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Response to Elexon Consultation on Governance arrangements for the Market Facilitator

Dear Ayo,

Who we are

NESO lies at the heart of the energy system as an independent, public corporation responsible for planning Great Britain's electricity and gas networks, operating the electricity system and creating insights and recommendations for the future whole energy system.

At the forefront of our efforts is delivering value for consumers. We work with government, regulators and our customers to create an integrated future-proof system that works for people, communities, businesses and industry, where everyone has access to clean, reliable and affordable energy.

NESO's primary duty is to promote three objectives: enabling the government to deliver net zero, promoting efficient, coordinated and economical systems for electricity and gas and the economy and efficiency of energy businesses and ensuring security of supply for current and future consumers. NESO will take a whole system approach, looking across natural gas, electricity and other forms of energy and will engage participants in all parts of the energy ecosystem to deliver the plans, markets and operations of the energy system of today and the future.

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Our key points

The Market Facilitator represents an opportunity to drive coordination and standardisation

- We agree with the need to reduce friction across markets and help providers realise the full value of their flexibility.
- An empowered, independent Market Facilitator can and should make design decisions faster, and take an objective, holistic view that removes potential biases that could be introduced from individual regulated businesses. It can provide transparency and confidence to flexibility providers about market design choices.

We welcome Elexon building capability quickly and its positive engagement with us and others

- Through running collaborative workshops, creating detailed design documents, and growing its team, Elexon is standing up to the challenge.
- We are having positive, constructive conversations with Elexon during this development phase. We want to see this continue to ensure it hits the ground running when it becomes fully operational later this year.

Elexon is proving itself thoughtful and robust in setting out governance arrangements

- Some of its proposals, such as a layered approach to defining flexibility markets, and end-to-end processes, demonstrates its considered, holistic approach to reforming flexibility markets.

The open change process risks undermining the policy intent of the Market Facilitator

- We agree that interested parties, including providers of flexibility, should be able to inform the prioritisation of and shape of market rules.
- We do not consider the open change process being the most efficient way to do this. First, proposers will have commercial interests that may mean proposed changes do not align with whole system value and consumer interest. Second, it risks drawing Elexon, NESO, DNOs, providers and other interested parties' resources away from, and therefore delaying, priority reforms. Third, it risks undermining Ofgem's policy objective for a Market Facilitator empowered to be the single, expert entity driving coherent market coordination reforms.
- We want to see an empowered Market Facilitator which takes on board the views of a range of stakeholders to set out the priority market reforms needed in the most effective way.

The scope of Flexibility Market Rules must reflect the Market Facilitator's objectives

- We believe Flexibility Market Rules must be directly related to market coordination.

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- We have concerns that the scope of Flexibility Market Rules is not clearly defined in these governance arrangements. Coupled with the open change process, this could result in proposers raising and progressing Flexibility Market Rules outside Ofgem's intended scope of the Market Facilitator, such as around technical parameters of NESO services that could risk system operability. Due to our unique responsibilities for system balancing, we agree with Ofgem's position that we must lead service design for our markets. We will continue to design services in consultation with industry – being clear on our requirements so our decisions are collaborative and explicit.

The broad scope and change process for defining Flexibility Market Rules for DNOs and NESO risks delaying key reforms

- We want to see more flexibility in the process for developing Flexibility Market Rules to ensure Elexon can deliver at pace.
- Similarly, we must avoid a risk that Flexibility Market Rules are so broad that any NESO reforms end up affecting a Flexibility Market Rule, initiating this change process and slowing down overall reform unnecessarily.
- Elexon must be proportionate in progressing change, able to recognise where robust, comprehensive analysis is needed, and where it is able to make quicker decisions that drive sooner delivery of vital reforms.

Elexon and Ofgem must recognise the Market Facilitator's role and its outputs in context of broader reform and NESO change plans

- We have a range of market reforms and system transformation projects in progress. Market Facilitator governance arrangements must account for how our existing reforms may impact, and be impacted by, Flexibility Market Rules. If delivery of a Flexibility Market Rule delays one of our existing change plans, we must be able to demonstrate that is in the consumer interest.

We look forward to engaging with you further. Should you require further information on any of the points raised in our response please contact Edwin Tammas-Williams, Flexibility Services Development Manager, at edwin.tammas-williams@neso.energy in the first instance.

Yours sincerely

Rebecca Beresford

Director of Markets

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Consultation Question Responses

Question 1: Do you agree with our proposed approach to cost-recovery, budgeting and finance for the Market Facilitator?

We agree that using existing processes, such as the BSCCo, for budget setting and cost recovery, will reduce the complexity and associated set-up costs compared with the other options that were proposed. As part of the BSCCo arrangements, the proposal for expected costs and expenditure must be clearly justified. Public consultation promotes transparency and can demonstrate the value for money to the consumer, while allowing for challenge.

Is the response to Q1 to be treated as confidential? No

Question 2: Do you agree with our proposed approach to developing and managing the Market Facilitator Delivery Plan and Annual Delivery Schedule?

We agree on the condition that Elexon will robustly consider deliverability of plans, including accounting for existing NESO change programmes, and ensure the plan is not so rigid as to prevent reprioritisation.

We agree with the two-year delivery plan and annual updates which reflects that market reforms are often across multiple years, but detailed development and reprioritisation creates the case for updates. **We do however want to see Elexon account for more regular reprioritisation and agile delivery such that we are not locked into rigid plans.**

Similarly, we suggest the plans should be outcome focused to reflect that detailed output design cannot and should not always be determined up to two years ahead of time. We are not clear on what the content of the plan will look like or how prescriptive it will be, so we welcome further detail from Elexon here. It is not clear, for example, whether development and delivery of Flexibility Market Rules (FMRs) will be included in the plan, and if so, what the implications are when new FMRs are raised during a Delivery Plan period.

We support Elexon's robust and consultative approach to developing the plan. Where the Delivery Plan imposes timelines and costs upon NESO, Elexon and the Stakeholder advisory Board **must consider this in context of NESO's and DNOs' existing commitments, plans and IT change programmes.** That means understanding the feasibility of the plan, identifying where progressing implementation of the Delivery Plan could delay other reforms, and considering the impact of that on whole system benefit. Similarly, Elexon must be mindful of other requirements upon NESO such as those around cyber security, resilience, direction from DESNZ or Ofgem, that could cause us to reprioritise. Without a route of appeal, it is essential that we have proper opportunity to input and that Elexon is required to duly consider it.

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We agree with the plan to transition the timing of the plan to reflect financial years. It is important that the timing and content of the Delivery Plan is aligned with our Business Planning requirements so that we can provide coherent, coordinated planning and ensure adequate funding to implement aspects of the Delivery Plan.

Is the response to Q2 to be treated as confidential? No

Question 3: What key topic areas should Elexon include in the first year Delivery Plan and Annual Delivery Schedule?

We believe current planned activities and commitments such as BP3 deliverables need to be taken into consideration in the development and setting of the first-year delivery plan and schedule. Current market reforms we are progressing include those described in our Markets Roadmap, our Enabling Demand Side Flexibility report and our Routes to Market review documents.

Our prioritisation and sequencing of reform reflects consumer benefit and deliverability, including in the context of existing system transformation projects. This work has also had considerable stakeholder feedback to help us define what these reforms should be. Elexon must have mind to this context.

This means we expect close collaboration with Elexon in defining plans, involving openness around resource capacity and IT system backlogs. As such, we must consider the value of a Flexibility Market Rule or change relative to other market reforms.

This does not mean Elexon should not challenge NESO around timelines, but it **must understand genuine constraints on delivery and where prioritising a Flexibility Market Rule might mean deprioritising a different change** industry expect to see.

Is the response to Q3 to be treated as confidential? No

Question 4: Do you agree with our proposed approach to monitoring implementation and tracking progress?

We agree that providing regular progress updates to the Market Facilitator on our change implementation is pivotal to ensure the success and benefits of changes can be realised across Markets.

Regarding Elexon's monitoring proposals (as in 11.2 of its Detailed Design Document), we **expect NESO's pre-existing reporting mechanism should generally satisfy Elexon's requirements**, e.g. Cost Monitoring Framework or performance reporting, rather than creating further regulatory burden with the introduction of any new reporting requirements. We set this out in in our response to Ofgem's Policy Framework consultation in February.

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We recognise the value of monitoring flexibility procured, **and have some thoughts on the proposed approach in section 11.2 of the Market Facilitator Detailed Design Document:**

- We agree metrics will be useful to monitor the successful implementation of flexibility rules and track progress, we would be happy to work further with Elexon to develop what the most appropriate metrics should be.
- The volume we procure through our markets is not an indication of compliant implementation of the Flexibility Market Rules or otherwise the success of markets. In fact, procuring lower volumes to meet our system requirements can indicate better efficiency.
- Elexon should be mindful of the difference between units and assets when considering data availability.
- When monitoring volumes associated with different asset types, Elexon should be mindful of relevant regulations and principles around non-discrimination. Through all of our services and markets, we procure based on a system need, not technology type. We are required to comply with regulations such as Regulation (EU) 2019/943, Article 6¹ that requires “non-discrimination between market participants”, and that we “ensure that services are defined in a transparent and technologically neutral manner.”

Is the response to Q4 to be treated as confidential? No

Question 5: Do you agree with our proposed approach to managing changes through change management process to Market Facilitator arrangements and Flexibility Market Rules?

We strongly oppose the proposed open change process as we consider it risks undermining core objectives of the market facilitator, whilst better arrangements exist to deliver transparent, collaborative and consultative design.

First, we think Elexon must be sufficiently empowered and have the expertise to raise and progress Flexibility Market Rules itself to ensure delivery of coherent, priority reforms. Enabling any person to raise and own the proposals fails to address the gap Ofgem’s of the lack of consistency and a lack of single accountability.

Second, this inherently enables proposers to own and develop changes where there are actual and perceived conflicts of interest. It risks changes being progressed that are not in the consumer interest or undermining confidence in the process.

Third, the industry has finite resources and must deliver reform at pace. Allowing any person to raise a change risks diverting resources from our priority reforms, whether this is implementation

¹ <https://www.legislation.gov.uk/eur/2019/943/article/6>

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of other FMRs or our other change plans. Clearly, Elexon must provide opportunity for the widest range of stakeholders to inform its decisions on what FMRs to raise and how to progress them. But we do not consider this is a proportionate or effective way to achieve this objective. This is **particularly concerning when the scope of FMRs does not appear to be limited** by these governance arrangements (see answer to Question 8). We consider our view reflective of the direction of travel for code governance, in which code managers will take on a more active role in decision making and identifying, raising and developing changes.

We suggest Elexon considers alternative means to bring wide stakeholder views into its change programme. Through robust engagement with interested parties, Elexon can define its change programme in a way that respects its objectives around openness and transparency, while also managing risks of biases and resource prioritisation.

In general, we agree with the tools and processes that Elexon proposes for assessing changes. We welcome Elexon reflecting that different tools, eg working groups and consultations, must be proportionate to the specific change.

We do not agree with the proposal that Elexon can require us to carry out an Impact Assessment (IA). It's not clear what the obligation would be on the NESO, including in what circumstances and for what justifications Elexon would require us to carry out an IA, how far in advance we would be notified of this requirement, what is in scope of the IA and how long we would have to carry it out.

This would have an impact on our costs and resourcing, which is not provided for in this proposal.

More broadly, we do have **concerns that the change process is unduly prescriptive**, e.g. with respect to limiting the number of alternative solutions. From our experience, developing service design is often more flexible and iterative than is provided by this change progress. We must also provide the flexibility that empowers Elexon to make quicker decisions, while respecting the broader principles of the change process, where that is in the consumer interest.

On implementation dates, we recognise the role for wide input (e.g. from a Working Group as Elexon proposes) into prioritisation and urgency of delivery. At the same time, it is essential that Elexon has processes **to ensure implementation timelines are realistic and desirable**. For example, timelines must account for any additional consultation requirements, IT system design and development work and the impact of and impact on existing commitments and change programmes. Elexon must be mindful of other requirements upon NESO such as those around cyber security, resilience, direction from DESNZ or Ofgem, that could cause us to reprioritise.

We propose that Elexon's FMR consultations and our Article 18 consultations should be sequential, rather than aligned. It is not feasible or efficient to carry out a consultation on the service terms and conditions until the FMR is finalised.

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Finally, while we agree with the proposed change objectives for FMRs, they **must also reflect the legislative and regulatory context for our services**. This includes compliance with the Electricity Regulation and European Balancing Guidelines as retained in UK law and our licence conditions. Otherwise, we increase the risk that we will at once be required to by our licence to implement FMRs which are not compliant with other regulations or other parts of our licence. This increases the **risk that Ofgem rejects our Article 18 submission on the basis of its disagreement with the content of the FMR**. This is clearly inefficient and could lead to significant delays. We are keen to work with Elexon and Ofgem to agree a solution to this risk.

Is the response to Q5 to be treated as confidential? No

Question 6: In order to facilitate planning and prioritisation, do you have any changes you believe should be raised and progressed?

Elexon should prioritise the key topics handed over from the Open Networks – including primacy, stacking, dispatch interoperability – in order to maintain momentum.

We look forward to working with Elexon in its prioritisation process. If raising and progressing additional changes, we would welcome the opportunity to consider the relationship with our existing change programmes where applicable.

Is the response to Q6 to be treated as confidential? No

Question 7: Do you agree with our proposed design and role of the Stakeholder Advisory Board?

We do agree with the general principle of the SAB. Having a formal way for a diverse range of stakeholders across industry to provide input and challenge to both the Flexibility Market Rules and the performance of the Market Facilitator is key to success.

NESO has a broader role beyond being a flexibility buyer. We operate as an independent public corporation, central to ensuring reliable, clean, and affordable energy for all. Our operational independence allows us to provide unbiased, data-driven analysis and recommendations essential for delivering an energy system that is secure, clean, economic and efficient. We are an experienced, impartial body with responsibilities across both the electricity and gas systems, driving progress towards net zero while maintaining energy security and minimising costs for consumers. We must consider how to promote competition, the impact of our activities on consumers and the whole energy system and the ways we can facilitate innovation.

As such, NESO should have a specific role on the SAB, reflective of its wider role. By providing a NESO view, we can provide better input and insights to drive the optimal system and market-based outcomes.

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We do not agree the SAB should be reviewing NESO's performance. This is the role of the regulator through our business planning and reporting process as well as through our regulatory obligations and licence conditions. Stakeholder input is taken on board by Ofgem in this process so there is already a route in place for feedback.

We have concerns the consultation states the SAB could run confidential sessions where NESO or DSO performance was being discussed. It is not clear if a DNO or NESO is able to participate in the discussion of its own performance, which we think this is inappropriate.

Is the response to Q7 to be treated as confidential? No

Question 8: Do you agree with our proposed structure and maintenance approach for the Flexibility Market Rules?

We agree with the structure in principle but require clarity on what will represent requirements on NESO. We also propose a defined scope of FMRs to align with Ofgem's policy objectives.

Overall, we think the structured and layered approach is an effective way to put Flexibility Market Rules in context, show relationships between rules and markets, and help interested stakeholders navigate the rules. We do however **need clarity about which components in this approach (e.g. Flex Market Catalogue, Sub-Market Definitions, etc) are Flexibility Market Rules**, i.e. a rule which we would be required to adopt, versus guidance or a directory to rules. We note we welcome Elexon's engagement with us on this matter to date.

Similarly, **the scope and breadth of Flexibility Market Rules, individually and collectively, must be more specifically defined.** If a sub-market definition is a Flexibility Market Rule, then there is a **risk that any change we intend to make to our service design will impact this FMR and initiate an FMR change process** where Elexon would be the final decision maker. This is not proportionate and undermines Ofgem's policy intent that NESO continues to lead its service design.

Second, we think Elexon should clarify the sorts of rules that can be in scope of an FMR. Ofgem proposed in its consultation that the design and development of FMRs is within the Market Facilitator's market coordination function. **The Flexibility Market Rules Framework does not make clear that FMRs are related to the Market Coordination function** and implies they can cover any area of service design.

We **agree with Elexon's proposed format for Flexibility Market Rules**, eg that they shall include the purpose and implementation timelines. As part of the implementation guidance, Elexon should consider additional design, development and consultation requirements.

With respect to maintenance of the FMRs, we agree with the importance of evaluating success. We provide comments on the change process in response to question 5.

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Is the response to Q8 to be treated as confidential? No

Question 9: Are there any areas of the proposed governance framework you believe require further clarity or development?

We have set out in response to other questions some areas where we require clarity or development, including:

- Clarity about what part of the FMR framework (catalogue, definition etc) would represent a requirement upon NESO (see question 8)
- Clarity about the scope of Flexibility Market Rules (see question 8)
- What is the content of the Delivery Plan and how does it relate to the FMR change process (see question 4).
- How to coordinate decision-making responsibilities across FMR and Article 18 consultations (see question 5)

Other areas where we require clarity or further development:

- How we provide for the Market Facilitator giving early stage input into NESO service design
- Clear roles and responsibilities throughout the process including Market Facilitator, NESO and Ofgem

We welcome continued positive engagement with Elexon on these points.

Is the response to Q9 to be treated as confidential? No

Question 10: Do you believe the proposed arrangements meet Ofgem's expectations as set out in its Market Facilitator policy framework decision?

We believe some proposed arrangements do, though some risk not doing so without further clarification or development. Specifically, we have concerns that:

- The change process could be too rigid and undermine the objective for delivery at pace
- The open change process undermines Ofgem's expectation that the Market Facilitator is a single, expert entity that designs and develops Flexibility Market Rules
- The breadth of scope of Flexibility Market Rules does not appear to align with Ofgem's consultation in which their role is in the context of market coordination.

We also note that Ofgem has not yet published its Market Facilitator policy framework decision, so our answer reflects the positions in its consultation.

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Is the response to Q10 to be treated as confidential? No