

15 January 2026

Energy Network Association's response to Ofgem's Energy Networks Ring-fence Review

Dear Andrew,

Energy Networks Association (ENA) is the industry body representing the electricity networks in the UK. Our members directly employ 26,000 people in England, Scotland, Wales and Northern Ireland, including around 1,500 apprentices and trainees. ENA's members operate a network of around 500,000 miles of lines and cables which deliver electricity to around 29 million homes and businesses across the country. Around 60% of the network is underground.

This submission is made on behalf of ENA's GB Distribution Network Operator (DNO) and Transmission Owner (TO) members.

The ring-fence arrangements are of fundamental importance to both customers and investors: the ring-fence provides investors with a clear articulation of the regulator's expectations and associated restrictions and protects customers from exposure to the financial or operational risks associated with certain riskier business activities. **We agree that it is sensible to periodically review ring-fence requirements**, especially in light of any events (including in other sectors) that have revealed financial resilience concerns. In general however, we think the current ring-fence processes have served customers well and are largely fit for purpose for the future. In undertaking the review, Ofgem must be mindful that frequent, unexpected or short-notice changes to the ring-fence undermine investor confidence in the regulatory framework. It is important from an investability perspective that investors have certainty over the restrictions that will be in place for the foreseeable future. Any suggestion that these arrangements may change on a frequent basis would undermine investability.

We agree that, where financial resilience risks align across sectors, it is sensible to ensure that obligations also align. For example, we have always understood that the absence of the requirement for Financial Resilience Report obligations from the ED2 licence was an inadvertent omission and that the requirement would be modified into the ED2 licence. However, where risks differ in other sectors, obligations may also need to differ and failures in some sectors may not indicate shortcomings in arrangements for others. In particular, we are pleased that Ofgem recognises the different resilience risks that are faced by gas networks compared to electricity networks. Ofgem should not default to assuming that any new obligations to mitigate the specific risks associated with the uncertain future of gas networks are relevant to or should be extended to electricity networks.

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Some of Ofgem’s proposed modifications to the ring-fence are disproportionate, ambiguous or conflict with other obligations.

We set out below our main concerns with elements of Ofgem’s proposed changes to the financial ring-fence.

A number of Ofgem’s proposed obligations on Sufficiently Independent Directors (SIDs) are in conflict with those directors’ duties conferred via other legislation including the Companies Act. These create conflict with or ambiguity about the interaction between the obligations under the ring-fence and other obligations placed on licensees or their directors. For example:

- an obligation upon SIDs to act in the best interest of the consumer may conflict with their duties as a director of the licensed entity. Furthermore, “the consumer interest” may often be subjectively interpreted, making this obligation ambiguous.
- licensees already have an obligation (Condition B22 ET, Condition 43A ED) which requires the SIDs to have the necessary skills, knowledge and experience to perform their roles. Furthermore, we already have an obligation to inform Ofgem when a SID changes. It is not clear why we now need a separate checklist, as an additional requirement, to confirm we are meeting current requirements. The checklist and template are unnecessary, and it is unclear what purpose it serves. It is also unclear why such a template is considered necessary for SIDs when no comparable requirement exists for Executive Directors.

While we agree with Ofgem that SIDs have a very important role to play in corporate governance, Ofgem must not introduce obligations that create conflict with SIDs’ duties as a director of those companies.

The proposed requirement for consent to alter existing capital and reserves is disproportionate and is also in conflict with Ofgem’s policy that financial arrangements are for shareholders to manage. Such an obligation would be too broad and would be disproportionately burdensome for both networks and Ofgem as, depending on how the restriction is drafted, business-as-usual obligations could fall within scope. Instead, Ofgem should focus on clearly defining the specific types of change that Ofgem wishes to be consulted on and also the circumstances under which it would be appropriate for Ofgem’s consent to be required (e.g. if the licensee has triggered the gearing or credit rating levels for lock-up). However we are unable to identify any proposed licence modification(s) pertaining to alteration of capital structures and licensees would need to see any proposals in order to comment. There are sufficient obligations already (and planned with the 36-month certificates) to ensure dividends are only paid if the licensee has sufficient financial resources so this measure is unnecessary.

We disagree with the need for and proposed definition of “regulatory ring-fence” and with how Ofgem proposes to incorporate it into the various licences. Fundamentally, we do not consider that any over-arching definition of “regulatory ring-fence” is required. We understand that the purpose of the proposed text is to provide an explanation and context of the

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financial ring-fence conditions, and less of a strict “definition”. As such, Ofgem’s public domain decision document on any changes to the ring-fence should be sufficiently clear to sit as a record of Ofgem’s policy intent. The licence should, instead, record the specific obligations and restrictions that Ofgem concludes are appropriately levied on licensees. Introducing a broader description of intent onto the face of the licence risks ambiguity of obligations and restrictions and must be avoided. This would clearly run counter to Ofgem’s aim *“to eliminate ambiguity and any misinterpretation of the purpose of the network ring-fence”*.

Notwithstanding our view that no definition is required, the proposed definition introduces material unintended consequences. In particular, it would seem to prohibit the procurement of shared services from other companies within the same ownership group, including the sharing of services between energy networks within the same ownership structure. Such a restriction would impose considerable inefficiencies and associated increased costs of separation onto networks and ultimately customers. Ofgem has assured us that it was not its intention to prevent such shared service arrangements, but this point should be made clear within the decision document. The proposed definition would also seem to preclude those deminimis activities that are permitted elsewhere in the licence.

Additionally, both of Ofgem’s proposed possible approaches to incorporating the proposed definition into the licence (inclusion in the introduction of the licence condition or as a new defined term) would create ambiguity about what legal status the proposed new wording has and how it is intended to interact with the specific obligations that are also included in the licence:

- If incorporated as a new defined term, as the term “regulatory ring-fence” is not used in the licence or in any of the proposed modified licence conditions, it would introduce a defined term that is not referenced by any obligation.
- If incorporated into the “Introduction” of one of the various licence conditions it would risk creating ambiguity about the intent of the specific obligation that Ofgem ultimately opts to preface with any broader policy intent. Additionally, as such introductions to licence conditions are considered non-operative it is unclear what legal status it would have.

Executive remuneration does not have any bearing on financial resilience or the financial ring-fence and should not be included within the scope of Ofgem’s ring-fence considerations. Furthermore, licensees are already required to comply with a number of corporate governance arrangements related to executive remuneration including Section 42C of the Electricity Act 1989 and Annex B3(a) to the Regulatory Financial Performance Report. We also note that a licensee has no incentive for executive remuneration to not be commensurate with the performance of the licensee.

Notwithstanding our view that executive remuneration is not relevant to the financial ring-fence, we also note that Ofgem’s proposal that at least one SID should attend the Remuneration Committee assumes a “one size fits all” approach to corporate governance, irrespective of their corporate governance arrangements. Some licensees do not have a licensee-level Remuneration Committee (but have alternative arrangements relevant to their circumstances);

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they should not have to create one just so a SID can attend. It is for companies to design governance arrangements that are most suitable to their particular circumstances in both the short and long-term.

It would not be appropriate to extend the references in the compliance certificates relating to dividends to all the ring-fence conditions. Most of those standard licence conditions do not have a material impact on the financial resilience of the licensee.

In particular, a dividend lock-up is a very significant restriction on the licensee's ability to run its business and to ensure investability. The dividend lock-up should only be triggered if there is a real risk that the licensee's financial resilience might be affected. The current list of standard licence conditions referenced in the certificate in relation to dividends achieves this. If Ofgem widens the scope of that certificate further, it would bring in restrictions that are either not actually relevant to this question (e.g. cross-subsidy) or risk being disproportionate (e.g. the value of an asset disposal that requires approval is currently c.£30k).

It is not appropriate for the requirement to obtain two investment grade credit ratings to be incorporated as an absolute obligation, as compliance with the requirement rests on the approach taken by a third party (i.e. the ratings agency). Consequently, the amended obligation on the licensee should be to use its reasonable endeavours to maintain two investment grade credit ratings.

Considerably more work is required to develop fit-for-purpose licence modifications

The accurate drafting of ring-fence obligations is hugely important. The proposed amended licence conditions that were shared by Ofgem within the consultation require considerable improvement before licensees are able to fully comment upon them and before they will be ready to modify into the various licences. The drafting issues that we have identified are material and have confused the interpretation of Ofgem's intent. For example, Ofgem appears to use "dividends" and "distributions" interchangeably in its drafting, leading to the potential for introduction of obligations that are much more onerous than we understood Ofgem's intent. We take comfort from Ofgem describing the drafts as "very preliminary" and committing to work with us to improve them.

The drafting included with the consultation is materially incomplete. The consultation does not include drafting for all proposed policy intents and some drafting is included for which no policy description has been provided e.g. the requirement of SIDs to act in the interests of the consumer. The consultation also only includes proposed drafting for ED. Drafting will be required for all sectors because of different defined terms and the different existing conditions that the new obligations need to interact with.

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Ofgem needs to give careful consideration as to which elements of its proposals should be encoded on the face of the licence and which should be within Associated Documents. As broad principles:

- It is not appropriate for important obligations relating to financial resilience to be conferred on licensees via Associated Documents that can be modified by self-modification processes.
- Conversely, where Ofgem wishes to provide guidance to licensees as to the reporting of their compliance with obligations that are conferred on licensees by means other than the licence, it may cause less confusion to include these within Associated Documents (provided that the guidance references those obligations and does not seek to go beyond the obligations that licensees already hold).

A lot of work is required to achieve and consult on acceptable drafting. We stand ready to assist. We recommend that, once it has published its policy decision, Ofgem puts in place a full licence drafting working group process to manage these changes. Ofgem must undertake a thorough consultation of all proposed licence modifications for all sectors.

We also note that the RIIO-3 statutory consultation does not consult on the licences for ED3 and that consultation on all proposed ED3 modifications (including the RIIO-3 changes) must be undertaken.

We trust that our views are clear and helpful. If you have any questions regarding our submission, please contact me in the first instance (Paul.McGimpsey@energynetworks.org).

Kind regards,

Paul McGimpsey
ENA Director of Markets and Regulation