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Dear David,

**Aqua Consultants' response to Ofgem's consultation "Policy direction for the Future System Operator's regulatory framework"**

Thank you for the opportunity to respond to this consultation. A successful Future System Operator (FSO) will benefit everyone, ensuring future energy networks that are fit for purpose. Future energy networks must not constrain new energy sources as the country decarbonises, but also not restrict the potential for new customers in different geographies, or the development of new industries or technologies. The FSO will therefore play a significant role in achieving Net Zero but also in helping to level up the country: the challenge is large, but the opportunity and prize are great.

With the above in mind, we consider your proposed policy direction suitable and well-considered. A not-for-profit model is appropriate in this case, with strong non-financial targets and a simple and transparent funding mechanism. The regulatory approach should be light-touch and a mix of ex-ante and ex-post measures. In particular the FSO should have a duty to demonstrate it is delivering a fit-for-purpose future network, given the various possible futures at any point in time.

Ensuring all stakeholder views are fairly represented is paramount. Safeguards should be put in place to ensure balance. The FSO should regularly identify and engage with all possible stakeholder groups, and that these groups may change over time. We also think there is an opportunity to introduce an expert panel function of technical specialists that can help to shape the future network, provide a different lens for the FSO and review any commissioned research or new developments.

As we state in our response to Ofgem's market facilitator consultation, we are not entirely clear on the separation of remits for the FSO versus the market facilitator. Some up-front work to fully define this will guarantee the right decision is made whether the functions should be provided by a single or separate organisations and ensure no conflicting priorities.

We provide detailed answers to the consultation questions overleaf.  
If we can assist in developing your plans any further, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Tom Hall', with a large, sweeping horizontal stroke underneath.

Tom Hall  
Chief Economist

## Responses to consultation questions

### *Q1. Do you have any views on our proposed financial regulatory framework for the FSO?*

We agree with the rationale for the FSO to operate under a not-for-profit regulatory model. While the FSO needs to deliver value for money, a focus on short-run profit maximisation has the potential to distort the overall long-term goals which will greatly benefit society for the very long term: ensuring energy networks that work for current and future customers. The prize is great, and it should therefore be the core principle of the FSO.

Strong non-financial targets will ensure the organisation operates in the right way. Ensuring all stakeholder voices are fairly heard and views balanced will be key.

A fast-money approach to funding is suitable: simplicity and transparency is important. It would be beneficial to understand any additional transaction costs from introducing the FSO and the resulting implication on energy and gas charges. FSO charges should be distributed fairly across energy and gas customers. Customer-level incidence effects are unlikely but should be considered and managed.

### *Q2. Do you have any views on our emerging thinking on how we should regulate the FSO, including our objectives, the case for change, and potential future options?*

We agree with your proposed framework objectives. The key is to result in a future network that is fit for purpose and does not constrain future potential technological developments. A key guiding principle could be a “fit for the future” duty. This would need to be fully defined and quantified with criteria that allows a holistic assessment of where the FSO is achieving and where action is needed.

Performance incentives: A mix of ex-ante and ex-post measures are appropriate. Option 2 (a lighter touch and a more strategic focus) produces a proportionate regulatory burden. Unless, of course, if the FSO fails to perform to the required standard, which should see greater performance monitoring. For the ex-post measures, a mix of option 3 & 4 appears appropriate depending on the requirement – although it should be proportionately applied. There is the opportunity for the development of an independent survey of main stakeholders and customers will provide confidence that the FSO is meeting its objectives.

Business plans: Ensuring long-term objectives are paramount – so the FSO should set out its progress towards, and achievement of its strategic outcomes along a pre-agreed timetable. This should also include how it meets the government’s Strategy and Policy Statement objectives. There should be requirements to report how near-term network needs are being addressed but also uncertain long-term needs, balancing different potential futures for the energy network to ensure potential future energy generation types, systems or downstream customers are not constrained by poor decisions.

*Q3. What role should industry stakeholders and external parties have in holding the FSO to account, and what platforms are needed to achieve this?*

Ensuring stakeholder views are represented is paramount: the energy network will need to change significantly, and stakeholders provide expert advice, guidance, and support to deliver a successful FSO.

All stakeholders' views should be fully represented, and safeguards put in place to ensure balance: it is critical that a small number of stakeholder groups do not exert disproportionate influence on the outcome of energy networks. One suggestion is for a requirement to assess all different stakeholder types and establish that each of these views are heard (or at least invited to participate). Stakeholders (and their relative importance) are likely to change over time, so the stakeholder groups should be reconsidered periodically.

There is also the opportunity to develop an independent expert panel function to provide expert technical advice: this may offer a different lens compared to the wider stakeholder engagement. This panel would also offer an alternative critique for any research commissioned by the FSO.

There is also an opportunity for independent surveying across the FSO's customers to ensure the FSO is meeting its objectives.

*Q4. Do you have any views on our approach to implementing changes?*

A phased approach, conducted in engagement with the existing FSO and the rest of the industry is sensible and appropriate. The timetable appears achievable at this early stage.

As we note in our response to the market facilitator consultation, we are not entirely clear on the separation of remits for the FSO and market facilitator. Some additional work now would be beneficial to provide confidence the correct decision of whether they should be conducted by the same or different organisations, and any conflicting priorities can be identified and mitigated.