly improved coordination with FSO on connections with Transmission implications but unclear hierarchy</li> </ul>	<ul style="list-style-type: none"> <li>Due to today's connection delay issues there will be doubts on what the FSO will do differently. There is likely to be a general bias towards EHV/132kV level and big kit over smaller scale connections at LV/HV</li> </ul>	<ul style="list-style-type: none"> <li>Uncertainty over responsibility could slow down investment in new arrangements pending FSO direction – could also be disagreements around what is needed</li> </ul>	<ul style="list-style-type: none"> <li>Could improve uniformity of response at expense of loss of diversity and innovation e.g. use of flexible connections</li> </ul>
Maintaining a high standard of local network reliability in context of transition	<ul style="list-style-type: none"> <li>DNO accountability clear in principle but in practice could be undermined by FSO making decisions that it has no control over</li> </ul>	<ul style="list-style-type: none"> <li>Loss of clear DNO accountability for planning and flex dispatch could cause decline in confidence in network reliability</li> </ul>	<ul style="list-style-type: none"> <li>Unaffected so long as FSO stays clear of duplicating existing responsibilities/processes</li> </ul>	<ul style="list-style-type: none"> <li>FSO will not be well placed to innovate without potentially compromising reliability – no rule book for this – could result in risk aversion at high cost to consumers</li> </ul>
Unlocking benefits of local flexibility i.e. maximising participation and use	<ul style="list-style-type: none"> <li>Would dilute accountability of the DNO in a way that makes contracting flexibility more complex – for example unclear liabilities</li> </ul>	<ul style="list-style-type: none"> <li>ESO does not have a track record of procuring flexibility for local needs</li> <li>DNOs have just put in place commitments that will be tracked by a DSO incentive, whereas the ESO has very little incentive to deliver progress in this area</li> </ul>	<ul style="list-style-type: none"> <li>Likely to delay the progress currently being made to develop local flex markets</li> <li>System balancing at the transmission level is very different to managing constraints at the street level</li> </ul>	<ul style="list-style-type: none"> <li>DNOs may innovate less as they will have less incentive/control to do so</li> <li>Detracts from private sector led innovation, which has a proven track record</li> <li>Could inhibit third parties from taking on DSO related capabilities</li> </ul>

RSP is dedicated to supporting local and regional government with Net Zero planning. DSOs focus on determining network capacity needs and delivering local flexibility and have legal separation from DNOs. FSO focuses on national requirements and through RSPs and licensees to ensure whole systems optimisation

Today's challenges	Clear Accountability	Organisational credibility	Speed of response	Continuous innovation
Engagement with communities on Net Zero	<ul style="list-style-type: none"> <li>• Yes – RSP would principally engage on Net Zero issues. Licensees would engage on network access and connections in their respective areas</li> </ul>	<ul style="list-style-type: none"> <li>• RSP would be dedicated to supporting Net Zero planning. FSO would have to develop the necessary resources, but presumably could do so. The CCC, for example, would also be credible in this role</li> </ul>	<ul style="list-style-type: none"> <li>• New group would take time to set up but in the meantime DSOs could continue to make progress</li> </ul>	<ul style="list-style-type: none"> <li>• Difficult to assess but the FSO could probably focus on regional differentiation and innovation if this was its primary role. The CCC, alternatively, would probably engage local thought leaders in universities and elsewhere and support place-based solutions. DSOs could also focus on embedding an innovation driven culture with local variation</li> </ul>
Defining the optimal regional decarbonisation pathway i.e. making cross vector recommendations	<ul style="list-style-type: none"> <li>• RSP would define optimised pathway led by local government with a mandate to do so, but still no clear framework for government decision-making</li> <li>• DFES and FES would reflect pathways identified by the RSP but DSOs and FSO would provide guidance to shape this</li> </ul>	<ul style="list-style-type: none"> <li>• Yes as RSP's primary focus would be to do this and there would be no change to existing responsibilities</li> </ul>	<ul style="list-style-type: none"> <li>• Dependent on speed of setting up the RSP and the powers it has, but CCC, for example, could probably use academic networks to build regional teams fairly quickly and blend national methodology and quality control with regional differentiation</li> </ul>	<ul style="list-style-type: none"> <li>• DSO led innovation in this area can continue, but with layer of further innovation to align with FSO/RSP cross-vectorial insights</li> <li>• Alternatively CCC regional planning for net Zero could unlock a variety of innovative approaches</li> </ul>
Turning local ambition into an action plan i.e. addressing the funding and other barriers to local decarbonisation	<ul style="list-style-type: none"> <li>• Yes, clear accountability would lie with regional/local government – RSPs would be critical enablers and would go beyond the proposed FSO narrower remit</li> <li>• Still need government to establish framework for validating/funding local plans</li> </ul>	<ul style="list-style-type: none"> <li>• Yes, local and regional authorities would value this support immensely and it would support any national government decision-making.</li> <li>• Still need government to establish framework for validating/funding local plans</li> </ul>	<ul style="list-style-type: none"> <li>• Requires clarity on local/regional authority responsibility for Net Zero planning and where any funding comes from – which is true in any scenario</li> </ul>	<ul style="list-style-type: none"> <li>• Diversity of approaches from different local/regional authorities will create opportunities for innovation and sharing of best practice</li> </ul>

RSP is dedicated to supporting local and regional government with Net Zero planning. DSOs focus on determining network capacity needs and delivering local flexibility and have legal separation from DNOs. FSO focuses on national requirements and through RSPs and licensees to ensure whole systems optimisation				
Today's challenges	Clear Accountability	Organisational credibility	Speed of response	Continuous innovation
Distribution Network Planning to facilitate demand changes i.e. deciding needs and solutions	<ul style="list-style-type: none"> <li>• Clear accountability on licensees which avoids any grey area between the FSO and/or RSP</li> </ul>	<ul style="list-style-type: none"> <li>• Yes on basis that Ofgem retains policy drive to ensure DSO operational independence from DNO</li> </ul>	<ul style="list-style-type: none"> <li>• As RIIO-ED2 plans will be implemented and Ofgem can demand faster progress through the DSO incentive and ahead of RIIO-ED3</li> </ul>	<ul style="list-style-type: none"> <li>• Ofgem will continue to incentivise innovation and competition between licensees to deliver best practice, with others following suit</li> </ul>
Facilitating timely connections at distribution i.e. queue management	<ul style="list-style-type: none"> <li>• Clear accountability for DNOs albeit a need for improved co-ordination with FSO on connections with transmission implications. Definition at GSP boundary could support this</li> </ul>	<ul style="list-style-type: none"> <li>• DNOs understand their networks the best and defining the boundary at the GSP would make interactions between RSP, FSO and the DNO easier</li> </ul>	<ul style="list-style-type: none"> <li>• Should help avoid any overlaps in responsibilities, which will then free up companies to focus on delivery</li> </ul>	<ul style="list-style-type: none"> <li>• With clear DNO responsibility, scope to incentivise risk management in this area – e.g. shared connections, secondary trading</li> </ul>
Maintaining a high standard of local network reliability	<ul style="list-style-type: none"> <li>• Clear accountability on the licensee</li> </ul>	<ul style="list-style-type: none"> <li>• Yes as is the case today</li> </ul>	<ul style="list-style-type: none"> <li>• Yes as the licensee is already incentivised to make trade-offs without compromising reliability</li> </ul>	<ul style="list-style-type: none"> <li>• Yes as licensees would progress DSO capabilities with confidence</li> </ul>
Unlocking benefits of local flexibility i.e. maximising participation and use	<ul style="list-style-type: none"> <li>• DSO would focus on using local flex and would be measured/tracked through the RIIO-ED2 incentive</li> <li>• Would require stronger and consistent rules between the FSO-DSO to avoid conflicts</li> </ul>	<ul style="list-style-type: none"> <li>• Some DNOs will advance faster than others and be more credible, but Ofgem can boost credibility by insisting on organisationally-independent DSOs that have a different culture and rewarding strongest performers</li> </ul>	<ul style="list-style-type: none"> <li>• DNOs moving at different speeds but the DSO incentive will reveal this and could penalise inaction</li> </ul>	<ul style="list-style-type: none"> <li>• Aligns to RIIO-ED2 Business Plan requirements and the new DSO incentive</li> <li>• Would leverage existing programmes, but could inhibit third parties from taking on DSO related capabilities due to regulated position</li> </ul>



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

We agree with the considerations that Ofgem has summarised, but we are yet to see evidence of how they have been applied. For example, the FSO does not currently possess the necessary skills and expertise. It is unlikely to fully take shape until 2025 at the earliest and any ESO capabilities it inherits will not equip it fully for an RSP role, as the ESO does not undertake any meaningful RSP responsibility today and its expertise in national/transmission issues is not transferable to the regional and local issues being faced.

We recommend that Ofgem uses the framework we presented in response to Question 1 as a way of testing its proposals. Regarding accountability there also needs to be more focus on the boundaries between roles.

- **Q3. Do you have views on the appropriate regional boundaries for the RSPs?**

Regional boundaries must be set in a way that empowers those with a democratic mandate to make decisions on how their areas can best decarbonise. We therefore recommend that the start point in England is combined authorities, which represent local authorities at a regional level. Where these do not exist, counties would be the next best alternative. We disagree with setting boundaries based on the position of energy networks as this would be counterproductive to what is trying to be achieved. The end goal is to deliver Net Zero at lowest cost, which requires decisions to be made that cut across energy, transport, housing and other public services. Therefore, if we are to succeed in engaging regional and local leaders to drive the change needed, we must focus on democratic boundaries.

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

Due to the size of the resource gap and complexity involved in setting regional and local area decarbonisation plans, there is no organisation that can perform this role optimally today.

A new and independent RSP role could be offered to the FSO, but it would need to acquire all the necessary skills and expertise as it does not exist today. Even if it absorbs the ESO entirely, it would not have the necessary experience, as the ESO is not engaged in cross-sectoral planning for Net Zero or in distribution network planning and does not engage with local and regional authorities meaningfully at the moment.

One alternative could be to extend the role of the Climate Change Commission (CCC) to produce regional roadmaps for Net Zero alongside its national work. The CCC could franchise in regional task forces led by leading figures in each region, including academics and other public figures as well as energy network leaders to ensure cross-disciplinary expertise and could exercise quality control centrally over the regional work. It could also effectively hold both national and local Government to account for delivery against published long term regional plans.

A focussed RSP function within either FSO or the CCC, but with a clear remit for regional decarbonisation planning would complement DSO/DNO network planning activity and allow all parties to build on best practice of what networks are doing today in advising local government, instead of simply duplicating today's DSO activities under the FSO.

We see a risk that a narrow, energy-only RSP creates an illusion of comprehensive action in support of regional strategies for Net Zero that in reality may slow down progress. Such an RSP would not be able to operate beyond the energy sector, but its establishment may delay or prevent the adoption of a more complete regional Net Zero planning and advisory service for local and regional government. We think it is critical that the stakeholder process is evolved today and that tools are put in place as quickly as possible to aid regional planning across the board.

A further issue is how to ensure that the RSP is adequately resourced. An under-resourced public body would probably tend to underplay regional and local specificities and engagement in favour of more homogenous approaches driven by national policy, for example. This could greatly inflate the total cost of Net Zero by failing to identify more cost-effective local solutions, leading to risk-averse investment decisions and displacing place-based innovative ideas. It would also make local engagement on delivery more difficult. Ofgem needs to think about how to ensure that the RSP function can best be delivered cost-effectively and with maximum confidence around future funding streams.

• **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?**

We agree that the FSO should take a key role in market facilitation, but there should be a formal way in which DSOs can influence the design of future flexibility products by the FSO such that they are fit for purpose for distribution level needs and pursue innovative approaches. It would be a mistake for the FSO to drive flexibility product development without a strong voice from the DSOs to ensure their needs are met.

We also believe that DSOs should retain formal influence over the decision making on flex procurement in terms of when, where and what requirements they have, whilst adhering to any common standards. DSOs will also need to engage with flexibility providers if they are to successfully contract with them and rely on their services. Indeed Ofgem's RIIO-ED2 DSO incentive recognises this important point by measuring this area specifically.

The ESO does not yet have the expertise to manage distribution level issues and distribution level flexibility markets are not at a level of maturity yet where DSOs can be relegated to simply identifying network needs and submitting requirements on a single market platform. The FSO could become a very different and more inclusive organisation over time, but there would still be a risk that any single platform would inhibit innovation and growth in a market which was still evolving rapidly.

In our parallel response to the Call for Input on Distributed Flexibility we state our support for the "medium" archetype of a common exchange for the time being, to balance ease of access for suppliers of flex with the maintenance of an ecosystem which can still experiment with innovative products and approaches. The market for distributed flexibility is still in its infancy and it is risky to pursue uniformity too early.

It is also important that there is full-bodied pursuit of distributed flexibility over the next five years, when the FSO will still be under construction, recruiting and finding its feet.

We are concerned that offering an all-encompassing role to the new organisation risks inhibiting deployment and innovation by DSOs in the meantime as people with the necessary skills may not be recruitable to organisations which will lose key responsibilities in the near future and organisations will be unwilling to invest in assets which may become stranded. This risks:

- Undoing five years of RIIO-ED2 planning that has led to the implementation of new licence requirements and ambitious commitments such as UK Power Networks' goal to deliver over £400m of DSO related benefits over the next five years;
- Creating an investment hiatus that delays progress towards meeting the government's targets to ban new petrol and diesel vehicles from 2030 and deploy 600k heat pumps per year by 2028;
- Delaying much needed expertise being shared with local and combined authorities in the short-medium term to help them get plans off the ground; and
- Weakening industry partnerships that would otherwise help to remove barriers to entry, such as improving procurement processes and standardising flexibility products, as the sustainability of any such improvements would be questioned.

Time pressure related to the 2035 deadline for a decarbonised electricity system suggests that reform should be designed to evolve, building on what has gone before, allowing all parties to advance at pace in the meantime. Transferring institutional responsibilities rather than building out new roles, threatens instead to slow down the transition.

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

Set out below we have summarised Ofgem's Table 2 in terms of how we have understood it and we have added a RAG status to highlight where we agree with Ofgem's allocation of roles and where we have concerns. Our greatest concern is with the market engagement activity. This is an area where we have invested a lot of effort in recent years and we believe it is crucial that we continue to build on the relationships we have developed, as well as forging new relationships to increase market participation. We do not see how we could credibly procure flexibility for our needs without engaging with providers – ultimately this will lead to contracts where both parties need to work together to a common aim with mutual trust.

Where we have put amber markings, the devil is in the detail of how this is implemented in practice. For example, we see a potential conflict of interest as the FSO is primarily focused on national requirements as a flex buyer instead of meeting distribution capacity needs, which we are accountable for. We also see a tension between standardisation of products and innovation in new product development and variation. We see DSOs as having a major role in contributing to the latter as needs and opportunities evolve.

As stated in our response to the Call for Input on Distributed Flexibility it is vital that any market facilitation body is consumer focused and driven by the needs of the suppliers and aggregators of flexibility as well as the buyers. It is possible that FSO, as a public body, may be able to ease potential concerns about bias and reassure all parties that it will be driven by the needs of the market, but there are alternatives. For example, the market exchange could be partly or fully owned and/or delivered by a collective industry grouping or by an independent third party, rather

than a buyer of flexibility; if this is progressed it would allay our concerns on responsibility for issuing flex tenders.

RAG	Activity	FSO		
		Market Facilitator	Market Platform	DNO
	Product Development & Standardisation	X		
	Market rules (primacy, revenue stacking, contracts etc.)	X		
	Market engagement	X		
	Market registration and management		X	
	Identify, specify and submit requirements			X
	Evaluate and select preferred option			X
	Issuing flex tenders		X	
	Hosting flex tenders		X	
	Recording and publishing market data		X	X
	Market oversight	X		

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

We have not identified any other activities.

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

Please see our answer to Q9.

- **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?**

This is a combined answer for Q8 and Q9.

Ofgem's consultation points to shortcomings of current arrangements and in particular the ENA's Open Networks programme. Whilst we recognise that there is scope for improvement, we believe there is a risk of placing too much emphasis on Open Networks as a vehicle for market facilitation, as we have not seen it as undertaking this function. In our view Open Networks intends to increase collaboration between stakeholders to deliver a common interest. In this regard we agree that there is a wider gap in terms of driving best practice and accountability for market facilitation.



As a general point we think there are unclear boundaries between the role of a flex buyer, market operator/facilitator and a market platform provider. More thought is also needed around the boundaries between markets for meeting distribution network needs versus markets for wider system needs to avoid any bias or unintended consequences. We would therefore welcome further discussion around how these boundaries could be better defined to ensure that clear accountabilities can be assigned to the appropriate parties.

A key issue here is around terminology, as we fully support establishing an independent market operator, which could be referred to as 'the market facilitator', which acts as interface between providers and buyers. Whereas the DNO/DSO and ESO/FSO could be better described as the flexibility buyers.

As outlined in our response to Ofgem's Call for Input on Distributed Flexibility we also support a collectively-owned market exchange that could be run by an independent market operator. We see this as covering several of the activities discussed by Ofgem as market facilitation. In our view this should be independent of the FSO and DSOs who would otherwise be conflicted as flex buyers. This exchange would permit the operation of several new and existing platforms that also facilitate flex trades, whilst easing market access for suppliers and improving information exchange. It would also add value by providing a 'single source of truth' that system operators can refer to.

The FSO, in taking up the ESO's responsibilities, will be a key buyer of flex, but equally as a DNO/DSO that is focused on delivering for customers at lowest cost, we will also be a market facilitator in one sense – in the same way that the ESO is for system balancing.

To maximise the participation, purchase and use of flex we recommend a combination of licence obligations and incentives, both of which are now being progressed under RIIO-ED2 arrangements. Alongside this we see a role for the FSO as a system coordinator that can help to ensure that processes and products have a level of consistency, but areas such as product design and primacy rules should be seen as a two-way process with DNOs/DSOs, as a key goal is to encourage them to use local flexibility. We are therefore concerned around some of the language Ofgem uses around a single decision-maker defining deliverables.

### Next steps

Looking forward we recommend that there is clarity on roles, a doubling down on incentives to drive best practice, alongside a renewed focus on the Open Networks programme. Together these focus points can deliver significant customer benefit by unlocking flex markets, whilst also strengthening collaboration regardless of any future model that is realised.

In the remainder of 2023 we propose to work with industry to reform the Open Networks Programme, by:

- Formalising its governance arrangements with greater ESO involvement, which would precede FSO leadership;
- Establishing an accelerated timeline with a clearer link to licence obligations, the ESO and DSO incentives and licence modifications where necessary;
- Reforming the Steering Group in a way that enhances its independence, powers and transparency and that strengthens its interaction with the Challenge Group; and
- Increasing the involvement of non-network parties to move away from DNO-centric groups.

In parallel we recommend Ofgem:

- Leverages the new DSO incentive and in particular its Performance Panel to ensure progress against the above. Ofgem should be confident that high powered incentives work based on evidence of how customer service and reliability have dramatically improved over RIIO-ED1;
  - Re-considers the mandating of legal separation of the DSO as UK Power Networks has pursued;
  - Sharpens the DSO incentive as part of RIIO-ED3 by increasing its value and making it symmetrical and by setting tougher targets by building on the learnings from RIIO-ED2; and
  - Increases its own engagement in Open Networks and explores with the Department for Energy Security and Net Zero how a new industry code arrangement could be applied to strengthen this work programme.
- **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.

We support Ofgem's proposal that DNOs will remain responsible for real time operations and keeping the lights on. This will enable us to build on our strong track record, which has involved reducing the number of customer interruptions by 18% and their length by 23% since 2015. Nevertheless, as set out in our RIIO-ED2 Business Plan we still see a need for a separate DSO control centre that focuses on the efficient dispatch of flexibility as without this there is a real risk that flexibility is not fully utilised.

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

We agree on the importance of producing an impact assessment to test the cost benefit of Ofgem's proposed reforms.

It is unclear how Ofgem can qualify its statement that their package of reform will contribute to "significant benefits" as there is not yet enough detail on what Ofgem is proposing and there is not yet an impact assessment in place. This highlights our concern that a decision has been put into motion that has not yet been costed and where the benefits have not been quantified.

It would also be important to identify the correct counterfactual. The RIIO-ED2 period will see an expansion of DSO activity and a progression of the Open Networks Programme in any case, alongside other reforms which should make network planning more predictable and boost the supply of flexibility – for example government decisions on district heat network zoning and on hydrogen for heat and reform of the retail energy market.

Nevertheless, we broadly agree that the “interacting organisations” model seems to be the most pragmatic choice. In our view this rests on the ability for industry to get on with delivering and addressing today’s challenges. It is also predicated on clear accountabilities that avoid cost duplication. This is where we recommend Ofgem focus their attention as it is currently unclear whether proposed reforms will avoid such duplication. For example, there are key aspects of market facilitation and network planning that are delivered by our DSO today, and which we will need to continue to deliver to meet our licence obligations and to avoid penalty in the DSO incentive. It is therefore important that the RSP and FSO builds on these responsibilities instead of replicating them. If for example Ofgem proposed to transfer responsibilities this would lead to a significant increase in implementation costs, which incidentally would increase public spending, which should be recognised.

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

We recently finished developing our RIIO-ED2 Business Plan that engaged over 19,000 people over a four year period, which culminated with an ambitious target to deliver over £400m of benefits in period by establishing a new DSO. As highlighted in figure 1 below the actual benefit of our DSO is over £1bn over the RIIO-ED2 period, once we account for flexible connections and the agility that the DSO provides, which is enabling us to maximise network utilisation and make use of uncertainty mechanisms to use up to date network data to release capacity as and when required.

If Ofgem is to pursue alternative arrangements that potentially remove or weaken the ability for us to fully deliver these benefits, it is then crucial that these are justified, in the context of figure 1, and we have the ability to comment on the assumptions used.

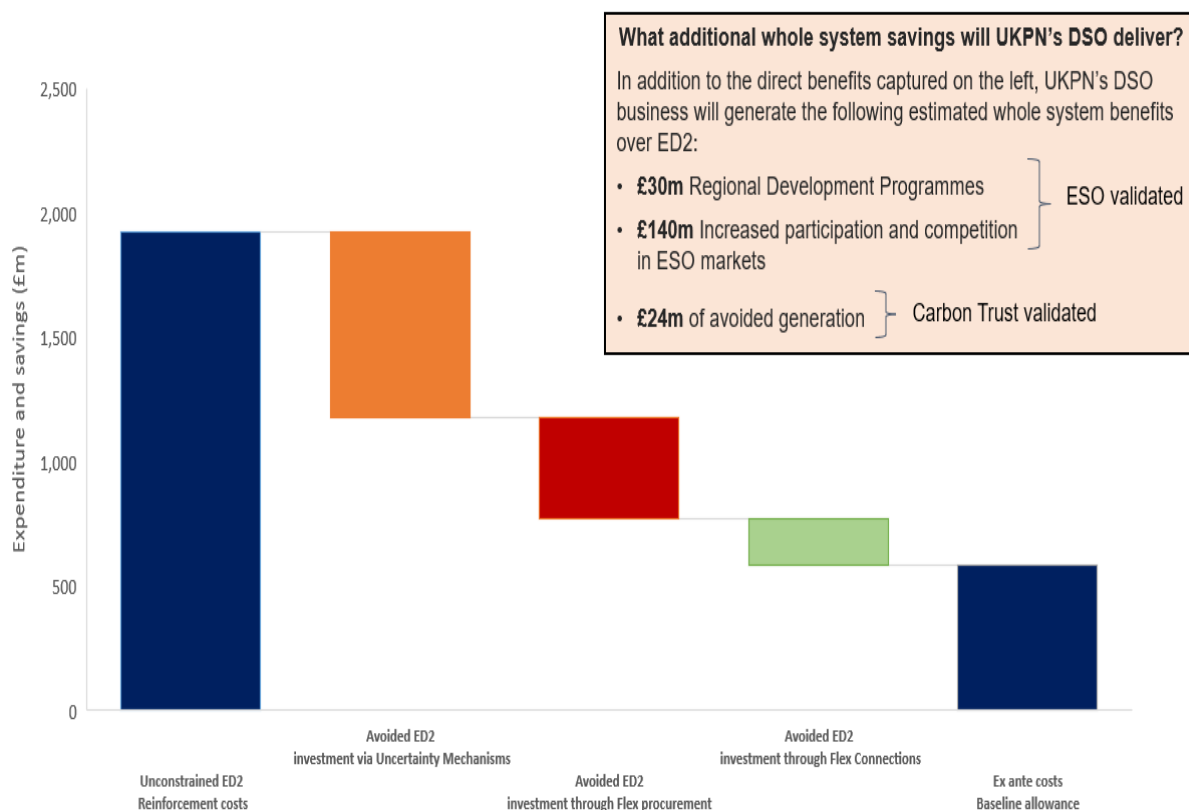


Figure 1: A summary of the cost benefit associated with UK Power Networks' DSO plan for RIIO-ED2

- **Q13. How should we attribute these benefits between the governance changes in the proposed option, and other changes required to achieve the 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.**

It is difficult to suggest how this could be done at this stage in the process as we need to see more detail from Ofgem on its proposed option and in parallel we need to further understand the wider reforms, of which there are many that have possible interactions and that are still in development. One area of overlap that we recommend Ofgem pay close attention to is the proposals being discussed under FSNR. For example it is noticeable that FSNR is potentially advocating a major programme of network reinforcement across electricity distribution as it is perceived that there is a low risk of asset stranding due to the electrification of heat and transport. We therefore question how compatible the FSNR objectives are with the benefits case being put forward here, which centres on increasing the procurement and use of local flexibility. The primary benefit of local flexibility is to defer or avoid network reinforcement, as such we advocate a holistic view on Ofgem's planned reforms.

- **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.**

Ofgem's start point should involve the amount of DSO related investment in the pipeline over RIIO-ED2, which is in excess of £1bn and links to the delivery of requirements set out by Ofgem. An evaluation should be undertaken into how much of this RIIO-ED2 expenditure would be affected by any new proposals. This should also consider the size of the DSO incentive that could lead up to an additional c.£250m of industry reward or £125m penalty depending on how licensees perform against Ofgem RIIO-ED2 targets.

The DSO incentive has just begun and the first performance report by Ofgem will not be published until autumn 2024. Ofgem are also yet to develop DSO KPI targets that form part of the overall assessment, which means that the first full DSO performance will not be known until autumn 2025. Given the overlapping costs and benefits with the themes captured in this consultation, it is imperative that Ofgem does not prejudge the outcome of the DSO incentive and waits until there is sufficient data to assess the progress that licensees are making.

- **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.**

As raised in our RFI response to Ofgem in 2022 this depends on the degree of separation pursued and the extent to which roles are integrated. We have advocated legal separation of the DSO from the DNO on the basis that it maintains strong synergies and single point accountability of network reliability, but because it also unlocks the benefits of flexibility by driving a culture change and creating clearer demarcation between responsibilities. Our view is that the three DSO roles covering market development, network planning and operations, as described by Ofgem, have



strong crossover and there would be a significant loss of accountability and optimisation if these roles were given to different parties. This explains why we have advocated for a thick DSO, which is distinct from both the FSO and the RSP function. However, we have not supported ownership separation of the DSO from the DNO as there has not yet been sufficient time to evaluate the benefits and credibility of legal separation. Nor is there any precedent that we are of around the world for doing this, but there would inevitably be a significant cost and risk if this was pursued.

It is also important that Ofgem considers the primary legislation associated with reforms and whether this will impede progress. This is particularly the case for establishing the RSP, which was not covered in the Energy Bill but that many stakeholders agree goes beyond energy networks. There is also a risk that the FSO timetable slips in parliament, which could undermine the changes being proposed. For example, it is unclear to us in such a scenario what the fallback option would be and what steps would be taken to avoid any investment hiatus. Furthermore, even when the FSO is established there is uncertainty around its funding level and the extent to which it will be able to undertake the breadth of responsibilities proposed.

## Appendix Two – Our understanding of overall, desired reform outcomes

