



Making a positive difference
for energy consumers

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Dear Stakeholders,

Consultation on the Performance Arrangements Governance Document and Licence Expectations Document for NESO for the RIIO-2 Business Plan 3 period

This letter explains our¹ proposals for two documents that support the implementation of National Energy System Operator (NESO)'s regulatory framework for the RIIO-2 Business Plan 3 (BP3) period:

- the NESO Performance Arrangements Governance Document (PAGD);² and
- the NESO Licence Expectations Document.³

We have published these draft documents alongside this letter. We welcome views from stakeholders on these documents and our proposed changes by 5 March 2025.

Background

NESO was introduced on 1 October 2024 (Day 1) as an expert, impartial body with key responsibilities across both electricity and gas systems. It has objectives related to driving progress towards net zero while maintaining energy security and minimising costs for

¹ References to the "Authority", "Ofgem", "we", "us" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work.

² Established under Part B of Condition G2 of both NESO's ESO & GSP Licences.

³ Established under Part F of Condition C1 of NESO's ESO licence and Part E of Condition C1 of its GSP licence.

consumers. NESO is an independent, not-for-profit public corporation, licensed and regulated by Ofgem.

The design of NESO's regulatory framework is critical in supporting NESO's performance against its statutory duties and delivering outcomes in the interest of consumers. We are introducing changes to NESO's regulatory framework in phases. For Day 1 of NESO, we introduced several key changes to reflect NESO's new organisational design and roles. NESO will soon commence the BP3 period, which runs from 1 April 2025 to 31 March 2026, and is the last period of its RIIO-2 price control. This will be our second phase of implementing changes to the regulatory framework for NESO.⁴

In November 2024, we published our decision on the performance incentives framework for NESO for the BP3 period.⁵ This included our decision on the key features of the business plan process, performance assessment approach, cost regulation and stakeholder feedback mechanisms. We decided to introduce a revised performance incentives framework from the one that applied to NESO during the RIIO-2 Business Plan 2 (BP2) period. The BP3 framework focusses on NESO's delivery of key objectives and major priorities and is underpinned by the introduction of new Performance Objectives. The changes aimed to ensure our regulatory assessments are targeted at the issues which matter most and have most impact on outcomes for the energy sector and consumers.

The NESO PAGD underpins NESO's performance regulation framework. It sets out the detailed processes and procedures for our public assessment of NESO's performance, as well as the information NESO is required to report on to demonstrate its performance. Our proposed approach to implementing NESO's new performance arrangements for BP3 are included in the draft PAGD, published alongside this letter.

We are also consulting on the NESO Licence Expectations Document, which provides further explanation of the behaviours we expect from NESO in relation to some of its licence obligations. NESO's Electricity System Operator (ESO) Licence and Gas System Planner (GSP) Licence set the minimum requirements and standards that NESO must comply with while performing its duties. The purpose of the Licence Expectations Document is to help align expectations between NESO, Ofgem, and stakeholders to support the enforceability of NESO's obligations. The predecessor to this document was the NESO Roles Guidance.⁶ Previously, the NESO Roles Guidance included both our licence expectations and incentives-related expectations for three distinct NESO roles. However, in our BP3 framework decision,

⁴ For more information on our phased implementation approach please see: [Policy direction for the Future System Operator's regulatory framework](#) (Pages 22-23) and [Future System Operator - Second Policy Consultation and Update](#) (Pages 51)

⁵ [Ofgem's Decision on NESO's performance incentives framework for BP3](#)

⁶ [NESO Roles Guidance 2023-2025](#)

we decided that incentives related expectations should be set primarily through the new Performance Objectives (and associated Success Measures). The BP3 Licence Expectations Document would consequently focus on providing guidance on how NESO can best meet its licence obligations. We considered it would be beneficial to create a clearer distinction between licence expectations and incentives expectations to ensure each area can be tailored to its purpose and used most effectively.

Following our consultation, we intend to publish final versions of both the NESO PAGD and the NESO Licence Expectations Document, which will come into effect from 1 April 2025 (the start of BP3 period).

Summary of key proposals in this consultation and reasons for the proposals

Below we summarise the key proposals in the two documents along with reasons for these proposals. Please see the draft documents, published alongside this cover letter, for our detailed proposed changes. We have not included tracked changes versions of these documents from the BP2 versions because they are materially different documents. We consider it would be easier for stakeholders to review clean versions of these proposed documents alongside our summaries below.⁷

For the avoidance of doubt, we are not reconsulting on the policy decisions already made in our November BP3 framework decision. Instead, we are consulting on the detailed implementation of these previous decisions.

Licence Expectations Document

During the RIIIO-2 BP2 period, NESO's regulatory framework was structured around three separate roles. For the BP3 period, we are no longer adopting this structure. We have therefore modified the structure of the Licence Expectations document and it is now organised into thematic chapters for clarity. Further, in line with our November BP3 framework decision, we have removed the 'Exceeds Expectations' text, as the document decouples incentives from licence expectations. We have retained majority of the 'Meets Expectations' text, and we have added further guidance in activities relating to connections reforms, strategic network planning, and CSNP.

⁷ The BP2 versions of these associated documents can be found here: [Decision on Associated Documents to the anticipated NESO licences – regulatory framework documents](#)

We have also sought to make updates where previous BP2 Roles Guidance text was no longer relevant or out of date (for example, where outputs or projects have come to their end). The key areas where the previous BP2 expectations have evolved are explained below.

We have proposed changes to our expectations related to NESO's connections activities to reflect the proposed TMO4+ Connection Reforms. These expectations will only take place if the proposed reforms are approved, and the associated licence changes are implemented. Our first decision on TMO4+ Connections Reforms is expected in March 2025.⁸

We have also made additions to reflect the Transitional CSNP2 Refresh⁹, which NESO needs to publish by January 2026. We have included our expectations on NESO to ensure that it assesses the Transmission Owners' (TOs) developed options and other proposed options to develop a strongly justified needs case, so that we can make appropriate funding and incentivisation decisions.

NESO is now a public corporation and an independent organisation. However, NESO still receives some of its corporate services (such as IT) from National Grid plc (NG) whilst it develops its own standalone capabilities. NESO is expected to exit these services in a timely and cost-effective manner. We have made updates in the document to reflect our updated expectations for NESO for the BP3 period in relation to establishing full independence.

Performance Arrangements Governance Document

We have developed a new version of the NESO PAGD for BP3 to reflect our November decision on NESO's new performance framework for BP3. This includes changes to reflect the introduction of a revised two-part performance assessment based on (1) NESO's achievement of its business plan aims, and (2) NESO's delivery of value for money. Our proposal for the BP3 PAGD maintains many of the overarching features in BP2 version. This includes processes and requirements for regular performance reporting, Ofgem monitoring discussions, and the collection of stakeholder feedback, which all inform an End of Year Review of NESO's performance by Ofgem and the NESO Performance Panel. Our key proposed changes to the PAGD from BP2 are summarised below.

⁸ For the avoidance of doubt, in making these proposed changes to the expectations related to the TMO4+ Connection Reforms, we have made no decision on these reforms and nothing in the Licence Expectations Document in any way fetters our discretion in respect of the reforms. With this being the case, we therefore may need to revisit the Licence Expectations Document depending on the decisions made in respect of the TMO4+ Connection Reforms.

⁹ For more information: [tCSNP2 decision](#)

We have updated the overarching scheme process (see Chapter 2 of the PAGD) to reflect that BP3 is a one-year period rather than two-year period. Given the reduced length, we no longer propose to hold a mid-scheme review process (where we previously provided an interim public assessment and grading of NESO's performance prior to our final assessment). Instead, we intend to provide ongoing feedback to NESO during BP3 through our regular monitoring meetings, which we have maintained from BP2. The proposed PAGD also now contains additional guidance to support NESO's licence requirements¹⁰ to collect regular and coordinated stakeholder feedback on its performance.

We have developed new detailed guidance for how we will assess NESO's performance at the BP3 End of Year Review (see Chapter 3 of the PAGD). We have generally aimed to simplify this guidance compared to the methodology we used for BP2. We have also sought to strike the right balance between providing clarity on our assessment approach whilst ensuring it is flexible to within year changes and developments. Our proposed guidance on how we will assess NESO's achievement of its business plan aims, explains how we will consider NESO's delivery of its BP3 Performance Objectives and associated Success Measures (as well as other relevant information). Our proposed value for money assessment follows a similar approach to BP2, although we have aimed to provide additional clarity on our approach and to reinforce the link to our up front assessment of NESO's business plan.

The reporting framework NESO must follow during the BP3 period (see Chapter 4 of the PAGD) is broadly similar to the one on place for the BP2 period. Our key proposed changes for BP3 include:

- Amending requirements related to Reported Metrics¹¹ to reflect the new framework decision and our intention to only confirm the details of additional Reported Metrics following the BP3 determinations;
- Replacing the previous detailed delivery schedule reporting with reporting by NESO on its progress against its Performance Objectives;
- Maintaining the existing frequency and content of public value for money reporting, but expanding our Cost Monitoring Framework to include NESO's performance exiting from the Transitional Services Agreement with NG (in addition to existing IT requirements); and
- Moving from an annual to a six-monthly Stakeholder Satisfaction Survey.

We have proposed to move the frequency of the Stakeholder Satisfaction Survey to six months as we consider that stakeholder feedback mechanisms should play a key role in holding NESO accountable for its performance across its different customer-facing

¹⁰ See Condition G2.4 of NESO's ESO Licence and GSP Licence

¹¹ These were in the previous BP2 PAGD referred to as Performance Measures

activities. We consider this will also support a shift to a more strategic Ofgem performance assessment. Our proposal also reflects the change in the BP3 scheme structure from BP2 and the potential benefits of getting clear, coordinated stakeholder feedback on NESO's performance prior to the End of Year Review. This would enable NESO, Ofgem and stakeholders to understand key areas of success or concern and any actions needed prior to the final assessment. We note that this is an increase in the equivalent reporting from the BP2 period and may therefore place additional burden on NESO and stakeholders. We therefore welcome views on whether this frequency is justified by the value it could create or if maintaining an annual requirement would be a more appropriate frequency.

We have also made several changes throughout the document to try and make the document more accessible and to avoid areas of duplicative requirements and guidance.

Next steps

We welcome views from stakeholders on our proposed NESO PAGD and Licence Expectations Document. Specifically, whether they effectively implement our BP3 framework decision and achieve our objective of improving and streamlining processes during the BP3 period. This includes any feedback on the new aspects we have proposed that build on to the previous arrangements, or any removed content that stakeholders consider provides value and therefore should be maintained. We will take this feedback into consideration when making a final decision on the documents.

This consultation is one of the several activities that we are carrying out to implement NESO's regulatory framework. We aim to publish our draft determinations on NESO's Business Plan for BP3 in Q1 2025. This will set out our draft assessment on NESO's BP3 submission, as well as further detailed proposals for specific reporting requirements over BP3. We are also further developing our policy on our enduring approach to regulating NESO. We plan to engage further with stakeholders this spring on the regulatory framework design for NESO from 1 April 2026 (when RIIO-2 BP3 ends).

If you have any questions on the contents of this letter, please contact us at nesoregulation@ofgem.gov.uk.

Yours faithfully,

David Beaumont

Head of NESO Framework Development

Energy Systems Management & Security

Signed for and on behalf of the Gas and Electricity Markets Authority