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for energy consumers

Email: [NESORegulation@ofgem.gov.uk](mailto:NESORegulation@ofgem.gov.uk)

To: All interested stakeholders

Date: 25 March 2026

Dear colleagues,

### **Decision to approve amendments to the Terms and Conditions related to Balancing for Demand Flexibility Service**

We<sup>1</sup> received a proposal from National Energy System Operator ("NESO") to amend the terms and conditions ("T&C") related to balancing required by Article 18 of [Commission Regulation \(EU\) 2017/2195 establishing a guideline on electricity balancing](#), as amended by the [Electricity Network Codes and Guidelines \(Markets and Trading\) \(Amendment\) \(EU Exit\) Regulations 2019](#) ("EBGL"). The proposal relates to an update to the T&C to incorporate service documentation for NESO's Demand Flexibility Service ("DFS").

On 30 January 2026, NESO submitted a proposal to amend the terms and conditions related to balancing ("T&C") by updating the DFS Service Terms and DFS Procurement Rules.

The Authority has decided to approve NESO's proposal to amend the relevant sections of the documentation for DFS (DFS Service Terms and DFS Procurement Rules) within the T&C, in accordance with Article 18 of the EBGL. Following this decision, with effect from 9 April 2026, references to DFS in the T&C should be read as referring to these updated versions, and earlier versions are superseded.

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<sup>1</sup> The terms "we", "us", "our", "Ofgem" and "the Authority" are used interchangeably in this document and refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

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## Background

In accordance with Article 18 of the EBGL, the Transmission System Operator<sup>2</sup> was required to develop a proposal regarding T&C for Balancing Service Providers ("BSPs") and Balance Responsible Parties ("BRPs").<sup>3</sup> On [8 October 2019](#), we published our decision to confirm, upon satisfaction of certain conditions, that the T&C proposed are the T&C required by Article 18 of the EBGL. On 25 June 2020, all the necessary conditions were met, and the proposed T&C came into force in Great Britain ("GB"). NESO has submitted the current proposal to amend these T&C by updating the mapped DFS Service Terms and DFS Procurement Rules.

The DFS was first introduced during the winter of 2022/23 to provide an additional system security (enhanced action) tool allowing access to additional volume to help balance the system during periods forecast to otherwise experience negative margins. The service was continued and refined ahead of winter 2023/24 for the same purpose. As the system margins outlook for winter 2024/25 improved, NESO repositioned DFS as a merit-based margin management tool. The service attracted volumes of demand-side response ("DSR") through suppliers, aggregators and Industrial and Commercial ("I&C") customers to provide a demand turn-down (or generation turn up) service to help NESO manage tight system margins. NESO reported, that DFS has delivered balancing cost savings of approximately £700,000 over the first year of operation, on this basis, suggesting that demand-side response can be competitive with other options available to NESO and can provide value to consumers as an in-merit balancing option.

NESO's latest proposal intends to expand the service by:

- (i) Introducing negative margin capability (or Demand Turn Up ("DTU")),
- (ii) Procuring DFS volumes on a locational basis,

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<sup>2</sup> National Energy System Operator (NESO) is now the body responsible for maintaining the T&C, having taken on the responsibilities of NGENSO on its incorporation on 1 October 2024.

<sup>3</sup> See footnote 2 and our decision of 14 September 2018 <https://www.ofgem.gov.uk/decision/decision-assignment-transmission-system-operator-obligations-under-guideline-electricity-balancing-regulation-within-gb>

- (iii) Introducing primacy arrangements which enable the exclusion of certain Meter Point Administrative Number (“MPANs”) from participating in DFS to prevent conflicts between local (Distribution Network Operator (“DNO”)) and transmission network actions,
- (iv) Introducing an optional self-nomination baseline for I&C participants and intermittent renewable assets, and
- (v) Reducing the eligibility criteria of a DFS unit to participate in the service from 1 MW to 0.1 MW, lowering barriers to participation for flexibility providers.

On 30 January 2026, NESO submitted a proposal to amend the T&C to integrate the updated DFS Service Terms and DFS Procurement Rules. This proposal followed a consultation period that concluded on [10 December 2025](#). To enhance the clarity of the T&C, NESO also supplied a mapping document alongside the proposal.

DFS has been designed to be procured and instructed at timescales such that its balancing energy gate closure is earlier than allowed under Article 6(4) of the Electricity Regulation.<sup>4</sup> As such, NESO also submitted a request to us for a derogation from this requirement for DFS. We have approved NESO’s derogation request alongside this decision, with the derogation valid until 31 August 2028.<sup>5</sup> NESO has been procuring the DFS ahead of gate closure (i.e., up to 8 hrs ahead) under a previous derogation. NESO’s latest submission has requested dispatch earlier than 8 hours in some circumstances, e.g., where there is benefit in operational flexibility to manage both demand turn-up and turn-down actions. As set out in our derogation decision, we expect NESO to optimise DFS dispatch in line with its best view of efficiency and that dispatch should move closer to real time over time as both NESO and industry participants improve the digitalisation and other capabilities and understanding of service provision.

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<sup>4</sup> Commission Regulation (EU) 2019/943 of 5 June 2019 on the internal market for electricity (“the Electricity Regulation”) dictates that “Market participants shall be allowed to bid as close to real time as possible, and balancing energy gate closure times shall not be before the intraday cross-zonal gate closure time.” Where the intraday cross-zonal gate closure time is currently T-1hour. The Electricity Regulation is accessible at: <https://eurlex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R0943&from=EN>, and has been adopted into UK law by UK SI 2020 No. 1006, available at: <https://www.legislation.gov.uk/ukSI/2020/1006/contents/made>.

<sup>5</sup> For clarity, NESO cannot procure the service ahead of gate closure regardless of its inclusion in the T&C, without a derogation in place.

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## **Rationale for our decision**

We have reviewed the DFS service documents (consisting of the DFS Service Terms and DFS Procurement Rules) submitted by NESO to be recognised as part of the T&C and submitted to us in line with the requirements of the EBGL, the wider principles of the Electricity Regulation, and our statutory duties and obligations. In order to do this, we engaged with NESO to better understand its proposals in several areas.

In reaching our decision, we also considered feedback from industry stakeholders in response to NESO's consultation on the proposed changes. The overall response was positive, but there were requests for clarifications in several areas, particularly in relation to data transparency, DNO exclusions, locational procurement and baselines. NESO addressed these inquiries and amended the T&C to incorporate relevant stakeholder feedback where appropriate. We have set out our views below.

### The Case for DFS

DFS continues to provide an important route to market for consumer-led flexibility, particularly for providers who are traditionally unable to participate in the electricity markets, consistent with our November 2024 decision. This also aligns with the [Clean Power 2030 Action Plan](#) ("CPAP") and [Clean Flexibility Roadmap](#) ("CFR"), which recognises flexibility, including consumer-led flexibility ("CLF"), as central to delivering a clean, affordable, and secure electricity system. The CFR promotes 'Clean Flexibility' which focuses on shifting demand or supply of electricity to balance the grid, maximising the use of low-cost renewables and providing resilience during periods of low generation. We also note that the roadmap references 'investigating and enabling Demand Turn Up' as an action on NESO and emphasises removal / reduction of barriers to participation.

In this context, we consider DFS to remain an appropriate tool for supporting these objectives. Additionally, NESO (and therefore the consumer) has seen value from the balancing energy delivered by DFS under its current design. We consider that the updated DFS service design proposed by NESO represent a proportionate evolution of the service, strengthening DFS as a viable route to market for meaningful DSR participation,

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particularly from providers who may otherwise face barriers to engaging in the electricity system (e.g., manually dispatched DSR).

Overall, the service design changes proposed should further enable flexibility and lower barriers to entry while maintaining appropriate balance between system needs and market accessibility. We therefore view the proposal as a positive evolution that strengthens the role of demand-side response, enhances competition and supports efficient outcomes for consumers.

### Service Design Changes

#### *(i) Negative Margin*

NESO proposed for DFS to be a bi-directional service, expanding its capability to include negative margin action (or Demand Turn Up) alongside the existing positive margin action (or Demand Turn Down). By introducing this change, NESO intends to improve its operational effectiveness, promote further growth of CLF, and enhance system security, competition and value for money. We also recognise strong support from industry to implement this proposal.

Having considered the objectives of CPAP, CFR and strong support from industry, we are satisfied with NESO's proposal (i), to include negative margin capability within the service. This change supports the CFR by unlocking consumer-led flexibility, enabling demand to increase when it is most valuable to the system improving utilisation of low-carbon generation and reducing curtailment, widening participation and competition among flexible resources, and enhancing operability and value for money through a bi-directional margin management tool. We also consider this aligns with the intent of principle (c) of the Electricity Regulation: "market rules shall facilitate the development of more flexible generation, sustainable low carbon generation, and more flexible demand".

#### *(ii) Locational Procurement*

A key aspect of this iteration was to introduce a locational procurement element into DFS. We understand that this can enable NESO to use DFS to help manage network constraints,

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as well as enabling more efficient service procurement by targeting volumes to the zones where they deliver the greatest system benefit, minimising congestion and redispatch. Overall, we noted broad support from industry for introduction of location-based DFS procurement. However, there were some requests for clarification and two respondents disagreed with NESO's proposal - we set out views on these particular aspects, below.

One respondent sought clarification on how locational procurement will operate in practice for DTU, particularly in relation to transmission boundary constraints and aggregation. We understand that DFS can now be procured on a zonal basis, with aggregation limited to MPANs within the same DFS zone and procurement volumes controlled through event-specific, per-zone caps which NESO can adjust based on the prevailing system conditions. We agree that this approach is appropriate to help preserve network integrity and support efficient procurement of the service.

Some respondents noted that zonal procurement could add complexity and suggested to test this approach in NESO's more established markets, obtain learnings there and later extend to DFS. Our view is that applying locational procurement in DFS protects consumers by avoiding actions that exacerbate constraints: CLF participation could be undermined if NESO needs to take a more cautious approach to using DFS where stranded volumes present operational risks. On balance, while we recognise there may be increased complexity to this approach, we consider that it will deliver a net benefit to NESO, the service and flexibility providers. Therefore, we are content with NESO's proposal to procure DFS with a locational aspect.

NESO received strong industry feedback on aligning its DFS zones with the DNO zones. NESO initially proposed 5 zones for DFS but later expanded to 12 zones in line with industry feedback. We consider this a positive outcome of the consultation process, however, for clarity we note that NESO retains the ability to redefine the number of zones where required. If NESO does decide to redefine the zoning, we would expect communication of any changes as early as practicable with sufficient notice to support a smooth transition.

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We consider that locational procurement can support more economic and efficient procurement and strengthens consumer value by focusing expenditure where it is most effective. We therefore approve NESO's proposal (ii), to procure DFS on a locational basis.

*(iii) Primacy Arrangements*

NESO proposed to manage potential distribution-level conflicts through a primacy process whereby DNOs can indicate where specific MPANs should be excluded from participation due to congestion on their local networks. We note that stakeholders broadly accepted the need for a primacy mechanism. Three DNO respondents also supported it in principle as a safeguard to support whole-system coordination and protect distribution network security, provided the arrangements are implemented transparently and consistently.

Several respondents requested a clearer decision framework for primacy exclusions, including the basis on which DNOs determine risk and how that assessment translates into an exclusion. Some noted that unexplained or excessive exclusions could disengage consumers and thereby reduce participation. From NESO's reply to the consultation feedback, we understand that MPANs are eligible by default unless a DNO returns a Risk-of-Conflict ("RoC") indication, and that a high threshold applies to any exclusion. We expect NESO and DNOs to robust evidence for any exclusions.

One respondent also asked whether exclusions are time-scoped, i.e. whether they apply only to specific Settlement Period(s) or for a longer duration. Our view is that RoCs should be regularly revised. We understand from NESO that its expectation is for RoCs to be revisited for each DFS event. For clarity, an exclusion should apply only to the specific period set out in the Primacy Exclusion Report, reflecting the conflict timings identified by the DNO that meet the threshold for exclusion. We understand that NESO has defined the primacy exclusion process in the DFS Procurement Rules.

Another respondent highlighted the risk that DNOs may initially apply primacy conservatively, noting that current DNO forecasting and conflict-checking processes may be insufficiently reliable on a day-ahead basis to identify all potential overload scenarios,

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which could reduce participation. We expect NESO and DNOs to communicate clearly, monitor outcomes, and unwind over-cautious exclusions as evidence accumulates, while maintaining consumer protection and network integrity as the priority.

Lastly, several respondents reported variability between DNOs in the granularity and transparency of RoC outputs. They also requested that DFS shouldn't have bespoke set of rules and must align with the common terms set by the [market facilitator](#) in the long-term. We are content to proceed with the current arrangements as an interim solution ahead of the market facilitator concluding more enduring primacy arrangements, and we understand that under ESO Licence Conditions C20. NESO would be required to align to those enduring rules if they differed from the current arrangements. In the meantime, NESO should continue to work with the market facilitator and DNOs to develop those enduring arrangements and improve consistency, transparency, and auditability of primacy across GB.

We agree that excluding specific MPANs from DFS participation, where justified, under primacy arrangements is a necessary safeguard to coordinate actions across transmission and distribution, minimise conflicts, and maintain network integrity. If done correctly and proportionately, this should represent a benefit to demand-side response engagement. We therefore approve NESO's proposal (iii), to implement the proposed primacy arrangements.

*(iv) Baseline Methodology Calculations*

For all domestic participants, NESO proposed to retain application of a baselining methodology derived from the version used in the Balancing and Settlement Code ("BL01"). However, NESO has now also proposed to allow for a self-nominated baseline approach for intermittent renewable assets and I&C assets. NESO's original position had been to maintain the adopted BL01 approach for I&C participation, however, NESO decided to extend the self-nomination option for I&C as well following strong industry

feedback. For clarity, the self-nomination baseline does not extend to domestic participants who own embedded renewable assets.<sup>6</sup>

Some respondents raised concerns about the introduction of self-nominated baselines, including the potential for gaming and reporting burden. To mitigate gaming risk, NESO has indicated that self-nominated values must be submitted ahead of the published Service Requirement, are subject to audit, and may be deemed ineligible where evidence is inconsistent. We are content that requiring baselines ahead of the event is proportionate and that the proposed controls are appropriate to mitigate gaming risks.

One respondent sought further clarification regarding export-limited and storage sites to avoid inadvertent distortion in baseline formation. We understand that the current calculation accounts for both import and export, and we are content with this approach. However, we consider it appropriate for NESO to publish clear guidance together with worked examples, to address any edge cases and to support participants' understanding of how to effectively provide the service.

Another respondent observed that days on which providers deliver other flexibility commitments may be designated as "active" and therefore excluded from the baseline data set, and that excessive exclusions could undermine the robustness of baseline formation. We recognise this concern; however, we consider greater coordination between NESO and DNOs, rather than changes to the core methodology, as the appropriate approach. We also consider that NESO should remain open to introducing alternative baselining methodologies where these are shown to be robust and to increase market access.

Having considered industry views and NESO's rationale, we are content with proposal (iv), to introduce self-nominated baselines for intermittent generation and I&C participants.

#### *(v) Eligibility Criteria*

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<sup>6</sup> Embedded renewable assets are small-to-medium-scale renewable energy generation or storage units—such as rooftop solar, wind turbines, or batteries—connected directly to a local distribution network.

NESO proposed to lower the minimum bid size for DFS units from 1MW to 0.1MW. For clarity, this applies to single unit bids as well as aggregated portfolios of 0.1 MW. We consider this a positive step in lowering barriers to participation for flexibility providers, supporting the objectives of the CFR and aligning with the direction of travel across NESO's balancing services to reduce unit and bid sizes, widen access for smaller resources, and increase competitive tension through increased liquidity. We also note that industry feedback was strongly supportive of this change.

We note that one respondent raised concerns that a lower threshold could create distortions, including in relation to *de minimis* rules for imbalance price formation and consequent opportunities for gaming. Our assessment, following discussions with both Elexon and NESO, of the *de minimis* threshold currently in use within the Balancing and Settlement Code, is set to 0.1MW and thus does not present any material risk. The *de minimis* rules for imbalance are set out in Section T of the BSC as [De-minimis Acceptance Threshold \("DMAT"\)](#). DMAT is used to exclude very small volumes (for example, 0.1MWh) from the calculation of the imbalance price. However, once the imbalance price is calculated, DMAT does not remove these volumes from providers' positions.

We believe NESO's proposal is in line with CFR objectives and is strongly supported by industry as it lowers barriers to participation for flexibility providers. Therefore, we approved the proposal (v), to lower the minimum submission size for DFS.

## Decision

Considering the above, the Authority hereby:

- approves that the DFS Service Terms and DFS Procurement Rules as mapped form part of the T&C required by Article 18 of the EBGL.

For clarity, our **approval is effective as of 9 April 2026**.

## Next Steps

We expect NESO to publish the updated DFS Service Terms and DFS Procurement Rules alongside an updated Article 18 mapping document by 9 April 2026.

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Stakeholders have asked for practical examples to support understanding of the updated processes. We expect NESO to publish clear guidance and communications to support onboarding, including worked examples on the primacy framework. We also expect NESO to update its customer-facing communications framework, particularly the DFS Communication Principles (and any associated guidance), to reflect the introduction of DTU and any changes to dispatch and participation arrangements and to provide clear, accessible messaging for consumers and providers.

We recognise that NESO now operates two markets, DFS and the Locational Constraint Market (“LCM”), which provide a route to market for less-traditional, non-BMU providers, and which now both have locational aspect and DTU included. This presents an opportunity to share learnings across these two markets. We expect NESO to work with industry to provide a clear, longer-term strategy on the respective roles of these existing services, and the future of market access for demand-side response volumes to ensure participation isn’t unnecessarily reduced by any market changes. Particularly, we note that there is uncertainty around how long the LCM will continue to operate for, coupled with the 2028 expiry of our derogation for the DFS (allowing for further data to inform next steps). We consider that providing such clarity on the longer-term strategy and access for these two markets ahead of NESO’s decision on the future of the LCM can support investor confidence in bringing demand-side flexibility volumes to market and supports CLF playing a key role in achieving Clean Power 2030 targets.

Stakeholders also requested that NESO improve unit-level transparency by publishing pre-dispatch baselines and outturn data. We expect NESO to improve transparency of DFS operation by providing clearer, accessible information to support market understanding of baselines and event outcomes, where feasible.

Finally, we expect NESO to keep the service design under review where appropriate and to put into practice learnings from the service across markets to help unlock the full potential of flexible demand.

If you have any queries regarding the information contained in this letter, please contact Shubh Mehta ([shubh.mehta@ofgem.gov.uk](mailto:shubh.mehta@ofgem.gov.uk)).

Yours sincerely,

**James Hill**

Principal Policy Expert – Electricity System Operation

For and on behalf of the Gas and Electricity Markets Authority