

Consultation

Market facilitator delivery body

Publication date: 13 December 2023

Response deadline: 7 February 2024

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We are consulting on the delivery body for the market facilitator role that we confirmed in our decision on the future of local energy institutions and governance, published on 15 November 2023.¹

This document outlines the scope, purpose, and questions of the consultation and how you can get involved. Once the consultation is closed, we will consider all responses. We want to be transparent in our consultations. We will publish the non-confidential responses we receive alongside a decision on next steps on our website at [ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations). If you want your response – in whole or in part – to be considered confidential, please tell us in your response and explain why. Please clearly mark the parts of your response that you consider to be confidential, and if possible, put the confidential material in separate appendices to your response.

¹ <https://www.ofgem.gov.uk/publications/decision-future-local-energy-institutions-and-governance>

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Executive Summary

To achieve the UK's net zero target by 2050, there must be significant reforms across the energy system. Radical transformation is underway in how we heat our homes, power our vehicles, and generate electricity. These changes will require significant shifts across electricity markets, which will mean changing how the market is operated for consumer benefit. It is vital that the energy system is smart, flexible and has well-facilitated accessible, transparent, and coordinated flexibility markets.

Market facilitation of flexible resources is a key activity to distribution system operation, critical to delivering this transition. It must be delivered by an institution with the right competence and skills, appropriately incentivised to contribute towards delivering net zero at pace and at least cost. There must be a change in how markets are facilitated to allow more transparency, coordination and joined up distribution and transmission market arrangements to unlock the full value of flexibility.

We published a Call for Input in April 2022² on the future of local energy institutions and governance. The responses validated our understanding of the key issues present in the governance arrangements for delivering activities critical to distribution system operation and demonstrated a strong case for change for reform to enable a smart, flexible energy system that will deliver a rapid low-cost net zero transition.

In the March 2023³ Consultation that followed, we proposed a package of reforms which included investing a market facilitator role in a single, expert entity, with a mandate to grow and develop local flexibility markets.

In consultation responses there was strong support for creating the market facilitator function. There was support for the Future System Operator (FSO) to take on the role and some respondents suggested Elexon as a viable option that should be considered.

We published our Decision on the future of local energy institutions and governance⁴ on 15 November 2023 confirming our intention to create a market facilitator. As we have not had substantive stakeholder input on Elexon's suitability, we think it is important to give an opportunity for stakeholders to provide views on which entity is best suited to take on the role: Elexon or the FSO.

Elexon is a strong option to take on the market facilitator role: its independence as well as its track record of delivering a substantive, robust, transparent change process means

² <https://www.ofgem.gov.uk/publications/call-input-future-local-energy-institutions-and-governance>

³ <https://www.ofgem.gov.uk/publications/consultation-future-local-energy-institutions-and-governance>

⁴ <https://www.ofgem.gov.uk/publications/decision-future-local-energy-institutions-and-governance>

it could be an effective market facilitator that could deliver the role in an inclusive and collaborative way.

The FSO is also a strong option: there are close synergies with its proposed role at the centre of the energy system and it will have relevant expertise (by virtue of its current role as the Electricity System Operator (ESO)). We also believe it would be well positioned to align distribution and transmission level flexibility market arrangements.

Elexon and the FSO are, therefore, both capable and viable options. In this consultation we explore the trade-offs and key considerations for both and give an initial appraisal of our proposals.

We are seeking stakeholder input and views on which entity has sufficient expertise and capability to deliver more accessible, transparent, and coordinated flexibility markets. We want to understand stakeholder priorities for the market facilitator delivery body, any concerns in relation to the two options and which one best meets the role requirements.

To ensure that the market facilitator delivers on our vision we also propose design principles. These represent the attributes the market facilitator should have and behaviours it should exhibit. We are seeking views on the design principles to help validate our thinking and to input into the development of the market facilitator.

After the consultation has closed we will consider responses and aim to make a decision in spring 2024. Our current thinking is that the market facilitator will be operational in late 2025 / early 2026, or sooner if possible.

1. Introduction

Section summary

This section sets out the background to the consultation, its purpose, what we are consulting on and how it fits into our wider review of local governance. It also introduces the subsequent sections, consultation stages, and explains how to respond to this consultation.

Context

- 1.1 As part of our legally binding target to reach net zero greenhouse gas emissions by 2050, the UK government has set an ambition to decarbonise the power sector by 2035. Meeting these targets will require radical changes across the energy system, including enabling a smart, flexible energy system.
- 1.2 There are three energy system functions that are critical to how distribution systems operate and ultimately transform: market facilitation of flexible resources, energy system planning, and real time operations. These functions must be performed by institutions with the competence, skillset, and incentives to drive net zero at least cost. Clear accountability and coordination are also essential to ensure that responsibilities are well defined and understood.
- 1.3 Decarbonisation and decentralisation are already changing the energy system and having suitable governance arrangements in place is critical to unlocking the full value of flexibility.
- 1.4 At a sub-national level, governance reform is needed to support the creation of accessible, transparent, and coordinated flexibility markets. At present, the institutional landscape is complex, and arrangements are not fit for purpose.

Our Call for Input and March Consultation

- 1.5 In April 2022, we launched a review into the effectiveness of institutional and governance arrangements at a sub-national level, through a Call for Input. The responses validated our understanding of the existing issues and demonstrated a strong case for change to governance arrangements.
- 1.6 Under current arrangements there is an absence of clear accountability and a lack of consistency in approaches between the DNOs. This is coupled with poor coordination between the local and national level, severely hindering the development of fair, transparent markets for procuring flexibility services.

- 1.7 This is causing unnecessary friction, which is making it increasingly difficult to unlock the full potential of flexibility for both consumers and the system. It is imperative these issues are addressed to unlock distributed flexibility at scale.
- 1.8 The current processes for how the market is facilitated are not providing confidence to participants that they can maximise the value they can provide, which risks less flexibility being incorporated into the system.
- 1.9 In March 2023, we published a Consultation (hereafter referred to as the "March Consultation") with a proposed package of reforms. For market facilitation of flexible resources, we proposed that a single entity with sufficient expertise and capability be assigned the role of market facilitator, with a mandate to grow and develop local flexibility markets.
- 1.10 We proposed that the FSO take on the market facilitator role in our March Consultation, in light of its existing expertise (as the ESO) and reflecting synergies with its current proposed role.

Consultation responses

We received 83 consultation responses to the future of local energy institutions and governance reform consultation (our March Consultation). There was strong support for our overall direction of travel, including creating a market facilitator.

Responses suggested that the FSO's existing market design expertise (as ESO) make it a good fit for the market facilitator role as it possesses most of the aspects required for this function.

Some responses raised concerns about the FSO's suitability for the market facilitator role. The main theme was a potential conflict of interest resulting from the FSO being a buyer of flexibility services. Respondents suggested that a clear remit, governance, rules, and transparency would be needed to overcome this concern.

A few responses suggested exploring Elexon as a viable option, given it is an independent entity.

Our November Decision

- 1.11 We published our Decision to the March Consultation on 15 November 2023 (hereafter referred to as 'our Decision') confirming our intention to create a market facilitator. We strongly believe that having a single, expert market

facilitator is essential to reduce friction across distribution markets and align distribution and transmission level market arrangements.

- 1.12 We emphasised that the market facilitator needs to be an independent expert body that can be held accountable for its decision-making and drive forward technical discussions at pace, through open, transparent, and participatory engagement.

What are we consulting on?

- 1.13 Following our Decision to assign a new market facilitator role to a single, expert entity, we are now consulting on which body is best suited to take on the role.
- 1.14 Respondents to our March Consultation expressed support for the FSO taking on the market facilitator role, while a few suggested Elexon as a viable option.
- 1.15 Since then, we have engaged with numerous stakeholders on the market facilitator design considerations. Our initial assessment is that Elexon is a credible candidate, however we have not had substantive stakeholder views on Elexon's suitability. As such we think it is important to provide an opportunity for stakeholders to input.
- 1.16 While some other options were also proposed in response to our March Consultation we do not believe they are viable, as such only Elexon and the FSO are in scope of this consultation.⁵
- 1.17 In this consultation we explore the extent to which Elexon and the FSO meet our design principles and are well placed to deliver effective governance. We are seeking input and views from stakeholders on which entity has sufficient expertise, competence, and capability to deliver more accessible, transparent, and coordinated flexibility markets. We also want to understand which characteristics and attributes are most important for the market facilitator delivery body and which option best meets the role requirements.
- 1.18 We do not explore detailed design arrangements for either Elexon or the FSO as we do not believe this is the key differentiator. Instead, we believe that how the delivery body demonstrates the market facilitator design principles is the key factor when deciding which entity to appoint. The detailed design work can then focus on the specific priority areas for the chosen delivery body.

⁵ These options that are listed in paragraph 4.17 in our November Decision. Suggestions included the Energy Systems Catapult, reforming current arrangements and selecting multiple parties to co-deliver via an open competition.

1.19 We intend to make a final decision in spring 2024.

Structure of the consultation

1.20 This consultation is structured as follows:

- Section 1 sets out the background to the consultation, including an outline of what we are consulting on and how it fits into our wider review into local governance.
- Section 2 sets out our vision for the market facilitator, including its role and key design characteristics.
- Section 3 explores the two delivery body options: Elexon and the FSO, including our key considerations when deciding on the market facilitator delivery body.
- Section 4 discusses the next steps following this publication, including that we intend to make a decision on the delivery body in spring 2024 ahead of the market facilitator going live in late 2025 / early 2026, or earlier if possible.

Consultation stages

1.21 This consultation was published on 13 December 2023, and will be open for nine weeks, with the closing date of 7 February 2024. Thereafter, we will review responses and intend to make a decision in spring 2024.

How to respond

1.22 We want to hear from anyone interested in this consultation. Please send your response to the person or team named on this document's front page.

1.23 We've asked for your feedback in each of the questions throughout. Please respond to each one as fully as you can.

1.24 We will publish non-confidential responses on our website at www.ofgem.gov.uk/consultations.

Your response, data and confidentiality

1.25 You can ask us to keep your response, or parts of your response, confidential. We will respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you want us to keep your response confidential, please clearly mark this on your response and explain why.

- 1.26 If you wish us to keep part of your response confidential, please clearly mark those parts you wish to be kept confidential and those that you don't. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information should be kept confidential, and which can be published. We might ask for reasons why.
- 1.27 If the information you give in your response contains personal data under the General Data Protection Regulation (Regulation (EU) 2016/679) as retained in domestic law following the UK's withdrawal from the European Union ("UK GDPR"), the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 4.
- 1.28 If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

General feedback

- 1.29 We believe that consultation is at the heart of good policy development. We welcome any comments about how we've run this consultation. We'd also like to get your answers to these questions:
- Do you have any comments about the overall process of this consultation?
 - Do you have any comments about its tone and content?
 - Was it easy to read and understand? Or could it have been better written?
 - Were its conclusions balanced?
 - Did it make reasoned recommendations for improvement?
 - Any further comments?

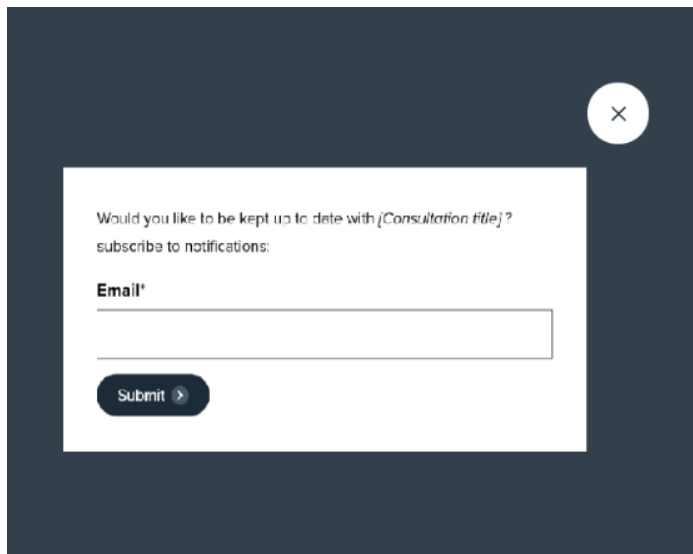
Please send any general feedback comments to stakeholders@ofgem.gov.uk

How to track the progress of the consultation

You can track the progress of a consultation from upcoming to decision status using the 'notify me' function on a consultation page when published on our website.

[Ofgem.gov.uk/consultations](https://www.ofgem.gov.uk/consultations)

Notify me +



A screenshot of a dark-themed notification subscription form. The form is contained within a dark blue rounded rectangle. At the top right of this rectangle is a white circle with a black 'x' icon. The form itself is a white rounded rectangle with the following text: "Would you like to be kept up to date with [Consultation title]?", "subscribe to notifications:", "Email*", and a text input field. Below the input field is a dark blue button with the text "Submit" and a right-pointing arrow.

Once subscribed to the notifications for a particular consultation, you will receive an email to notify you when it has changed status. Our consultation stages are:

Upcoming > Open > Closed (awaiting decision) > Closed (with decision)

2. Our vision for the market facilitator

Section summary

This section restates our vision for market facilitation alongside the market facilitator role, including its functions and activities. We also describe design principles for the market facilitator, detailing the attributes it should have and behaviours it should exhibit.

- 2.1 Our vision for market facilitation of flexible resources is for open and transparent markets that are not biased by the commercial interests of the buyer(s). We believe this is key to achieving the scale of flexibility needed and ensuring the most efficient solution for the energy system can be found. This includes using both demand side and local generation (including storage) flexibility, which is imperative in meeting the scale of the decarbonisation challenge.
- 2.2 Governance arrangements must ensure there are fair and transparent rules and processes for procuring flexibility services, that enable service providers to participate easily in open, transparent, and coordinated markets. Smaller scale assets ("distributed flexibility") must also be able to participate on a level playing field with larger assets.
- 2.3 These processes should be standardised to reduce friction for market participants and there should be clear accountability for delivering this. There should be easy access to accurate and user-friendly market information that allows providers to respond to system needs.
- 2.4 This enhanced simplicity for market participation should support opportunities to easily stack revenue, leading to increased participation and liquidity within the market for balancing services (where flexibility's value is highest). This should keep system costs down and support the delivery of a cost effective net zero energy system.
- 2.5 The governance arrangements for market facilitation should also support open, coordinated markets that mesh smoothly across electricity distribution and transmission networks.
- 2.6 This vision for market facilitation underpins the market facilitator role and design principles we set out below.

The market facilitator role

- 2.7 To meet its objectives and to deliver on our vision for market facilitation of flexible resources there are a number of key functions and activities that the market facilitator will need to perform.
- 2.8 The market facilitator will be empowered and responsible for delivering standardised, easily accessible, and transparent DSO markets. It will also be responsible for aligning ESO and DSO market arrangements.
- 2.9 It will have a mandate to grow and develop local flexibility markets and ensure processes are standardised to reduce friction for market participants, with both small and larger assets, leading to increased participation and liquidity.
- 2.10 To do so, the market facilitator will need to be an independent, expert body that can be held accountable for its decision-making and deliver at pace through open, transparent, and participatory engagement with DNOs, the FSO, and market participants.
- 2.11 We intend to require relevant licensees to adopt the outputs specified by the market facilitator through changes to their licences.
- 2.12 In our Decision, we set out three functions that the market facilitator will perform: strategic leadership, market coordination, and implementation monitoring. Table 1 below sets out the functions and potential associated activities of the market facilitator. These functions and activities build on the roles and responsibilities we proposed in the March Consultation.

Table 1 - Market facilitator functions and activities

Function	Potential activities
Strategic leadership	<ul style="list-style-type: none"> • Translate Ofgem and the Department for Energy Security and Net Zero's (DESNZ's) vision for local flexibility markets into a market coordination delivery plan. • Monitor developments across policy, regulation, innovation, and energy markets and proactively identify upcoming challenges, opportunities and risks that may require intervention. • Identify if changes are required to the market facilitator's functions, engaging with Ofgem where necessary to update roles and responsibilities. • Provide advice to government and Ofgem where regulatory or policy gaps are identified or where there is a need for joining-up and coordination.
Market coordination	<ul style="list-style-type: none"> • Propose and manage changes to the processes, rules, and standards in a transparent and collaborative way. • Facilitate open, participative discussions with wide stakeholder representation as part of the change management process. • Decision-making on processes, rules, and standards. • Develop and publish a delivery plan and implementation timetable, identifying the deliverables required for standardised, transparent, and coordinated local flexibility markets and for alignment with transmission flexibility market arrangements. • Commission or undertake market and technical research, analysis or modelling.
Implementation monitoring	<ul style="list-style-type: none"> • Monitor whether and how the agreed processes, rules, and standards are adopted to ensure they are implemented on time and as intended. • Report implementation issues to Ofgem which will assess whether compliance and enforcement action are required. • Assess how the new processes, rules, and standards work in practice, creating a feedback loop to the market coordination function where issues or potential improvements are identified.

2.13 The functions and activities in Table 1 are provided to illustrate the scope and parameters of the market facilitator as well as provide clarity on its roles and responsibilities. However, they could evolve further as we advance with our detailed design work.

2.14 The market facilitator will be responsible for identifying how to realise our vision of local flexibility markets in practice, which will be set out in a delivery plan with an implementation timetable. While the starting point for the market facilitator's role is local flexibility, we also want it to drive alignment between transmission and distribution market arrangements. This is a critical objective of the reformed governance arrangements and achieving more coordinated, accessible flexibility markets. This would have implications for the relationship between Elexon and the FSO if Elexon was appointed to the market facilitator role, and would need to be considered as part of the next steps.

- 2.15 We expect the market facilitator will consult on and publish the delivery plan, supporting transparency and scrutiny. We will consider the frequency with which the delivery plan is refreshed as part of our detailed design work.
- 2.16 In the delivery plan, the market facilitator will set out its areas of focus including the specific rules, processes, and standards that need creating or updating. Although much of this work is currently being undertaken through Open Networks, under the new arrangements the market facilitator will be responsible for delivery. We intend to work closely with the ENA, DNOs, the ESO, DESNZ and other Open Networks participants to ensure a smooth transition, as explored in Chapter 4.
- 2.17 A key element of the market facilitator's role is that it will be empowered to be a decision-maker. We believe this is essential to ensure a single body is accountable and can deliver at pace. Ofgem and government's role will be to shape the strategy for flexibility markets. Ofgem will also be responsible for oversight, compliance, and enforcement, however we will not be an active decision-maker on the specific rules, processes, and standards.

Market facilitator design principles

- 2.18 To ensure the market facilitator delivers our vision for market facilitation, we have defined some key design principles which build on the thinking we set out in our review's previous publications.⁶ We welcome views on whether you agree with these design principles, including whether you believe additions or changes are required.
- 2.19 The design principles represent the attributes the market facilitator should have and behaviours it should exhibit. They offer a lens through which to evaluate the merits of the delivery body options and help understand whether Elexon or the FSO are better suited for the market facilitator role, as explored in Chapter 3.
- 2.20 We will also use these design principles to underpin the governance arrangements and processes we develop as part of the detailed design work, which is described in Chapter 4.
- 2.21 The criteria listed below are provided in alphabetic order without weightings, however we welcome views on which design principles, if any, should be prioritised.

⁶ The term 'our review's previous publications' refers to our Consultation and Decision published in March 2023 and November 2023 respectively.

Proposed market facilitator design principles

- 2.22 **Accountable** - the market facilitator must take ownership of its decisions and actions. The delivery body's institutional arrangements should be aligned with the market facilitator's remit, with the right incentives and drivers to fulfil its functions effectively. As the market facilitator will be responsible for delivering Ofgem and DESNZ's vision for local flexibility it is essential there are clear mechanisms in place so the market facilitator can be held to account.
- 2.23 **Agile** - an agile approach to delivery, an ability to quickly adjust its approach and activities in response to the changing needs of the energy system and market are essential attributes for the market facilitator. This goes hand in hand with delivery at pace and is an important attribute for the market facilitator.
- 2.24 **Delivery at pace** - the market facilitator will be expected to deliver at pace, and to enable this it will be empowered to make decisions and progress tangible outputs and results. A key issue with current arrangements is a lack of clear accountability for decision-making. The market facilitator must be an empowered decision-maker, confident in making decisions at pace and acting decisively to deliver on the vision for market facilitation of flexible resources and unlock the benefits of flexibility at scale. We see this as being key for delivery at pace.
- 2.25 **Expert and strategic** - the market facilitator's approach, work programme, and decisions will need to reflect the latest developments in the complex and fast changing energy sector. The market facilitator will need to be strategic and proactive to both identify and then manage current and future risks, opportunities, and interdependencies. We believe that the delivery body will need to have strong flexibility and market design expertise to ensure it fully understands the complexities and interdependencies across the policy, regulation, and energy market landscape.
- 2.26 **Impartial** - To maintain industry's trust and confidence, the market facilitator must act and be seen to be acting objectively. It must take a whole system approach to guide its decision-making, acting impartially in the best interests of consumers.
- 2.27 **Inclusive and collaborative** - to inform its decision-making the market facilitator will need to actively seek to build collective buy-in for its actions and decisions. It will need to take a collaborative approach, undertaking open and wide regular stakeholder engagement. This is essential to ensure the rules, standards, and processes it develops are fit for purpose, reflect stakeholder and customer needs and contribute towards growing local flexibility markets.

- 2.28 **Transparent** - to build trust in the decision-making process, the market facilitator will need to be transparent in its actions and decisions. It will need to clearly document its decision-making processes and outcomes, enabling effective scrutiny, and ensure that all outputs are easily accessible for all.

Wider considerations

- 2.29 In addition to the design principles there are two wider considerations for the market facilitator that we believe will be key to maximising the benefits it can deliver.
- 2.30 The first consideration is the ability to drive alignment between transmission and distribution market arrangements. We believe this is a key part of unlocking the full value of flexibility and therefore an important consideration when deciding which body is best placed to take on the market facilitator role.
- 2.31 The second consideration is the ease of implementation and enabling a smooth transition. In other words, the speed and ease to get the market facilitator operational. We believe this is important to avoid a hiatus and ensure the benefits of the reform are unlocked as soon as possible.

Questions

- Q1. Do you agree with the proposed market facilitator design principles (in paragraphs 2.22 - 2.28)? If not, what additions or changes do you suggest?
- Q2. Do you think some of the design principles are more important than others? If so, which should we attach greater weight to?
- Q3. How important is it for the market facilitator to be able to align transmission and distribution flexibility market arrangements? Why?
- Q4. How important is ease of implementation and enabling a smooth transition when considering the market facilitator delivery body? Why?

3. Delivery body options

Section summary

This section discusses the delivery body options, details of their implementation, design principles, and other considerations.

- 3.1 We are considering two options to take on the market facilitator role: Elexon and the FSO.
- 3.2 We proposed the FSO as an option for the market facilitator role in our March Consultation, where we also requested views on its suitability, while Elexon was suggested as an option by some respondents in consultation responses.
- 3.3 We believe both options are credible and in this section we discuss their suitability in relation to our design principles and the two wider considerations, as set out paragraphs 2.30 and 2.31.

Option 1: Elexon

Introduction

- 3.4 Elexon was suggested in response to our March Consultation. We have since explored the practicalities of appointing and regulating Elexon, and believe it is a credible option that offers both advantages and disadvantages relative to the FSO, as we explore below.
- 3.5 Elexon is the Balancing and Settlement Code Company (BSCCo).⁷ It is the Code Administrator for the Balancing and Settlement Code (BSC), oversees the day-to-day management of the BSC arrangements, and carries out several other additional roles, as explained in Appendix 1.

Implementation and enduring arrangements

- 3.6 Elexon is not a licensed entity and therefore has a different relationship with Ofgem as it is not directly regulated, unlike the FSO. The activities that Elexon is permitted to undertake are outlined in the BSC.⁸ As such, for Elexon to take on the market facilitator role the BSC would need to be modified, extending Elexon's

⁷ The BSC refers to Elexon as BSCCo. It is used throughout this document with the same meaning as Elexon.

⁸ Section C 'BSCCo and its Subsidiaries': <https://bscdocs.elexon.co.uk/bsc/bsc-section-c-bscco-and-its-subsidiaries>

remit to include the market facilitator role before further design and development work is undertaken.⁹

- 3.7 As Ofgem can only raise BSC modification proposals under specific circumstances, which do not apply here,¹⁰ an entitled party would need to raise this initial enabling modification proposal on our behalf were Elexon to be appointed.
- 3.8 A second modification would then be needed for the detailed market facilitator arrangements, including the model for governance, funding, and operation. This would be led by Elexon with industry but with Ofgem involvement. This modification would also need to be raised by an entitled party and progressed through the BSC change process before being submitted to Ofgem for approval. This BSC modification proposal may be preceded by a BSC issue group if necessary.
- 3.9 This process (from raising an enabling BSC modification proposal, setting up and running the issue group (if required), then raising a second BSC modification proposal through to Ofgem decision and then implementation), can be lengthy due to the required governance process and need for stakeholder engagement and solution development. It does, however, provide significant opportunities for stakeholder input.
- 3.10 Elexon is a not for profit, independent entity delivering key energy system functions. It is not a procurer of flexibility and does not participate in the markets that the market facilitator will be responsible for, and its overarching institutional arrangements are well aligned with taking on the market facilitator role. If appointed, Elexon would have a clear mandate to grow and develop local flexibility markets as the market facilitator with appropriate drivers to deliver effectively.
- 3.11 As noted in Chapter 2, the market facilitator will be responsible for delivering aspects of Ofgem and DESNZ's vision for local flexibility, so it is important that the delivery body can be held to account. To do so, we would produce a market

⁹ The powers for Elexon to extend their own vires established under [P390 'Allowing extensions to Elexon's business and activities, subject to additional conditions'](#) would not apply here as those powers relate to where Elexon seeks to tender for a new role. In respect of the current scenario, we would be assessing and then appointing (should Elexon be chosen), not tendering for the market facilitator delivery body.

¹⁰ Ofgem can only raise a modification proposal in two situations: (i) where it reasonably considers the modifications are necessary to comply with or implement the Electricity Regulation and/or any relevant legally binding decisions of the European Commission and/or the Agency; and/or (ii) the modification proposal is in respect of a Significant Code Review (SCR). However, neither of these situations are applicable here. We do not consider the modifications to meet the requirements of (i) as they do not relate to compliance with the matters mentioned. In respect of (ii), our local governance policy reforms are not being developed under a SCR, so this is also not applicable.

facilitator governance framework document similar to that in place for Elexon's role in delivering the Market-wide Half Hourly Settlement (MHHS) Programme.¹¹ We have explored and discounted other governance models for the market facilitator as they are not applicable.^{12 13}

- 3.12 The framework document would set out the governance structure, Elexon's roles and responsibilities and the processes for monitoring Elexon's performance, including regular reporting to Ofgem and under what circumstances Ofgem can intervene. It would also outline Elexon's responsibilities as market facilitator.
- 3.13 For the MHHS Programme, the governance document sets out that Elexon is empowered and obliged to deliver MHHS implementation and cannot rely on Ofgem to step-in. An ultimate last resort sanction is that Ofgem can appoint another delivery body if performance and delivery was consistently below expectations.
- 3.14 The MHHS governance framework is established under BSC Section C12¹⁴ and compliance with the document is required under the BSC. Should Elexon be appointed to the market facilitator role, we would look to ensure there is a similar relationship between the market facilitator governance framework document and the BSC to ensure Elexon's compliance.

Option assessment

- 3.15 Elexon meets many of the design principles outlined in Chapter 2 while representing a different proposition to the FSO. We discuss Elexon's suitability to meet the market facilitator design principles below. For presentation purposes we start with the design principles we consider each institution best meets. We then discuss the two wider considerations.
- 3.16 **Impartial** - As Elexon does not directly participate in ESO or DSO flexibility markets there is no risk or perception of bias. While Elexon's ownership is changing with the creation of the FSO, as explored in Appendix 1, Elexon will remain fully operationally independent. We are therefore confident in Elexon's

¹¹ <https://www.ofgem.gov.uk/publications/decision-designation-market-wide-half-hourly-settlement-governance-framework>

¹² See Appendix 1 for an overview of the interaction with Energy Code Governance Reform.

¹³ For the EMR Settlement activity, there are contractual arrangements in place between Elexon and both the Low Carbon Contracts Company and the Electricity Settlements Company for the provision of settlement services. This model would not be applicable for the market facilitator delivery body, as this role would not be performed under a contract, however it does demonstrate how Elexon can be held accountable.

¹⁴ <https://bscdocs.elexon.co.uk/bsc/bsc-section-c-bscco-and-its-subsidiaries#section-c-12>

independence and that it could deliver the market facilitator role impartially if appointed.

- 3.17 **Transparent** - We are also confident that Elexon would dispense its market facilitator duties in an open and transparent manner if appointed. Elexon is well regarded as an effective and competent delivery body in administering the BSC, delivering a robust and transparent change process.
- 3.18 **Inclusive and collaborative** - We believe that Elexon, if appointed, would be well suited to deliver the market facilitator activities in an inclusive and collaborative way. It has a strong record in this regard and scores highly in stakeholder surveys,¹⁵ indicating competencies in this area.
- 3.19 **Agile** - Elexon has taken on new roles in recent years, as explored in Appendix 1, suggesting its structure and delivery model are adaptable and allow it to accommodate new roles and responsibilities. This indicates it may be well placed to deliver in an agile way if appointed. That said, market facilitation would be a new subject matter for Elexon, which it would have to develop new expertise in, whereas its other roles predominately relate to settlement.
- 3.20 **Delivery at pace** - The market facilitator may need to take decisions and interventions to help grow and develop local flexibility markets at pace. The delivery body will therefore need to develop deep subject matter expertise to be able to assess stakeholder views objectively before taking decisive action to deliver our strategic vision for local flexibility markets. Elexon is required to lead on complex issues and projects¹⁶ as part of its existing roles but would need to build local flexibility market subject matter expertise if appointed.
- 3.21 **Expert and strategic** - Elexon's most substantive roles relate to code administration, settlement and scheme administration.¹⁷ Its core expertise and competency therefore relate to these areas. The market facilitator role will require the delivery body to track and manage complex interdependencies across areas of policy, regulation, and markets. Elexon has demonstrable expertise across these areas, although it would have to further develop its subject matter

¹⁵ The most recent code administrator survey was undertaken in 2021:

<https://www.ofgem.gov.uk/publications/code-administrators-performance-survey-findings-2021>

¹⁶ For instance Project TERRE (P344) and EMR Settlement were both complex issues that required Elexon to take a leadership role.

¹⁷ This includes administering and running the BSC, providing settlement services in respect of Contracts for Difference and the Capacity Market, implementation manager for MHHS and administering EPG and EBDS, among others. See Appendix 1 for more details.

knowledge to ensure it can take a leadership role across local flexibility if appointed.

- 3.22 **Accountable** - As an independent, not for profit, and trusted body with clearly set out roles and responsibilities, Elexon would have a clear mandate to deliver. However, holding Elexon to account may be more challenging than if it was licensed. While a governance framework document, as is in place for MHHS implementation, would enable us to clearly set out Elexon's roles and responsibilities and processes for regular reporting to Ofgem, as an unlicensed entity there will be fewer levers to hold Elexon to account short of the last resort of removing the role from Elexon if it significantly underperformed.¹⁸ As such, if we decided to appoint Elexon the governance framework would need to be an important area to focus on as part of the next steps.
- 3.23 **Implementation and transition** - Appointing Elexon to the market facilitator role is reliant on a third party raising a modification proposal and the timeline is determined by the BSC Panel, on recommendation from Elexon, and is therefore out of our control. This introduces greater risk into the process and could result in delays to appointing and setting up the market facilitator role.
- 3.24 When thinking about transition arrangements, while Elexon participates in Open Networks it does not currently sit on the Steering Group and is less involved than the ESO in the technical working groups and overall delivery.¹⁹ This could make it harder and take longer for Elexon, if appointed, to take a substantive leadership role ahead of formally becoming the market facilitator.
- 3.25 Overall, there are therefore some challenges to appointing and getting the market facilitator set up for Elexon if appointed.
- 3.26 **Aligning transmission and distribution arrangements** - We also believe that aligning transmission and distribution market arrangements could be challenging for Elexon to deliver as the market facilitator. If appointed, the separation of responsibilities between the FSO and Elexon, responsible for transmission and distribution respectively, would make it harder to coordinate and drive alignment. This would therefore need to be an important area of focus as part of the next steps.

¹⁸ While the contractual arrangement option exists, as used for EMR settlement activity, as explored in Footnote 13, we do not believe this is a viable option for the market facilitator role.

¹⁹ Elexon is a member of the Open Networks Challenge Group which is a mix of flexibility service providers and stakeholders: <https://www.energynetworks.org/assets/images/Publications/2023/230818-open-networks-challenge-group-membership-list.pdf?1701860484>

Option 2: the FSO

Introduction

- 3.27 The FSO will be a new body established by the Energy Act 2023²⁰ (Energy Act) which we aim to be operational in 2024, depending on a number of factors including discussing timelines with key parties. The FSO will take on all existing roles from the Electricity System Operator (ESO) and the longer-term planning, forecasting and market strategy functions in respect of gas (but not real-time gas system operation or Network Emergency Coordinator functions).²¹
- 3.28 Given this central role in the energy system and because of its existing market design expertise (as the ESO) we proposed the FSO as our lead option to take on the market facilitator role in our March Consultation.
- 3.29 Respondents recognised our rationale, agreeing that it was a logical option, however concerns around the FSO's suitability were also raised, particularly in relation to impartiality. Respondents suggested that a clear remit, governance, rules, and transparency will be needed to overcome this, which we discuss below.
- 3.30 In Appendix 1 we provide more detailed information on the FSO, including the background to its creation, its remit, and a summary of recent publications.

Implementation and enduring arrangements

- 3.31 Once designated, the FSO will be a licensed public sector body at the centre of the energy system, with a whole system perspective to deliver in the best interests of consumers.
- 3.32 Amongst other statutory duties, the FSO will have statutory duties to carry out its functions in the way that it considers is best calculated to promote objectives relating to net zero, security of supply and efficiency and economy. It will also have a statutory duty, when carrying out its functions, to have regard to the whole-system impact of a relevant activity (as defined in the Energy Act).²² As such, we believe these overarching duties of the FSO are well aligned with effective delivery of the market facilitator activities.

²⁰ <https://www.legislation.gov.uk/ukpga/2023/52/contents/enacted>

²¹ <https://www.ofgem.gov.uk/publications/consultation-proposals-future-system-operator-role>

²² In addition to having regard to the whole system impact, the FSO will also have statutory duties, when carrying out its functions, to have regard to facilitating competition between persons carrying out relevant activities (note there is an exception to this duty, see s164(1)(a) of the Energy Act), consumer impact of a relevant activity, and the desirability of facilitating innovation in relation to the carrying out of relevant activities.

- 3.33 In practice, if chosen for the market facilitator role we would set out the roles and responsibilities in the FSO's licence(s) and in the relevant governance documents (eg guidance documents). This would define the new market facilitator role in detail, including setting out our expectations alongside any specific reporting and governance requirements for the market facilitator role.
- 3.34 Embedding the market facilitator role in the overarching FSO regulatory framework in this way would provide us with the tools to ensure there is a clear remit, governance, rules, and transparency, as called for in responses to our March Consultation.

Option assessment

- 3.35 We believe that the FSO would be well placed to meet many of the market facilitator design principles if appointed to the market facilitator role. We discuss this below. As noted above, for presentation purposes we start with the design principles we consider each institution best meets. We then discuss the two wider considerations.
- 3.36 **Expert and strategic** - The creation of the FSO will build upon the capabilities and functions of the ESO, encompassing the ESO's existing flexibility market and market design expertise, while adding new strategic, longer-term gas forecasting, market, and planning roles. The FSO will be tasked with taking a strategic, whole system approach to the energy system, including having regard to DESNZ's Strategic Policy Statement (SPS), and it will hold several strategic roles. Its role at the centre of the energy system, with a whole system remit set out in the FSO's licences, mean it would be well placed to take a strategic approach to delivering the market facilitator activities and effectively identify and manage relevant challenges, opportunities, risks, and interdependencies if appointed.
- 3.37 **Accountable** - The FSO is being set up as a technically expert and operationally excellent entity that is accountable to consumers, able to support the delivery of net zero on behalf of the public. As noted above, the FSO will have a statutory duty to have regard for consumer and whole-system impacts, among others. We are therefore confident that, if appointed, the FSO's overarching objectives and duties would be well aligned with effective delivery of the market facilitator role and its mandate to grow and develop local flexibility markets.
- 3.38 In addition, as explained in paragraphs 3.33 and 3.34, as a licensed body, there would be a robust and established framework to monitor the FSO's performance and hold it to account, including through licence conditions associated with the market facilitator role.

- 3.39 **Delivery at pace** - The FSO will be taking on roles across network planning, including gas strategic planning and Central Strategic Network Planning,²³ meaning it will provide expert advice on wide-ranging topics. Based on its roles, we are confident it would be comfortable making decisions for market coordination as part of the market facilitator role, which would be important for delivery at pace. The ESO already makes decisions as part of its market development and transactions role,²⁴ however we recognise that there have been some concerns about pace of delivery in the past. Overall, however, with a clear mandate, combined with the right skills and competencies, we are confident the FSO would be able to deliver at pace but recognise that we will need to work with the FSO as part of the next steps to address any historic issues.
- 3.40 **Transparent** - Our vision is for the FSO to be a trusted body, that is accountable to consumers via its licensing obligations. Building this level of trust will require high levels of transparency which we would expect to see from the FSO. We are therefore confident that, if appointed, the institutional design of the FSO, combined with how the market facilitator role will be defined, could deliver transparency in respect of the market facilitator role. In addition, should the FSO be appointed to the market facilitator role, we would consider whether specific provisions are required for the market facilitator role to deliver the required level of transparency.
- 3.41 **Agile** - We recognise that as a large organisation with wide-ranging roles it may be more difficult for the FSO to be as agile in its delivery compared to a smaller, more narrowly focused organisation. As such it would be an important area to consider as part of next steps. That said, given the breadth of expertise the FSO will have and its wide remit we believe it would be well placed to take on additional, related activities in future, offering optionality for the future.
- 3.42 **Inclusive and collaborative** - We believe that inclusivity and collaboration would need to be an area of focus for the FSO, if appointed, as the ESO has a mixed track record in this regard. For instance, when assessing the ESO's performance for the market development and transactions role in 2021-2023, known as Business Plan 1, while the ESO met our expectations on stakeholder evidence overall we noted dissatisfaction in several areas. This included on

²³ <https://www.ofgem.gov.uk/publications/centralised-strategic-network-plan-consultation-framework-identifying-and-assessing-transmission-investment-options>

²⁴ <https://www.ofgem.gov.uk/publications/decision-eso-roles-guidance-2023-2025>

balancing services development, where the ESO could have done better on communication and providing clarity around reasons for change and delays.²⁵

- 3.43 As such, if appointed, we would need to work with the ESO / FSO and wider stakeholders to ensure stakeholder engagement processes are developed to allow clear communication of rationale behind market design choices, especially where this might not reflect the views of stakeholders but is in consumer interest.
- 3.44 **Impartial** - The FSO is being established as an expert and impartial body in public ownership. Along with government, we have made it clear that the FSO must be independent, not only of other commercial energy interests, but also from the day-to-day operational control of government. This is at the heart of the FSO's creation and is underpinned by its objectives and duties, as discussed in paragraph 3.32.
- 3.45 That said, we recognise that the FSO being responsible for setting the processes, rules and standards for both distribution and transmission markets, while also procuring flexibility, is a concern for many stakeholders.
- 3.46 As an independent and not for profit body, the FSO will not have an incentive to favour transmission over distribution. However, we are aware of the risk of an implicit bias based on its previous organisational role (as a transmission focussed organisation). This was an area of concern in consultation responses and would be a key area of focus for us as part of our next steps should we decide to appoint the FSO as the delivery body.
- 3.47 To address this, if appointed, we would work with the FSO and industry to put in place governance arrangements and reporting requirements which enable robust scrutiny, prioritise transparency in decision-making and garner trust. We would also expect the FSO to proactively work with stakeholders on an ongoing basis to review and improve its processes and governance to maintain industry confidence.
- 3.48 Equally, we appreciate that the FSO being responsible for implementation monitoring could be perceived as the FSO "marking its own homework". There are options to mitigate this risk, for instance by requiring the FSO to commission an independent third party to collect this information on its behalf, in the same way that surveys are conducted for the ESO incentive today. We would consider this as part of our next steps.

²⁵ <https://www.ofgem.gov.uk/publications/end-scheme-decision-electricity-system-operators-performance-2021-2023>

- 3.49 **Aligning transmission and distribution arrangements** - Transmission and distribution market arrangements need to be better aligned. There needs to be greater coordination between system operators to unlock the full value of flexibility and deliver a smart, flexible energy system.
- 3.50 We believe that having transmission and distribution arrangements within one institution's accountability will support that outcome: reducing the amount of separation and required coordination could make it easier for the market facilitator to drive alignment. As the FSO will be responsible for transmission market arrangements we believe it could be well placed to drive alignment between transmission and distribution.
- 3.51 **Implementation and transition** - Another important consideration is the ease of implementation and ensuring a smooth transition. As outlined above, appointing the FSO to the market facilitator role would involve changing the FSO's Electricity System Operator licence which Ofgem can do alongside the detailed design work.²⁶ When considering transition arrangements, as the ESO is already embedded within Open Networks we believe it could be well placed to take a more central role ahead of formally becoming the market facilitator.
- 3.52 Overall, establishing the FSO as the market facilitator would be an Ofgem-led process, which grants us some control over timescales. We also believe disruption could be minimised due to the ESO's existing role within Open Networks.

Conclusion

- 3.53 We believe that both Elexon and the FSO are credible candidates that meet many of our design principles, however as can be seen from the above, they represent fundamentally different propositions for the market facilitator role.
- 3.54 A key difference between the delivery bodies relates to aligning transmission and distribution flexibility market arrangements. Another difference is the relationship the market facilitator would have with Ofgem as a result of the different regulatory tools that would apply to Elexon and the FSO, as explored above.
- 3.55 In our March Consultation we proposed the FSO as our lead option as we expect it to have the required ambition and strategic vision. We suggested there were close synergies with its current proposed role. We also highlighted its relevant

²⁶ By virtue of s11A of the Electricity Act 1989.

expertise and that it can be held to account. Finally, we flagged that it would be well positioned to align distribution and transmission markets.

- 3.56 We believe the FSO remains a strong candidate for these reasons. We do however recognise that a clear remit, governance, rules, and transparency would need to be embedded into the regulatory framework to address stakeholder concerns.
- 3.57 Elexon is also a strong option to take on the market facilitator role. Its independence as well as its track record means it could be an effective market facilitator that could deliver the role in a transparent, inclusive, and collaborative way, building on its existing competencies.
- 3.58 If it took on the market facilitator role, Elexon would need to grow its market design expertise as well as develop clear mechanisms for effective collaboration with the FSO and DNOs to enable effective alignment between transmission and distribution market arrangements.

Questions

Q5. Do you agree with our assessment of Elexon's suitability for the market facilitator role? If not, why not?

Q6. Do you agree with our assessment of the FSO's suitability for the market facilitator role? If not, why not?

Q7. Do you believe Elexon or the FSO is better suited to take on the market facilitator role when considering the design principles and wider considerations?

4. Next steps

Section summary

This section summarises our next steps towards an intended decision in spring 2024.

- 4.1 This consultation will be open for nine weeks and will close on the 7 February 2024. We encourage responses from all interested stakeholders.
- 4.2 We will analyse stakeholder responses and carry out stakeholder engagement and working groups, if needed. We then intend to make a final decision on assigning the market facilitator role in spring 2024.
- 4.3 Following publication of the decision document, the work will enter its implementation phase. Detailed next steps will depend on the conclusions we reach and will be outlined in our decision document.
- 4.4 We intend to work with the relevant organisation and wider stakeholders on the detailed design of the market facilitator's role and implement a transition plan. At a minimum, a statutory consultation on licence modifications will be required.²⁷
- 4.5 Ofgem will continue to lead, be involved, and work closely with the chosen delivery body to co-develop proposals where required while remaining the decision maker on the market facilitator role and associated governance. Ofgem's involvement will ensure the market facilitator and detailed arrangements are fit for purpose and meet our vision for market facilitation.
- 4.6 As we move from the current arrangements to the new market facilitator arrangements, we intend to work with the chosen delivery body, DESNZ, the ENA, DNOs and the ESO to ensure a smooth transition. This work will take place over the course of 2024 and 2025 and be aimed at facilitating the transition to our longer-term arrangements, for instance by ensuring that Open Networks outputs are easily transferrable to the market facilitator to prevent a hiatus in activity - a key principle in our open letter.²⁸
- 4.7 We expect Open Networks to continue to deliver during the transition arrangements and see no reason for the creation of the market facilitator to impede progress.

²⁷ At the very least, we believe the licence modifications required will be to add conditions to relevant licences to oblige relevant licensees to adhere to the processes, rules and standards set by the market facilitator. Dependent on the delivery body appointed, modifications to the FSO's licence(s) may also be required.

²⁸ <https://www.ofgem.gov.uk/publications/open-letter-open-networks-project>

- 4.8 We are aware of significant overlaps between the creation of the market facilitator role and the future of distributed flexibility workstream, including in relation to the steps outlined above. We are working closely to ensure alignment between the two workstreams.
- 4.9 We intend for the market facilitator to go live by late 2025 / early 2026, or sooner if possible.

Appendices

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Appendix 1 – Background information

Elxon overview

- A1.1 Elxon is the Balancing and Settlement Code Company (BSCCo) and its primary functions are Code Administrator for the Balancing and Settlement Code (BSC) and central systems delivery body for the BSC, which enable it to oversee the day-to-day management of the BSC arrangements. The BSC is a legal document which defines the rules and governance for the Balancing Mechanism (BM) and imbalance settlement processes in the Great Britain (GB) electricity market. There is a requirement in Condition C3 of the Transmission Licence²⁹ for a BSC to be in place at all times.
- A1.2 The BSC is governed by the BSC Panel which consists of industry experts and consumer representatives, who also ensure that all BSC Parties comply with the code's rules. They assess, consult, and decide on BSC modification proposals. Proposals which are material and do not meet self-governance criteria (eg typographical errors, correcting out-of-date references, etc) are sent to Ofgem for decision. The decision as to whether to approve or reject³⁰ a BSC modification proposal is assessed³¹ against the Applicable BSC Objectives,³² set out in Condition C3 of the Transmission Licence, Ofgem's principal objective and other statutory duties.³³
- A1.3 Elxon, through its wholly owned subsidiary EMR Settlement Limited, is the settlement services provider on behalf of the Low Carbon Contracts Company in relation to Contracts for Difference and on behalf of the Electricity Settlements Company in relation to the Capacity Market.
- A1.4 Elxon is the Senior Responsible Owner and Implementation Manager for the Market-wide Half Hourly Settlement (MHHS) Programme. Elxon is delivering

²⁹ <https://www.ofgem.gov.uk/sites/default/files/2023-03/Electricity%20Transmission%20Consolidated%20Standard%20Licence%20Conditions%20-%20Current.pdf#page=157>

³⁰ Note that Ofgem can also send back modification proposals if it considers that it is unable to form an opinion on the modification proposal. The procedure for sending back modification proposals is further detailed in paragraph 2.7A of Section F of the BSC.

³¹ As well as the matters set out here, for previous modifications where we approved an extension to Elxon's vires, we listed four criteria to assess whether such an activity would be appropriate for Elxon to pursue. The criteria were: i) BSC Parties should benefit from any diversification, ii) the arrangements should not place disproportionate risk on BSC Parties, iii) standards of service under the BSC should be maintained, and iv) Elxon's BSC role should not give it any undue competitive advantage in a contestable activity.

³² <https://www.ofgem.gov.uk/sites/default/files/2023-03/Electricity%20Transmission%20Consolidated%20Standard%20Licence%20Conditions%20-%20Current.pdf#page=160>

³³ The Authority's statutory duties are wider than matters which the BSC Panel must take into consideration and are detailed mainly in the Electricity Act 1989.

the MHHS Programme under a Business Separation Plan, as Elexon (as the BSCCo) is also a MHHS Programme participant.

- A1.5 Elexon carries out a number of other additional activities, which typically relate to settlement, including the Capacity Market Advisory Group Secretariat and administering a number of support schemes on behalf of government.
- A1.6 Elexon is currently wholly owned by, but operationally independent from, National Grid ESO, but as a result of the establishment of the FSO becoming a public body, DESNZ and Ofgem consulted³⁴ on two credible ownership options: Elexon remaining in industry ownership or becoming a public body as a subsidiary of the FSO.
- A1.7 It has been decided that Elexon will remain in industry ownership and that the 13 largest suppliers and generators³⁵ be mandated to take on one share each in Elexon. These shareholders will not have any influence on Elexon's operations and impartiality, nor be required to provide funding, so Elexon will continue to remain operationally independent.
- A1.8 Elexon is not currently regulated by Ofgem, but do have non-voting representation on the BSC Panel, approve the appointment of the Panel Chair, attend Workgroups and decide whether to approve, reject or send back modifications proposals that are sent to us for decision.

FSO overview

- A1.9 The Future System Operator (FSO) will be a new body established by the Energy Act,³⁶ which was granted Royal Assent on 26 October 2023. The FSO is referred to as the Independent System Operator and Planner (ISOP) in the legislation.
- A1.10 As a trusted and expert body at the centre of the gas and electricity systems, the FSO will play an important role in coordinating and ensuring strategic planning across the sector, to help achieve net zero by 2050. The FSO will adopt a whole system approach within the energy system through responsibilities in operations, strategic network planning, long-term forecasting, and market strategy. It will provide independent advice to Ofgem and government on request to inform policy decisions.

³⁴ <https://www.gov.uk/government/consultations/the-future-ownership-of-elexon>

³⁵ The 13 licensed BSC funding parties with a greater than 2% funding share as of 1 January 2023

³⁶ <https://www.legislation.gov.uk/ukpga/2023/52/contents/enacted>

- A1.11 The creation of an independent System Operator (SO) was recommended to government by Ofgem in January 2021 as part of the Review of GB energy system operations,³⁷ to provide SOs with additional responsibilities and to make the Electricity System Operator (ESO) fully independent from Transmission System Operators (TSOs).
- A1.12 The ESO became a legally separate company within the National Grid Group (which includes National Grid's Transmission and Distribution businesses) on 1 April 2019, to remove any perceived conflicts of interest and provide greater transparency of ESO operations.
- A1.13 The FSO will be a public corporation within the public sector, but operationally independent from government, and it will be funded by consumers through price control arrangements. It will be regulated by Ofgem through licence conditions and general statutory enforcement.
- A1.14 It will take on all the main ESO roles to balance the system and maintain security of supply, whilst also playing an increasingly significant role in shaping the energy system and driving competition across the energy sector. It will also take on the strategic, longer-term forecasting and planning roles for gas. The FSO will coordinate with Distribution Network Operators (DNOs) to ensure optimal system-wide planning, use of flexibility, and data exchange.
- A1.15 Ofgem and DESNZ have a shared ambition for the FSO to be operational in 2024, with a phased implementation approach. We published our decision on the funding of the transition from ESO to FSO³⁸ on 28 September 2023 and our non-statutory consultation on draft FSO licences³⁹ closed on 20 October 2023. An additional consultation on the FSO's proposed financial framework and our emerging thinking on the enduring FSO regulatory framework is due to take place shortly, before a statutory consultation prior to FSO designation. Subsequent changes to other licences and codes will also be required. A Cross-Code Workgroup⁴⁰ will develop the industry code changes required for the establishment of the FSO.

³⁷ <https://www.ofgem.gov.uk/publications/review-gb-energy-system-operation>

³⁸ <https://www.ofgem.gov.uk/publications/decision-funding-transition-future-system-operator>

³⁹ <https://www.ofgem.gov.uk/publications/future-system-operator-fso-draft-licences-consultation>

⁴⁰ <https://www.ofgem.gov.uk/publications/decision-letter-ofgems-call-volunteers-fso-codes-change-programme>

A1.16 We have a dedicated Future System Operation page⁴¹ on our website which sets out our vision for the FSO and contains a repository of relevant documents we have published.

Energy code governance

A1.17 Elexon currently administers the BSC which is in scope of Energy Code Governance Reform.⁴² Whereas the ESO currently administers the Connection and Use of System Code (CUSC), the Grid Code (GC), the System Operator – Transmission Owner Code (STC), and the Security and Quality of Supply Standard (SQSS), all of which are in scope of Energy Code Governance Reform.

A1.18 Energy Code Governance Reform, which will be enabled by the Energy Act, will consider Code consolidation, and will require Ofgem to set an annual strategic direction statement, and will introduce the concept of Licensed Code Managers. These code managers will be selected and regulated by Ofgem. Code managers will be empowered to make decisions under the codes, including on whether to approve certain Code Modifications, as well as making recommendations to Ofgem on whether to approve others. Our Call for Input on Energy Code Governance Reform closed on 2 February 2023.⁴³

A1.19 When developing our market facilitator proposals, we have been mindful of the impact that Energy Code Reform will have on the future governance of the energy system. We will continue to consider the potential interactions between these two projects as the detailed role of the market facilitator is developed, particularly where synergies or potential overlaps may exist (eg the process by which we develop and communicate our strategic vision for the Market Facilitator versus our Strategic Direction for codes). However currently we do not believe that Energy Code Reform will impact our implementation options for the market facilitator role for either Elexon or the FSO.

⁴¹ <https://www.ofgem.gov.uk/energy-policy-and-regulation/policy-and-regulatory-programmes/future-system-operation-fso>

⁴² <https://www.ofgem.gov.uk/energy-policy-and-regulation/policy-and-regulatory-programmes/energy-code-reform>

⁴³ <https://www.ofgem.gov.uk/publications/energy-code-governance-reform>

Appendix 2 – Related publications

- Decision – Future of local energy institutions and governance (November 2023): <https://www.ofgem.gov.uk/publications/decision-future-local-energy-institutions-and-governance>
- Consultation – Future of local energy institutions and governance (March 2023): <https://www.ofgem.gov.uk/publications/consultation-future-local-energy-institutions-and-governance>
- Call for Input – Future of local energy institutions and governance (April 2022): <https://www.ofgem.gov.uk/publications/call-input-future-local-energy-institutions-and-governance>
- Future System Operator (FSO) draft licences consultation (September 2023): <https://www.ofgem.gov.uk/publications/future-system-operator-fso-draft-licences-consultation>
- Proposal for a Future System Operator role – Decision (April 2022): <https://www.ofgem.gov.uk/publications/proposal-future-system-operator-role-decision>
- Future System Operator: second policy consultation and project update (August 2023): <https://www.gov.uk/government/consultations/future-system-operator-second-policy-consultation-and-project-update>
- Centralised Strategic Network Plan: Consultation on framework for identifying and assessing transmission investment options (July 2023): <https://www.ofgem.gov.uk/publications/centralised-strategic-network-plan-consultation-framework-identifying-and-assessing-transmission-investment-options>
- Elexon Ownership Government and Ofgem’s response to consultation (March 2023): <https://www.ofgem.gov.uk/publications/elexon-ownership-government-and-ofgems-response-consultation>
- The future ownership of Elexon (July 2022): <https://www.gov.uk/government/consultations/the-future-ownership-of-elexon>
- Call for Input: The Future of Distributed Flexibility (March 2023): <https://www.ofgem.gov.uk/publications/call-input-future-distributed-flexibility>
- Consultation on proposals for a Future System Operator role (July 2021): <https://www.ofgem.gov.uk/publications/consultation-proposals-future-system-operator-role>
- Review of GB energy system operation (January 2021): <https://www.ofgem.gov.uk/publications/review-gb-energy-system-operation>
- Full chain flexibility (May 2022): <https://www.ofgem.gov.uk/energy-policy-and-regulation/policy-and-regulatory-programmes/full-chain-flexibility>

- Net Zero Strategy: Build Back Greener (October 2021): <https://www.gov.uk/government/publications/net-zero-strategy>
- The Climate Change Act 2008 (2050 Target Amendment) Order (June 2019): <https://www.legislation.gov.uk/ukxi/2019/1056/contents/made>
- The Energy Act (October 2023): <https://bills.parliament.uk/bills/3311>
- Smart Systems and Flexibility Plan (July 2021): <https://www.gov.uk/government/publications/transitioning-to-a-net-zero-energy-system-smart-systems-and-flexibility-plan-2021>
- Ofgem's Future Insights Paper 6 - Flexibility Platforms in electricity markets (September 2019): <https://www.ofgem.gov.uk/publications/ofgems-future-insights-paper-6-flexibility-platforms-electricity-markets>
- End-Scheme decision on the Electricity System Operator's performance 2021-2023 (August 2023): <https://www.ofgem.gov.uk/publications/end-scheme-decision-electricity-system-operators-performance-2021-2023>
- Section C 'BSCCo and its Subsidiaries' (November 2023): <https://bscdocs.elexon.co.uk/bsc/bsc-section-c-bscco-and-its-subsidiaries>
- Decision on designation of the Market-wide Half-hourly Settlement Governance Framework (November 2021): <https://www.ofgem.gov.uk/publications/decision-designation-market-wide-half-hourly-settlement-governance-framework>
- Code Administrators' Performance Survey Findings (January 2022): <https://www.ofgem.gov.uk/publications/code-administrators-performance-survey-findings-2021>
- Energy Code Governance Reform (December 2022): <https://www.ofgem.gov.uk/publications/energy-code-governance-reform>

Appendix 3 – Glossary

Term	Definition
Balancing and Settlement Code (BSC)	The Balancing and Settlement Code contains the rules and governance arrangements for electricity balancing and settlement in Great Britain. This code is administered by Elexon.
Connection and Use of System Code (CUSC)	The Connection and Use of System Code is the contractual framework for connecting to and using the national electricity transmission system (NETS). The code is administered by the ESO.
Cross-Code Workgroup	Refers to a group of volunteers helping to develop proposals for the industry code changes required for the establishment of the FSO to facilitate FSO Day 1 roles and duties.
Decentralisation	Refers both to the general trend of smaller scale sources of generation and storage, but also a trend towards decisions being made at a smaller scale when it comes to the energy transition.
Deliverables	Refers to the outputs of delivery bodies. In the context of the market facilitation of flexible resources, the deliverables may include the common outputs that are developed by the market facilitator to be adopted by DNOs and the FSO.
Delivery body	An entity responsible for overseeing, managing and driving forward initiatives, to meet the expectations of the role.
Department for Energy Security and Net Zero (DESNZ)	This is a ministerial department focused on delivering the energy portfolio. It was formerly known as the Department for Business, Energy, and Industrial Strategy (BEIS).
Distribution Network Operator (DNO)	A DNO is a company that operates the electricity distribution network, which includes all parts of the network from 132kV down to 230V in England and Wales. In Scotland 132kV is a part of transmission rather than distribution so their operation is not included in the DNOs' activities. There are 14 DNO licensees that are subject to RIIIO price controls. These are owned by six different groups.
Distribution system	The system of low voltage electric lines and low-pressure pipelines providing for the transfer of electricity and gas within specific regions of Great Britain.
Distribution System Operation (DSO)	The set of activities that are needed to support the transition to a smarter, flexible, and digitally enabled local energy system. DNOs have been building capabilities in planning, operating and market facilitation of flexible resources to drive more efficient development and use of the decarbonising electricity system. This differs from the more traditional responsibility of a DNO, which is to take power from the transmission network

	and deliver it at safe, lower voltages to homes and businesses.
Energy Networks Association (ENA)	The Energy Networks Association represents the companies which operate the electricity wires, gas pipes and energy system in the UK and Ireland.
Electricity System Operator (ESO)	National Grid Electricity System Operator is the electricity transmission system operator in Great Britain. The entity responsible for operating the electricity transmission system and for entering contracts with those who want to connect to and/or use the electricity transmission system.
Flexibility	Modifying generation and/or consumption patterns in reaction to an external signal (such as a change in price) to provide a service within the energy system.
Flexibility markets	Flexibility market refers to the arena of flexibility service procurement processes across various market operators within GB. This includes DNO local flexibility markets, ESO Frequency and Ancillary services, Balancing Mechanism, Wholesale Market, Capacity Market, P2P services (ie Power Purchase Agreements (PPAs)) etc.
Flexibility services	Using on-network or customer owned equipment to control power and energy flows across network infrastructure, leading to more efficient and cost-effective outcomes.
Forecasting	The process of using data to estimate the likely future energy demand. Used to ensure the proper allocation of resources and assist in infrastructure investment decisions.
Future System Operator (FSO)	The FSO will take on all the main existing roles and responsibilities of National Grid ESO and the longer-term planning, forecasting and market strategy functions.
Governance	A framework overseeing and directing changes in the energy sector, through mechanisms underpinned by democracy.
Grid Code (GC)	The Grid Code details the technical requirements for connecting to and using the national electricity transmission system (NETS). Compliance with the grid code is one of the requirements of the Connection and Use of System Code (CUSC). The Grid Code is administered by the ESO.
Licensed body	An organisation obliged to comply with licence conditions for their type of licence from the day the licence is granted.
Market facilitation	Creating accessible and coordinated markets which enable the full value of flexibility to be realised.
Market facilitator	In the context of the local governance review, it is a new role we are defining with responsibility for delivering more joined up flexibility markets.
Market participants	These are actors in the markets who are involved in the trade, generation and supply of energy.

Market-wide Half Hourly Settlement (MHHS) Programme	MHHS is a vital enabler of flexibility. It builds on changes already made requiring half-hourly settlement (HHS) for medium to large non-domestic consumers, and elective HHS for domestic and smaller non-domestic consumers
Network planning	Refers to the transmission and distribution of energy. Delivering sufficient capacity, when it is it is needed, using the most cost-efficient solutions whilst maintaining network resilience and reliability.
Open Networks programme	The Open Networks programme is a project led by the ENA and supported by DNOs and the ESO to support the development of local flexibility markets. It was launched in 2017 in response to the Smart System and Flexibility Plan.
Price control	This is a method developed by Ofgem to set targets and allowed revenues for network companies. The characteristics and mechanisms are developed in the price control review period depending on network company performance over the last control period and predicted expenditure (companies' business plans) in the next.
Regional Energy Strategic Planner (RESP)	A new role responsible for the development of strategic energy plans at the regional level and providing critical planning assumptions to inform system and network needs.
Revenue stacking	The ability to earn revenue simultaneously from multiple sources using the same capacity.
Security and Quality of Supply Standard (SQSS)	The Security and Quality of Supply Standard sets out the criteria and methodology for planning and operating the national electricity transmission system (NETS). The code is administered by the ESO.
Strategic leadership	Monitoring developments across policy, regulation, innovation, and energy markets to proactively identify upcoming challenges, opportunities and risks that may require intervention.
Strategy and policy statement (SPS)	The strategy and policy statement (SPS) is developed in accordance with the energy act and sets out the government's strategic priorities and other main considerations of its energy policy. It sets out the policy outcomes to be achieved and the roles and responsibilities of those who are involved in policy implementation.
System needs	The amount of energy needed (MWh). Dependent on regional customers and economic, net zero and cross vector plans.
System Operator – Transmission Owner Code (STC)	The System Operator Transmission Owner Code defines the relationship between the transmission system owners and the system operator. The STC is administered by the ESO.

Transmission network	The system of high voltage electric lines and high-pressure pipelines providing for the bulk transfer of electricity and gas across GB.
Whole System	An approach that considers the gas, electricity (transmission and distribution) networks as well as the impact the heat and transport sectors have on the system as a whole.

Appendix 4 – Privacy notice on consultations

Personal data

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

1. The identity of the controller and contact details of our Data Protection Officer

The Gas and Electricity Markets Authority is the controller, (for ease of reference, “Ofgem”). The Data Protection Officer can be contacted at dpo@ofgem.gov.uk

2. Why we are collecting your personal data

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

4. For how long we will keep your personal data, or criteria used to determine the retention period.

In this consultation, we intend to hold your data for 1 year before it is reviewed.

5. With whom we will be sharing your personal data

Your personal data will not be shared outside of Ofgem. We will publish your response on our website, but you can request us to keep it confidential subject to obligations to disclose information, for example, under the Freedom of Information Act 2000,⁴⁴ the Environmental Information Regulations 2004,⁴⁵ statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If your response contains personal information, we will publish it as it is, unless you ask us to remove any names. If you want to keep your response confidential, please indicate this

⁴⁴ <https://www.legislation.gov.uk/ukpga/2000/36/contents>

⁴⁵ <https://www.legislation.gov.uk/uksi/2004/3391/contents/made>

clearly on your response and put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published.

6. Your rights

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data.
- access your personal data.
- have personal data corrected if it is inaccurate or incomplete.
- ask us to delete personal data when we no longer need it.
- ask us to restrict how we process your data.
- get your data from us and re-use it across other services.
- object to certain ways we use your data.
- be safeguarded against risks where decisions based on your data are taken entirely automatically.
- tell us if we can share your information with 3rd parties.
- tell us your preferred frequency, content and format of our communications with you.
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at <https://ico.org.uk/>, or telephone 0303 123 1113.

7. Your personal data will not be sent overseas

8. Your personal data will not be used for any automated decision making.

9. Your personal data will be stored in a secure government IT system.

10. For more information on how Ofgem processes your data, click on the link to our "[ofgem privacy promise](#)".