



Department for
Energy Security
& Net Zero

Elexon Ownership

Government and Ofgem's response to
consultation



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Glossary

BAU operations or BAU activities	Business as usual operations or activities
BEIS	Department for Business, Energy and Industrial Strategy
BESS	British Energy Security Strategy
BSC	Balancing and Settlement Code
BSCCo	The BSC refers to Elexon as BSCCo (BSC Company). It is used throughout this document with the same meaning as Elexon and its subsidiaries.
BSC Panel	A group of industry experts and consumer representatives who oversee the BSC.
BSC Parties	All industry parties signed up to the BSC .
Capacity Market	Provides payments to encourage investment in new capacity or for existing capacity to remain open.
Code consolidation	Refers to merging all or some of the codes into one or several codes to improve accessibility and facilitate coordinated change.
Code consultation response	Refers to the government response to the 2021 Consultation on the Design and Delivery of the Energy Code Reform, published in March 2022.
CfD	Refers to the Contracts for Difference scheme which creates contracts between electricity generators and the Low Carbon Contracts Company which incentivise low-carbon electricity generation.
Consultation	This refers to the joint Government/Ofgem consultation, “The Future Ownership of Elexon”, published 14 July 2022.
DCC	Data Communications Company
DESNZ	Department for Energy Security and Net Zero
DNO	Distribution Network Owners
Elexon	As in the Consultation, ‘Elexon’ refers to Elexon Ltd and its subsidiaries unless stated otherwise.
EMR	Electricity Market Reform
EMRS	Electricity Market Reform Settlement Services, a subsidiary of Elexon

FSO	Future System Operator
FSO consultation response	Refers to the government response to the Future System Operator Consultation published in April 2022.
Funding share	“Annual funding share”, as defined in the BSC.
GB	Great Britain
HMT	His Majesty’s Treasury
LCCC	Low Carbon Contracts Company Ltd
NGESO	National Grid Electricity System Operator Ltd
NGET	National Grid Electricity Transmission plc
Ofgem	The Office of Gas and Electricity Markets. It also refers to the Gas and Electricity Markets Authority, when relevant.
REC	Retail Energy Code
RECCo	Retail Energy Code Company
REMA	Review of Electricity Market Arrangements

1 Executive Summary

1.1 Introduction and consultation overview

On 14 July 2022, the Government and Ofgem published the Elexon Ownership consultation (referred to throughout as the ‘Consultation’), following on from the decision in April 2022 to establish the Future System Operator.

The Government and Ofgem response to the consultation on the FSO¹ set out the Government’s decision to establish a publicly owned FSO, taking on all the current roles of National Grid Electricity System Operator (NGESO) and some key roles in the gas system. Because the FSO will be founded on the existing capabilities and functions of NGESO (and, where appropriate, National Gas Transmission), we must also consider the future ownership of Elexon Limited, a subsidiary of NGESO. Elexon Limited (referred to as Elexon in this document) was established to administer the Balancing and Settlement Code (BSC) and procure the systems needed to implement it ahead of the New Electricity Trading Arrangements. Elexon also performs other roles in the electricity market, for example related to Electricity Market Reform Settlement (EMRS).

Elexon is wholly owned by NGESO, however it is operationally and financially independent from its parent company and is controlled by its own board with input from the BSC Panel. NGESO’s powers to appoint or remove directors are therefore completely constrained under the BSC, as are any other powers it may have as shareholder. NGESO and Elexon have very different roles, and considerations around their future ownership may be different. Therefore, the changes proposed for NGESO necessitated consideration of Elexon’s ownership, taking into account the unique factors concerning Elexon as an organisation. For this reason, we have consulted to gather evidence and views on our proposals for the future ownership of Elexon. The ownership change discussed in this document includes subsidiaries of Elexon Ltd.

Since NGESO exerts no control over Elexon in its capacity as shareholder, the establishment of the FSO should not in itself impact significantly on Elexon’s role, operations, funding, or governance. The only question it raises is the question of ownership. There may be some consequential changes to governance that are necessary based on the new ownership arrangements, however our only objective is to create an appropriate ownership structure and not to change the funding structures. In addition, we are not considering the role of the BSC or Elexon’s role in relation to it. These policy areas are within scope of DESNZ and Ofgem’s separate code reform project.

1.2 Summary of stakeholder engagement and responses received

Following the publication of the Consultation we held an open webinar to present the contents of the Consultation and allow attendees to ask any initial questions they had. Towards the end of the Consultation period, we held workshops with different groups of industry parties, giving further opportunity for questions and clarifications.

¹ <https://www.gov.uk/government/consultations/proposals-for-a-future-system-operator-role>

We received 28 responses to the Consultation. These came from a mixture of generators and suppliers, including firms which have both supply and generation licences; system bodies and transmission networks; and other organisations, including a consumer body.

In the response analysis section, we do not use the exact or absolute numbers of respondents in this document, mainly because the number of respondents to each question varied. Instead, we use the following categories:

- “majority” is used when referring to 15 or more of those that provided a response to the question;
- “many” is used when referring to 10 – 14 of those that provided a response to the question;
- “some” is used when referring to 4 – 9 of those that provided a response to the question;
- “a few” is used when referring to 3 of those that provided a response to the question;
- “a small number” is used when referring to 1 – 2 of those that provided a response to the question.

1.3 Overview of our positions and key policy decisions taken

Following the analysis of responses, DESNZ and Ofgem have made the following decisions on the key policy areas, that:

- The enduring ownership option for Elexon should be in the private sector, with shares held by industry parties.
- The shares in Elexon will initially be transferred to the 13 licensed BSC funding parties with a greater than 2% funding share in Elexon as of 1 January 2023, with the 13 specific parties set out in section 2.3. The licensed funding parties are the parties that pay a proportion of Elexon’s costs each month, dependent on how much electricity they have traded, supplied, or generated.
- The qualifying parties based on this test will each be required to take ownership of one share in Elexon by a new licence condition, the approach to and wording of which will shortly be the subject of Ofgem consultation.
- DESNZ and Ofgem retain the option to temporarily move Elexon into public sector ownership, should the implementation of the enduring ownership option pose a risk to timelines for the establishment of the FSO.

2 Response Analysis

This section provides a summary of our Consultation positions, a summary of stakeholder responses for each Consultation question, and finally the policy decisions Government and Ofgem have taken.

2.1 Question 1 – Policy criteria

Do you agree with the proposed criteria to determine the future ownership of Elexon? Please state why.

Consultation Position

In the Consultation, we set out our criteria for making a policy decision as below:

- 1. Minimise disruption to work on the BSC, Market-wide Half-Hourly Settlement (MHHS), and Electricity Market Reform (EMR):** the ownership structure needs to be deliverable in a manner which minimises disruption to Elexon’s crucial work on the BSC, as well as its work on energy system transformation through MHHS and EMRS. It is not our objective to alter the roles or governance of Elexon, although minor consequential alterations may be needed because of ownership change.
- 2. Avoid disruption to the FSO delivery timeline:** the ownership structure needs to ensure Elexon continues to function well without disrupting the timely creation of the FSO.
- 3. Preserve accountability to industry stakeholders and independence:** the ownership structure of Elexon needs to preserve the accountability of Elexon to their key stakeholders, as well as the independence of Elexon from any other specific organisation.
- 4. Ensure resilience to future change:** including to the impact of code reform on Elexon’s work.

In the Consultation we asked if consultees agreed with the proposed criteria to determine the future ownership of Elexon and to state their reasons.

Summary of responses

Some respondents expressly agreed with our criteria and the majority provided comments that indicated broad agreement, with some stating their agreement with the importance of specific criteria.

Some respondents commented on the impact on future owners, citing the costs of implementation and the possibility of the new owners facing liabilities.

Government/Ofgem Response

We believe that our criteria are appropriate, as indicated by the agreement and supportive comments from respondents. Our view is supported by the importance placed by respondents

on preserving Elexon's independence and accountability, minimising disruption to Elexon's business as usual operations, and ensuring resilience to future change.

The question of potential liabilities falling to new owners is dealt with in section 2.6. Wider costs of the policy are dealt with in section 2.8.

2.2 Question 2 – Possible ownership options for Elexon

Do you agree that public ownership and industry ownership are the two most credible ownership options? In your view, are there any other ownership options that we should consider, and why?

Consultation Position

In the Consultation document, we established two options for the enduring ownership option for Elexon that met the four policy criteria.

Firstly, that **Elexon move into public ownership as a subsidiary of the FSO** to ultimately be owned by government, but still be governed through the BSC. We anticipate that there would be few, if any, changes to the existing governance structure, funding arrangements, data sharing provisions and mandatory activities of Elexon outlined within the BSC, allowing it to continue its business as usual (BAU) operations. Under this option, we consider that it would be important that (as with the FSO itself) Elexon was operationally independent of government, meaning government would not be involved in day-to-day operational decisions. Where new public bodies are created, they are subject to separate government classification and approvals processes.

The second option was that **Elexon remain in industry ownership**. This ownership option would involve Elexon being owned collectively by relevant energy industry parties and governed through the BSC. The shares in Elexon would be reallocated from NGEN to all or a sub-set of the BSC Parties. We expect that there would be minimal changes to Elexon's existing governance structure (beyond the change in ownership), funding arrangements, data sharing provisions and mandatory activities of Elexon outlined within the BSC. This would allow Elexon to continue their BAU operations and maintain the organisation's industry accountability.

Other ownership options set out below were considered and discounted in the Consultation for the following reasons:

- Elexon being merged with the FSO. This was discounted due to the potential for interference with Elexon's essential services, possible interference with the establishment of the FSO and NGEN/FSO's essential operations.
- Elexon having a single private owner. Another part of National Grid plc could be a single owner, but they would need to become a BSC party. This would be complex, especially since Transmission Owners are not a current category of BSC Party. It would also be an unnecessary BSC change as there are suitable BSC parties who could be shareholders. Outside of National Grid plc, we have not identified any other single BSC party that would be appropriate. Other classes of industry licensees have more than one member, so it would be arbitrary to give shares to just one member of any larger group or class of BSC party.

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- Elexon could be owned by a new holding company limited by guarantee (CLG) with industry parties as members. A CLG is a company owned by members, rather than shareholders, who guarantee a certain amount of money they may have to pay if necessary. They do not hold shares, and the company would be non-profit. This would be a more complex change to the Elexon corporate structure taking longer to implement, which could risk FSO implementation. It brings no benefits commensurate to these risks because ownership of Elexon does not confer control or have any liabilities anyway due to the protections for and controls on shareholders set out in the BSC.

Summary of responses

The majority of respondents agreed that the public and industry ownership options were the two most credible ownership options for Elexon. There was general agreement that the enduring options both met the four policy criteria set out in the Consultation. More specifically, there was clear understanding of the need to avoid delaying the FSO implementation timeline, and that both options would allow for it to stay on track. A further common theme was the comment that industry ownership has allowed Elexon to operate effectively and maintain its independence.

Some disagreed with our Consultation position on this question overall. With regard to public ownership, a small number of respondents disagreed on the basis that it could pose a significant risk to the continued focus of Elexon on industry and consumer outcomes, due to potential additional obligations. Conversely, a small number disagreed that industry ownership is the most appropriate option, due to a perception that the public ownership option would require few, if any, changes to the existing governance structure, funding arrangements, data sharing provisions and mandatory activities of Elexon outlined within the BSC.

Some respondents mentioned other enduring ownership options they did not believe had been explored sufficiently, including Elexon being a company limited by guarantee, or another part of National Grid plc owning Elexon, such as National Grid Electricity Transmission (NGET).

Other notable comments included specifying that any change in ownership must not impact access to, and the quality of, data used for Contracts for Difference (CfD) and Capacity Market (CM) schemes; and that the correct controls should be in place to achieve industry outcomes and tackle the current challenges faced in the energy market.

Government and Ofgem Response

We maintain that Elexon remaining under industry ownership or public ownership as a subsidiary of the FSO are the most appropriate enduring ownership options. Our position that both ownership options meet the policy criteria to an adequate extent has not changed, and this view is supported by the majority of respondents.

We note the comments that public ownership could impact industry and consumer outcomes, however, we do not consider that there would be material impact, as both suggested ownership options would allow business as usual operations within Elexon. Similarly, there would be no changes to governance arrangements affecting the data Elexon handles.

With regard to the alternative ownership options proposed, no evidence has been presented which impacts our analysis or our conclusions. We therefore maintain that it would be inappropriate to pass ownership of Elexon to a non-BSC party, e.g. NGET, and it would be an unnecessarily complex change, as set out above.

Pursuing industry ownership under a company limited by guarantee would be more complex to implement than maintaining the existing company limited by shares as it would necessitate a much greater change to Elexon's current ownership structure, and this could endanger both Elexon's BAU operations and the FSO implementation timeline. It also does not provide any additional protection to shareholders from future liabilities beyond that offered by a company limited by shares. Taking these factors into account, we consider that Elexon should remain as a company limited by shares. See section 2.6 for more detail on liabilities.

We note the comments that industry ownership has allowed Elexon to operate effectively and maintain its independence. Taking this into account, and for the reasons set out under question 4, our policy decision is for Elexon to move into industry ownership as the enduring option. We provide greater detail on this decision in section 2.4.

2.3 Question 3 – Proposed shareholders

Do you agree with our stated preference of the potential combinations of BSC Parties which could own Elexon if industry ownership were chosen? Please state why.

Consultation Position

In the Consultation, we proposed that there were three broad sub-sets of BSC Parties which would be appropriate to own Elexon under industry ownership. The possible options of broad groupings included licensed BSC Parties, licensed funding BSC Parties and BSC Voting Parties, three sub-sets defined in the BSC:

- Licensed BSC Parties: generators, suppliers, the system operator, DNOs, and interconnectors. This has the advantage that all of these parties can be given a licence condition, which enables a direct regulatory route of enforcement to cooperate in taking on the shares, implement the new structure and undertake ownership obligations.
- Licensed parties who fund Elexon: generators and suppliers. This has similar advantages to above, in that all parties would be given a licence obligation, with the additional advantage that there are fewer parties involved. This smaller membership would make implementation and maintenance of the ownership structure easier, as co-ordinating parties to undertake relevant tasks would be less onerous.
- Voting Parties: all licensed parties, plus some non-physical traders. This carries the advantage that there is an existing decision-making forum that already votes on certain matters under the BSC and could take the shareholder decisions required to ratify a code modification in the same meetings. However, it has the disadvantage of being a wider range of parties than licensed, funding parties, including some parties who are not licensed, meaning licence obligations could not be placed on all new shareholders.

Whilst all of the options are viable and given that ownership does not confer control in accordance with the existing BSC governance arrangements, we recommended that the key considerations in deciding on a sub-set should be ease of implementation and the sub-set's resilience to change as parties join and leave the cohort. Implementation would be most effective if the group is relatively small, and all the new owners are licensed. Our preference was therefore that the new shareholders be the licensed, funding parties, i.e. generators and suppliers.

Summary of Stakeholder Response

The majority of respondents agreed that the BSC Party sub-sets proposed in the Consultation would be viable shareholder groups for Elexon under industry ownership. Many agreed that licensed, funding parties should be the shareholders, largely as this option would make implementation of the ownership structure easier. A small number of respondents highlighted the additional point that this sub-set was most appropriate due to suppliers' and generators' activities being more directly related to Elexon's BSC settlement services.

Some stakeholders preferred all licensed parties as shareholders. They considered it was important to include organisations, such as the System Operator and the DNOs, which are funded by the electricity Transmission and Distribution Price Controls, and which may therefore be more financially stable than suppliers and generators.

Some respondents preferred a sub-set of licensed, funding parties as shareholders. A smaller group was considered necessary due to the diverse characteristics of suppliers and generators; for instance, some may have specific financial or corporate governance structures which could make it particularly onerous to take on a share. In addition, it was noted that a larger group could make implementation harder due to the complexity of coordinating more parties.

Some thought that parties should take on the shares in a voluntary capacity as opposed to this being mandated through a licence condition. A small number considered that a voluntary approach was important for ease of implementation, as parties which could find it difficult to take on shares due to specific financial or corporate governance structures would not be mandated to do so.

Government/Ofgem Response

Some respondents suggested that all licensed BSC Parties could become shareholders. As outlined in the Consultation, we believe that this option is worth consideration as implementation and enforcement would be easier if all the new owners are licensed.

In the Consultation, we also stated that along with holding licences, a smaller group size for the Elexon shareholders is preferable as this simplifies implementation, and we have seen no evidence or arguments to change our view on this. As such, we stated that our preference was the licensed, funding parties (suppliers and generators) over the group of all licensed parties, as the former represents a smaller cohort.

Furthermore, due to suppliers' and generators' activities being more directly related to Elexon's settlement services than those of other licensed parties, we consider that these BSC parties would adjust more quickly to the shareholder role and be better prepared for implementation.

Taking this into account and the fact that the licensed, funding parties represents a smaller group than all licensed BSC Parties, we recommend that the new shareholders be licensed, funding BSC Parties.

Should all licensed, funding BSC Parties own shares or a sub-set of them?

Despite alternative shareholder options being proposed, there was consensus amongst the majority of respondents that licensed, funding parties as shareholders was the most suitable group. We maintain the argument made in the Consultation for preferring licensed, funding parties over any other group.

We acknowledge however the preference of some respondents for a sub-set of licensed, funding parties to take on shares due to the importance of ease of implementation and have refined our position on this basis. We examined two policy options: the full group of all licensed, funding parties, and a smaller sub-set of licensed funding parties against the policy criteria to understand whether refining our preferred option to a smaller grouping of suppliers and generators would be more appropriate; and considered how we might select a sub-set.

Within this assessment, we recognise the consideration raised by respondents: that the parties within the whole licensed, funding group vary significantly in characteristics such as funding share, resource availability and relationships with industry and government bodies. A larger group would include more parties which may have less capacity or lack regulatory teams/advisers which would aid with completion of implementation tasks. In addition, the practicability of coordinating tasks for implementation in sufficient time for a larger group could also be more onerous for both BSC Parties and government. There would be more associated costs for all stakeholders because of this, including costs which are passed through to consumers and to BSC funding parties. In turn, by limiting the number of shareholder parties, we are reducing costs for all affected.

Moreover, administrative work presents itself not only immediately during implementation but also in future once the new structure is in place. If a larger group contained mandated parties who had limited capacity to engage with Elexon, future administrative tasks (for example, approval of Articles of Association changes for Companies House) could become more difficult.

Overall, having a larger group would likely be more disruptive to Elexon's business as usual activities both in the short and longer term as it would have to dedicate greater resource to establishing and maintaining the ownership structure. This means higher costs, and more uncertainty.

From this analysis, we conclude that having a sub-set of the licensed, funding parties become shareholders meets the policy criteria to a greater extent than all licensed, funding parties. **Therefore, our policy decision is to have a sub-set of licensed generators and suppliers take on shares.**

Identification of a sub-set of licensed, funding parties

This assessment highlights that there are two key characteristics which the sub-set of licensed, funding parties should have to aid the shareholder group in meeting the policy criteria:

- Organisations with a large funding share: BSC Parties with large funding shares in Elexon have greater resources for implementing the new ownership structure, undertaking ownership obligations and to deal with any future changes. This is further aided by having additional teams/advisers which work with Elexon due to their funding share and size.
- Organisations with diversity across licence classes. There is a small risk that, with only a small sub-set of BSC Parties owning shares, changes in the structure of the energy market could lead to organisations with one particular business model (e.g. supply or generation) being disproportionately affected. Although we consider this eventuality to be unlikely, the risk of it happening can be further reduced if the sub-set includes both suppliers and generators, as well as vertically integrated organisations, as a variety of business models would ensure greater resilience to market changes. We consider that such a cohort would provide greater stability to the Elexon ownership structure.

The funding shares, paid by suppliers and generators, cover around two-thirds of Elexon's costs. The other third of the BSC costs are covered by a flat-rate tariff-based system. The funding shares are calculated for each BSC Party depending on the amount of electricity that they generate or supply over a specific time period. This amount of electricity then determines what share of the two-thirds of Elexon's costs they are required to pay. Parties which generate or supply more electricity pay a larger proportion of the costs². Funding shares are hence a good indicator of size of organisation and interaction with Elexon's settlement services.

Using the published data for each party's funding share in Elexon, it is evident that the majority of Elexon's funding is provided by small number of suppliers and generators. As of January 2023, only 20 BSC Parties have a funding share greater than 1%, and these parties contribute over 87% of Elexon's total funding.

As outlined above, a suitable sub-set requires BSC Parties with large funding shares and organisations with various different licence classes. This means a reasonable number of suppliers, of generators, and of organisations whose business integrates both licence types. Additionally, however, the sub-set needs to be small enough to reduce administrative tasks which could impact implementation and increase costs. This helps to ensure criteria one, minimising disruption to Elexon's activities, and criterion two, adhering to the FSO implementation timeline, are met.

Licensed, funding parties with a funding share above 2%

We have conducted analysis of the groups of licensed, funding parties that would be produced by setting the boundary at each 0.5% increment in funding share in order to identify which increment produced a small sub-set with diversity of licence classes. We carried out this analysis against the January 2023 data set.

This analysis showed that when we considered licensed funding parties with funding share above 3%, although the group was small and therefore reduced the implementation burden, it would not ensure resilience to market change (criterion 4) to the same extent as the 2/2.5% funding share group. The 3% subset contained predominantly generators and firms with integrated business models involving supply and generation, but few suppliers. As above, we consider that less diversity in licence classes held by the shareholding group is likely to reduce the resilience of that group to market change.

Comparatively, it was apparent that a sub-set group of licensed BSC parties with a funding share over 1% would contain at least as much diversity as drawing the line at a larger 0.5% increment, but by introducing extra mandated shareholders without commensurate material benefits in diversity, it would increase the risk of disrupting Elexon's activities or the FSO timeline, and it would increase implementation costs.

The subsets of parties with a funding share above 2.5% and the subset of parties with a funding share above 2% are the same. No funding parties had a funding share between 2% and 2.5% in January 2023.

Based on this rationale and analysis against the policy criteria, **our policy decision therefore is that the licensed, funding BSC Parties with over 2% funding share represent the**

² <https://bscdocs.elexon.co.uk/guidance-notes/funding-shares>. Data on the funding shares of suppliers and generators can be found on the Elexon Portal; a site that provides operational BSC data: <https://www.elexonportal.co.uk/news/latest?cachebust=rrtzsgfrj>.

group which is most appropriate to be the initial cohort of mandated shareholders of Elexon.

The list of 13 licensed, funding BSC Parties with over 2% funding share as of January 2023 (in order of size of funding share, starting with the largest and decreasing in size moving down the list) is as follows.

EDF Energy Limited
E.ON UK Energy Markets Limited
British Gas Trading Limited
RWE Generation UK Plc
SSE Energy Supply Limited
Orsted Salg and Service AS
Scottish Power Energy Management Ltd
Drax Energy Solutions Limited
Uniper Global Commodities SE
Ovo Energy
Octopus Energy Limited
Drax Power Limited
TotalEnergies Gas and Power Limited

These 13 parties make up just over 76% of Elexon's total funding shares, which is a substantial percentage.

We have used the funding shares for January 2023. This data set is based on BSC charges 1st January 2022 to 31st December 2022. We believe this is the most appropriate data set to use for three reasons:

- 1 Using a full calendar year's data ensures that seasonality is not a factor in parties' funding shares (e.g. if some parties have greater levels of activity in a certain part of the year).
- 2 This is the last full calendar year before we intend to implement this policy. This means the data set accurately reflects the current state of the energy market.
- 3 By using a data set that is published on the Elexon Portal prior to the publication of this document, we can give certainty today on which parties will be becoming shareholders.

Implementation Approach

We maintain that shareholders being mandated to take on a share with a licence condition is the most appropriate implementation approach.

Reflecting on comments from respondents, we considered the possibility of a small sub-set of licensed funding parties taking on shares in a voluntary capacity. There is a risk with a

voluntary approach that insufficient parties would take on a shareholding in a timely way. There is also the possibility that parties in a voluntary cohort all face exposure to similar risks in the wider market. For instance, if there was a lack of diversity of licence holders in the grouping and there were changes in the market which disproportionately impacted a certain class of licence holder, the stability of the sub-set could be reduced. These risks mean that this implementation approach does not meet the policy criteria for Elexon ownership as well as mandating a small sub-set of licensed, funding parties does.

We note under question 6 that many respondents wanted the Government and Ofgem to prioritise swift and low effort implementation to minimise disruption. The mandatory approach is designed to ensure this is facilitated. Under such an approach, using licence obligations establishes a direct regulatory route of oversight and enforceability of implementation tasks and ownership obligations. It also places appropriate emphasis on the importance of the shareholding, which should facilitate the new shareholders gaining internal and external consents to acquire shares. Overall, such an approach ensures alignment with the FSO implementation timeline and minimal disruption to Elexon's activities.

As stated above, share ownership does not confer control, therefore we do not consider that there is a risk that shareholders will benefit from additional influence beyond that of other BSC Parties. However, if any other parties are concerned by the perception that they might do, we believe this can be alleviated if those parties are able to apply to Elexon to acquire a share after the transfer of shares to the group listed above. This will be subject to detailed rules set out in the BSC modification and the Articles of Association of Elexon. This is in line with the approach taken by RECCo. We do however believe that this ability should be restricted to licensed parties. This is because these parties have a licence condition to comply with the BSC, which allows Ofgem to ensure they comply with the restrictions on shareholder control as outlined in the BSC.

Our policy decision is therefore that we would provide for licensed, funding parties with a funding share of over 2% on 1 January 2023 to be required to hold Elexon shares on an enduring basis.

There is a possibility that over time the initial group of mandated shareholders could reduce in size due to firms exiting the market to a sufficient extent that the number of shareholders becomes too small. To avoid this, we intend to make provision for any of the 13 largest funding parties by funding share from time to time to be required to take a share if the shareholder cohort falls below 13 parties. The assessment of the 13 largest funding parties would be based on the most recent annual data as reported monthly at that time. This does not require that the largest 13 funding parties always hold shares and does not affect any party beyond the largest 13 funding parties. It means only that if, and only if, the number of mandated shareholders drops below 13, there will be provision to top the group back up to 13 by requiring the largest parties that do not already hold shares at that point in time to acquire shares (in addition to the remaining shareholders). This policy ensures that Elexon can never have too few shareholders.

If a party with a funding share of over 2% as of 1 January 2023 had their funding share drop below 2% at a later point in time, that party would still be required by their licence to keep the share unless directed otherwise by Ofgem of the DESZN SoS.

2.4 Question 4 – Enduring ownership option

To what extent do you agree with the above analysis of the two main ownership options, public ownership and industry ownership, and our preference for industry ownership?

Consultation position

The Consultation assessed the risk and benefits of both industry and public ownership options against the criteria set out above. We concluded that the two ownership options met these four criteria to a sufficient extent. Without a clear rationale or market failure which might be solved by the creation of a public body, our preferred enduring option in the Consultation was industry ownership for Elexon.

Summary of stakeholder response

The majority of respondents agreed with the preference for industry ownership as the enduring ownership option, with a few outlining that industry ownership would cause the least disruption to Elexon's core BAU operations and implementation of industry policies, including the digitalisation of a smart and secure GB electricity system. It was also considered to be the most effective solution to mitigate risks of disruption to the FSO delivery timeline.

There were some respondents however who cautioned that the analysis downplays potential risks of industry ownership. Areas noted include impacts on Elexon's wider programmes, legal and administrative costs that may be incurred by new shareholders and lack of details on shareholder liabilities. The liabilities with which respondents were concerned were potential liabilities arising from deficits in pensions, and any potential liabilities that could arise if Elexon were to become a licensed Code Manager (as part of Code Reform) subject to regulatory fines.

With regard to preserving Elexon's accountability and independence under industry ownership, comments were largely positive, with some respondents contending that the maintenance of Elexon's existing governance arrangements would ensure this. Concern however was raised by a small number of respondents that industry owners could exert undue influence on BSC policy.

Some respondents commented that industry ownership would offer more resilience to future change compared to the public ownership option. This was due to the view that industry ownership could ensure that Elexon's procurement, remuneration, staffing and recruitment arrangements remain, and that under public ownership there could be administrative and resource restrictions, as well as inflexible procedures, which ultimately could impact Elexon's BAU activities.

Government/Ofgem Response

We acknowledge the concerns surrounding possible impacts to Elexon's wider programmes, as well as those regarding shareholders having undue influence on BSC policy. Given that governance, funding, and operational arrangements will not change beyond consequential changes to implement the change in ownership of shares, we are confident that the change in ownership will not give the future shareholders any additional direct or indirect control. With regard to the first policy criterion, minimising disruption to Elexon's business as usual (BAU)

activities, our position remains that neither ownership option would hinder the delivery of Elexon's core responsibilities as detailed in section 2.3.

In line with respondents' feedback and our previous assessment in the Consultation, we remain of the view that both ownership options can be implemented within the FSO implementation timescale. Industry ownership may require greater coordination, agreement, and mobilisation of industry stakeholders; however, we believe that any associated risks can be mitigated in our implementation arrangements, including the choice of shareholder sub-set and the proposed fallback option.

In assessing the third criterion, preserving accountability to industry and independence, we remain confident that existing governance arrangements will safeguard against potential undue influence on the BSC arrangements and Elexon's operational and strategic independence. We agree that industry ownership would not create significant disruption to the efficiency of Elexon's current administrative, procurement and remuneration procedures, and acknowledge views that this would support the retention and recruitment of staff and support Elexon's resilience to leverage existing knowledge. No respondent has provided evidence that the choice of shareholders would change Elexon's existing accountabilities.

We believe that both industry and public ownership options would be resilient to the impact of, and be sufficiently flexible to accommodate, future code reform. The management of potential conflicts that could arise in future if Elexon is selected to be a code manager will continue to be considered. There will also be opportunities for Elexon and its shareholders to engage with future consultation processes on code reform.

Overall, we have not seen any evidence to reassess our view that both options meet the criteria to an adequate extent, with the added consideration that industry ownership could enable greater flexibility for Elexon's operations. In the absence of a clear rationale to create a public body and the lack of evidence of a market failure under existing private ownership arrangements, **our policy decision is that the enduring option be industry ownership.**

Concerns regarding shareholder liabilities are addressed in section 2.6.

2.5 Question 5 – Fallback option

To what extent do you agree with our proposal that Elexon should transfer temporarily into the public sector as a subsidiary of the FSO as a last resort, if industry ownership was chosen following consultation but could not be implemented without delaying the creation of the FSO? Please explain why.

Consultation Position

If we were to decide, post-consultation, to implement the industry ownership option, we would also need to understand how quickly it could be delivered, as it will require careful coordination across many different parties. There is a small risk that this process could delay the wider changes proposed to ownership of the FSO. In this case, we suggest mitigating the risk of disruption by deploying the public ownership option as a temporary fallback option. The fallback option would only be implemented if it became apparent that industry ownership could not be implemented before the FSO contract signature date.

Summary of Stakeholder Responses

Many respondents agreed with our proposal that Elexon should transfer temporarily into the public sector as the fallback option. A small number reiterated however that if adopted, there needs to be a time limit imposed so that it does not continue for longer than needed, if for example, it was difficult to extricate Elexon from public ownership once it has transferred, or it is perceived to be simpler to keep Elexon in the public sector once the change in ownership has been established. Additionally, some respondents noted that all possible steps should be taken, to avoid the need to use the temporary fallback option.

Some also disagreed with this proposal, with a few wary of the inefficiencies and associated costs and work stemming from changing the ownership of Elexon twice and putting any public sector controls in place for a short period. Related to this, there was concern by a small number that Elexon's contracts, procurement, staff retention and recruitment could be impacted due to the uncertainty created. A small number of respondents viewed any form of public ownership of Elexon as a risk to the continued industry focus or believed it would put the BSC at risk.

It was noted by some respondents that the temporary fallback option could be better placed in the private sector, such as another part of National Grid plc owning the shares in Elexon. The reasons given were consistent with the concerns about public ownership set out above.

Government and Ofgem Response

The feedback from respondents shows that whilst there are concerns about the temporary fallback option, in particular about the inefficiencies and costs which may arise, there is recognition that it is important to maintain the option in order to protect FSO timelines. We acknowledge comments that there could be additional costs to adopting it and maintain that whilst it is essential to have it as a contingency, this option would only be used if it became apparent that the implementation of the enduring ownership option posed a risk to timelines for the establishment of the FSO, as the fallback option is only a temporary solution to prevent delaying the progress of the FSO project overall. The fallback option would therefore only be implemented under very defined circumstances, namely that transferring Elexon ownership from NGESO to industry takes longer than anticipated and risks impeding the progress of creating the FSO.

We also recognise comments that all steps should be taken to ensure the fallback option is not needed, and if it is, that it should only be in place for as short a time as possible. We agree that it is important to mitigate the need for adopting this option. In order to do so, we set out under question 3 the shareholder grouping and implementation approach we propose to reduce the likelihood of needing to use this option. In addition, we are prioritising implementation planning to minimise this risk. With respect to the potential timeframe if this option were exercised, an estimate will only be possible once the circumstances and any variables are ascertained.

We recognise respondents' objections to using the public fallback option, however we do not believe it would be more straightforward for the temporary fallback option to be in the private sector. Moving Elexon's share within National Grid plc's corporate structure is not a straightforward process, and it would be necessary to make NGET a signatory for the BSC temporarily just for this purpose, and then remove them following the transfer to industry parties.

For these reasons, our decision remains for Elexon to move into public sector as a subsidiary of the FSO as a last resort if industry ownership cannot be implemented without delaying the creation of the FSO. Government and Ofgem will work with Elexon and industry to ensure the

enduring option can be implemented to align with implementation of the FSO and the need for the temporary fallback option is therefore avoided.

At present, our intention is to make a decision on whether such a step is necessary in or around late summer 2023. This is an indicative timeline, subject to change based on wider FSO implementation project planning. The decision will be based on progress against implementation (see section 4 on next steps) with a particular focus on whether the new shareholders have gained the necessary internal and external approvals to acquire a share.

2.6 Question 6 – Implementation proposals

Are any other changes required to implement either of the two ownership options?

Consultation position

In the Consultation, we set out the aspects required for implementation for both ownership options. This included stakeholder engagement and additional administrative tasks required by industry and government. We asked whether respondents had identified any other key implementation tasks that we had not covered.

Stakeholder Response

The majority of respondents thought that all considerations for implementation had been considered and that we had covered the key areas.

Some respondents wanted greater information on the liabilities the new shareholders could face. Respondents said both that the potential future owners would need more information on what the potential liabilities are; and asked the Government or Ofgem to provide either assurance that the liabilities are not an issue, or some form of protection. They suggested this could be some form of indemnity, or another type of coverage, such as wording in the BSC to exempt shareholders from these liabilities.

Additionally, stakeholders suggested that Elexon, the Government, or Ofgem needed to coordinate implementation tasks. Some respondents noted under Consultation question 1, question 6, or question 8 that they felt minimising disruption and implementing the new ownership structure quickly was essential and that disruption could be minimised by coordinating all the actions that the new shareholders need to take.

Related to the policy criteria specifically, a few respondents requested it to be ensured that all of Elexon's BAU operations were protected, not just core BSC work.

Government/Ofgem Response

We recognise respondents' concern about financial liabilities. We wish firstly to reiterate that the BSC currently removes any obligation on NGESO to provide shareholder funding. We will ensure that the BSC, similarly, contains wording **removing any obligation on the new shareholders to provide funding to Elexon** so that new shareholders have the same protections NGESO has currently. We do not believe, in light of this commitment, that it is necessary or useful for any further indemnity to be provided to the shareholders. The BSC already ensures that BSC Funding Parties are responsible for all costs, not shareholders.

Some shareholders raised specific issues with regard to pensions liabilities, and with regard to potential costs that could arise following code reform.

Regarding pensions liabilities, our policy is that **all pension costs and liabilities relating to Elexon's employees be borne by Elexon** following the implementation of the new ownership arrangements and funded using the existing funding arrangements. This is in line with Elexon's existing funding arrangements, including as regards employment and pensions costs, and it means that costs will be passed on to BSC funding parties as they are currently.

With regard to concerns about code reform, we note that the approach to selecting code managers and the content of the code manager licence will be consulted on as work to implement energy code reform progresses. However, in the April 2022 government response to the consultation on Code Reform, we noted that we believed code managers should be funded through charges levied on code parties in accordance with a charging methodology in the relevant code(s). This will be consulted on further in due course, and future shareholders will have a chance to feed into relevant consultations related to code reform that may impact Elexon.

DESNZ and Ofgem agree that it is essential that implementation work is coordinated carefully to ensure efficient implementation and minimise costs, so **will take on a central role in coordinating implementation**. The specifics of our implementation strategy, including the use of licences and codes to implement the new ownership structure, therefore remain unchanged and we will directly contact organisations involved to agree detailed plans.

Finally, we agree that Elexon's wider functions are also essential, and we considered all of Elexon's BAU operations, such as work on the Energy Price Guarantee, not just core BSC work, when conducting policy analysis using the criteria set out under question 1.

2.7 Question 7 – Licence and code changes

What are your views on the proposed licence and code changes set out above?

Consultation Position

In the Consultation, we set out proposals for licence and code changes. We proposed that the new shareholders should receive a licence condition obliging them to take a share in Elexon and that parallel wording should be removed from NGEN's licence.

Summary of responses

Some respondents expressly agreed with our proposed changes. The majority of respondents provided comments which indicated broad support for our proposed approach.

A small number of respondents suggested making ownership a requirement of the Code (if implementing the "all BSC parties" option) as opposed to using licence conditions to impose it.

Some respondents articulated concerns about the potential for liabilities to fall to Elexon shareholders, similar to those described in section 2.6. We respond to these concerns there.

Some respondents commented on timescales and links with Energy Code Reform work. Points were made on the need to co-ordinate timescales with Energy Code Reform work and

to take account of uncertainties regarding Elexon’s function if it were to become a Code Manager.

Government/Ofgem Response

We continue to believe that our proposed licence and code changes are appropriate to deliver new ownership arrangements for Elexon. We acknowledge the suggestions for using codes instead of licences to implement new ownership arrangements, in particular the suggestion for making ownership a requirement of the code if implementing the “all BSC parties” option. However, in light of our decision (see section 3.2) that a sub-set of licensed funding parties rather than all licensed funding parties will be mandated to own shares, we believe that a licence condition would be a direct and effective route by which Ofgem could enforce a requirement that parties identified as the new shareholders of Elexon hold shares.

We note the comments on the need to co-ordinate timescales with Energy Code Reform work. We recognise the need to ensure that the proposed changes are robust to Code Reform and we are working very closely with the Code Reform teams in DESNZ and Ofgem to compare implementation timelines and sequence associated activities accordingly.

We intend therefore to introduce a licence condition enabling DESNZ or Ofgem to mandate the largest 13 parties to take on shares. To deliver this policy, we propose a standard licence condition in both the generation and electricity supply licences that is turned on by exception, through a direction process. This would give Ofgem/SoS the power to direct parties to take on a share as needed, consistent with this policy. It would also give Ofgem or DESNZ SoS the ability to provide exemptions to the mandate proposed in this document if a licensee was able to demonstrate that this was necessary. Such a licence condition could be used both to establish an initial cohort and to top up a cohort to the same number of shareholders as in the initial cohort.

2.8 Question 8 – Costs and benefits

Have we considered all relevant costs and benefits of these proposals? Please state why.

Consultation position

In the Consultation, we outlined the costs and benefits of both ownership proposals. We stated that for both options, the main costs would likely only be the operational costs borne by organisations involved in implementing and maintaining the new ownership structure, and that these would not be significant. Under the public option, the costs of implementation would be similar, but a higher portion of the costs would fall to the Government, whereas industry would cover a greater amount of these under industry ownership.

Stakeholder Response

Some respondents indicated that we had captured all of the main costs and benefits. A similar number however indicated that we had not, with the most fundamental concern being that we had not fully accounted for the potential costs to industry. This related to the same issue addressed in section 2.6 that more information with respect to pensions liabilities and code manager fines is required.

Respondents generally agreed with our assessment that the implementation costs were both minor and necessary to secure Elexon's continued success. A small number of respondents reiterated the additional point made in relation to question 6, that the Government, Ofgem, or Elexon should take on a coordination role to ensure industry parties don't duplicate work. This was considered necessary as duplication would increase overall costs.

A small number of respondents also stressed that the costs of public ownership are higher than we indicated in the Consultation. In particular, there were concerns that public ownership controls presented risks to Elexon's operations, and that it was consequently argued that these must be avoided, even if public ownership is only adopted as the temporary fallback.

Government/Ofgem Response

As discussed under Question 6, we agree with the recommendation that the Government, Ofgem and Elexon reduce costs by taking a coordination role and we have planned our implementation strategies in accordance with this. We discuss shareholder liabilities in section 2.6.

With respect to the concern that costs under public ownership are higher than our analysis suggests, we maintain that the public ownership option would not impact Elexon's BAU activities or independence, given that the only thing that is changing is the owner of the shares and not any governance arrangements.

However, we do acknowledge the importance of mitigating risks to Elexon's BAU operations, and we have taken these into account when using our policy criteria to inform the policy analysis and decisions.

3 Policy decisions

In this section we reiterate the policy decisions for Elexon's ownership with respect to the enduring ownership option, the proposed industry shareholders, the fallback option and the licence and code changes required for implementation.

3.1 Enduring ownership option

Overall, we have not found any evidence to reassess our view that both options meet the criteria to an adequate extent. Additionally, we recognise that industry ownership is the best model for Elexon's future service delivery, independence and resilience, in comparison to the public option.

Under the public ownership option, Elexon would enter public ownership as its own public body. New public bodies should only be created if there is a clear and pressing requirement and no viable alternative. Given the lack of a market failure or other rationale to create a new public body, and the consideration that industry ownership can meet the policy criteria to a slightly greater extent than the public ownership option, **our policy decision is that the enduring option be industry ownership, as a company limited by shares.**

3.2 Proposed shareholders

We maintain that the licensed, funding BSC parties becoming shareholders is the most appropriate option in comparison to the other broad groups proposed in the Consultation, as this group aids implementation, preservation of Elexon's BAU activities and resilience to change best.

Reflecting on respondents' comments, we considered if a refinement in our approach to focus on a sub-set of licensed funding parties would be more appropriate than all licensed funding parties becoming shareholders. Following analysis of these options against the policy criteria, **our decision is for the licensed, funding BSC parties with over 2% funding shares to become the shareholders**. Such a sub-set best meets our criteria because it includes organisations with large funding shares, sufficient diversity of licence holder class to be resilient to market changes and is of appropriate size to reduce administrative burden.

Regarding implementation, our position remains that taking on a share should be mandated through both a code and licence condition, as such an approach provides a direct regulatory route for oversight of implementation progress and enforcement of ownership obligations. This is of importance for meeting the policy criteria.

3.3 Details of the shareholding structure

Shares will initially be transferred to the sub-set of licensed, funding parties with over 2% funding shares. After this initial transfer, the option will be open to licensed parties to request a share from Elexon, subject to rules set out in the BSC modification and the revised Articles of Association of Elexon. This sequential approach minimises any risk to timelines for the establishment of the FSO. We believe it is only appropriate for licensed parties to take on shares, as their licence condition to comply with the rules set out in the BSC gives Ofgem a clear enforcement mechanism if any shareholder should not follow the restrictions placed upon them by the BSC to, for example, not interfere with Elexon's independent governance processes.

There is a possibility that, once we transfer shares to the largest 13 licensed, funding parties, over time this group could reduce in size due to firms exiting the market to a sufficient extent that the shareholding became too small. To avoid this, **DESNZ and Ofgem will have the ability to require that any of the 13 largest BSC funding parties at any point in future acquire a share to restore the number of mandated shareholders to up to 13**. If a party with a funding share of over 2% as of 1 January 2023 experienced a reduction in their funding share below 2% at some future date, that party would still be required to retain their share in Elexon unless directed otherwise by Ofgem or DESNZ SoS. It means only that if the number of mandated shareholders drops below 13, parties amongst the largest 13 at that point in time not already holding shares may be required to hold one. This policy ensures Elexon will retain a sufficient number of shareholders in future.

Given that shares do not grant any form of control over Elexon, there is no reason for firms to hold more than one share; and no benefit of doing so. Therefore, each shareholder will only be able to hold one share.

3.4 Temporary fallback ownership option

Our decision is for Elexon to move into the public sector as a subsidiary of the FSO as a last resort if industry ownership could not be implemented without delaying the establishment of the FSO.

Triggering the use of the temporary fallback option, if it is needed, at the correct point will be very important to ensure that there is still time for the change to occur without affecting FSO implementation timelines.

We envisage that if the fallback option were triggered it would likely be in late Summer 2023. This would happen in the scenario that the new shareholders had made insufficient progress on implementation, focused in particular on any internal and external approvals they needed to obtain. We would focus on whether the sub-set was ready to a sufficient extent to meet the policy criteria we set out in this document in time to protect the FSO timeline.

Exact deadlines will be agreed with the proposed shareholders as part of joint implementation planning in the next phase of the project.

3.5 Licence and code changes

In light of our decision that a sub-set of 13 licensed funding parties comprising those that provide the greatest share of Elexon funding as of 1 January 2023 would form the initial cohort of shareholders, our policy decision is to introduce a licence condition that will provide for creating such a cohort.

It is possible that some or all of these parties taking shares initially could exit the market in future. Our policy is to have the ability to maintain a cohort of up to 13 mandated shareholders. Accordingly, we intend to introduce a licence condition such that we may require any of the 13 largest funding parties by funding share to take a share if the shareholder cohort falls below 13 parties. The assessment of the 13 largest funding parties would be based on the most recent annual data as reported monthly at that time.

To deliver this policy, we propose a standard licence condition for electricity suppliers and generators that is turned on by exception, through a direction process. This would give Ofgem/SoS the power to direct parties to take on a share as needed, consistent with this policy. It would also give Ofgem or DESNZ SoS the ability to provide exemptions to the mandate proposed in this document if a licensee was able to demonstrate that this was necessary. Such a licence condition could be used both to establish an initial cohort and to top up a cohort to the same number of shareholders as in the initial cohort.

We intend that provision be made in the BSC to align with our decisions as regards ensuring shares are available for the initial mandated shareholders, setting out a process for future applications by potential voluntary shareholders and managing restrictions on dealings with shares by shareholders as market participants enter or exit the market or circumstances change.

It is also our intention that the BSC will contain wording removing any obligation on the new shareholders to provide funding to Elexon, noting the provision for no obligation to finance as currently set out in the BSC in respect of the current Elexon shareholder.

It is our intention that the BSC would set out the rights and responsibilities of the shareholders and these provisions would mirror those currently in the BSC in relation to the existing shareholder.

In the Consultation we stated that we propose to place on new shareholders an obligation to co-operate in the maintenance of Elexon as necessary. It is our intention to mirror current arrangements in respect of shareholder of the Retail Energy Code Company (RECCo) as currently set out in the Retail Energy Code (REC). In the case of REC, Schedule 4 of the REC states that: “each Shareholder shall co-operate with the other Shareholders and execute and deliver to the other Shareholders such other instruments and documents and take such other actions as may be reasonably requested from time to time in order to carry out, evidence and confirm their rights under, and the intended purpose of, this REC Schedule”.

4 Next steps

Following the publication of this document, we will engage directly with the proposed 13 new shareholders to agree implementation plans with them; and discuss the steps they need to take to acquire a share.

Our implementation strategy is based on the clauses for the FSO within the Energy Bill, which is currently being considered by Parliament³, and accordingly subject to parliamentary progress. The Bill contains clauses for the FSO that would grant relevant powers to DESNZ and Ofgem to make the necessary licence and code changes for this project, as well as powers to ensure that Elexon’s employees retain access to their pensions and to create a Transfer Scheme for this transaction. A Transfer Scheme is a legal device, often used where businesses, or aspects of a business are to be transferred to or from other organisations. In this scenario, it will be used to transfer shares from NGEN to the new shareholders.

Currently, Ofgem plans to run a formal licence consultation on this modification in Autumn 2023, with informal consultation occurring from late Spring onwards. We are grateful for Elexon’s help preparing an appropriate code modification to implement the new shareholding structure.

We are aware that the new shareholders will have to seek approval from various internal and external bodies to acquire the shares. We will contact these organisations to begin discussions regarding this.

We will additionally ensure appropriate pensions arrangement are in place. DESNZ and Ofgem will also formally consult, in accordance with the Bill, on pensions matters and the necessary Transfer Scheme, later in 2023.

³ <https://bills.parliament.uk/bills/3311> Please note that in the Energy Bill, the FSO is referred to as the Independent System Operator.

This response is available from: <https://www.gov.uk/government/consultations/the-future-ownership-of-elexon>

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