



Department for  
Energy Security  
& Net Zero

# National Energy System Operator Licences Statutory Consultation Response

Summary of responses received and joint  
government/Ofgem response

August 2024



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Any enquiries regarding this publication should be sent to us at: [NESOproject@energysecurity.gov.uk](mailto:NESOproject@energysecurity.gov.uk) and [FSO@ofgem.gov.uk](mailto:FSO@ofgem.gov.uk)

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# Foreword Secretary of State

In an era marked by unprecedented challenges and opportunities within the energy sector, the establishment of the National Energy System Operator (NESO) represents a pivotal moment for the country. As we transition towards a more sustainable and resilient energy future, NESO will play a crucial role in ensuring the security, affordability, and environmental sustainability of our energy systems.

NESO will adopt a holistic approach to planning and operating our energy infrastructure. NESO's independence from commercial interests and operational control of the government will enable it to provide unbiased, expert advice on critical decisions that will shape our energy landscape for decades to come, including our mission to deliver Clean Power by 2030.

This document outlines the responses received from stakeholders to the statutory consultation on NESO's licences and the subsequent decisions made by the government and Ofgem. This collaborative effort underscores our commitment to transparency, stakeholder engagement, and the continuous improvement of our energy system.

As we move forward, NESO's role will be instrumental in achieving our net zero and energy security goals. By fostering innovation, enhancing system resilience, and promoting transparency, NESO will help navigate the complexities of our evolving energy system. We are enormously grateful for the valuable input from industry stakeholders, whose insights have been integral to shaping the future of NESO.

Together we embark on this transformative journey towards a cleaner, more secure, and more efficient energy future for the country.

**Rt Hon Ed Miliband MP**

Secretary of State for Energy

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# Foreword Ofgem

As the energy sector transforms, it will be critical that the right governance and institutions are in place to deliver an efficient, coordinated, effective and flexible energy system for all. The establishment of NESO is a crucial step towards achieving secure, affordable and clean energy in Great Britain and building a brighter future for our energy system that can fairly deliver net zero in consumers' interests, particularly the most vulnerable.

NESO will be a trusted, expert body with a key role in coordinating strategic whole system planning across gas and electricity sectors and providing independent advice to the government and Ofgem.

We are delighted today to publish our response to the NESO licence consultation. This publication helps to deliver one of the top objectives from our Multiyear Strategy and is a testament to what can be achieved when Ofgem, government and industry work together to deliver sector-transforming change.

The contents of this licence package establish NESO's core obligations and set out how it will interact with the rest of the sector. Included within this are NESO's responsibilities as the electricity system operator, its growth into whole system activities, and its mission-critical role delivering strategic planning across energy vectors. To protect consumers, we will regulate NESO and drive high-performance through its regulatory framework. We will also continue to work closely with government on the development of enhanced and new roles for NESO as system requirements evolve in the future.

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# Executive Summary

The Energy Act 2023 sets the legislative framework for a new, publicly owned National Energy System Operator (NESO).<sup>1</sup> NESO will take on responsibilities across electricity, gas and hydrogen, including all the existing functions of the Electricity System Operator (NGESO), to enable it to take an enhanced whole system approach to planning and operating the energy sector.

NESO will be independent not only of other commercial energy interests, but also from the operational control of government, serving as a trusted voice at the heart of our energy sector. It will drive progress towards our ambitious goal of creating a secure and decarbonised power system by 2030, taking on the crucial role of strategically planning our electricity and gas systems and networks and advising government and Ofgem.

The consultation published on 28 March 2024 ('the March consultation') sought feedback on the two licences intended for NESO and closed on 9 May.<sup>2</sup> This document sets out government and Ofgem's joint responses to the stakeholder comments received in response to this consultation, and the decisions taken by both organisations on the shape and content of the licences. Note that this document does not constitute a decision to grant the proposed licences or to make the proposed modifications to impacted licences. A final decision on the granting of licences and making the modifications to impacted licences is to be taken by the Secretary of State in sequence with a wider set of decisions to establish NESO. Once this decision is taken it will set the date for 'Day 1' when NESO will be created.<sup>3</sup>

This document begins with a summary of the consultation and the responses received. The following sections consider some of these stakeholder responses by theme, with a Government/Ofgem response. It should be noted that every comment raised by respondents to the consultation has been considered and direct responses related to the conditions of the licences should be contained in this document or within the Issues Log published by Ofgem. Alongside this document, Ofgem have also published consolidated versions of NESO's two new licences, amendments to existing licence conditions impacted by the creation of NESO, reasons and effects, and non-confidential stakeholder responses to our statutory consultation. Finally, we set out the next steps towards granting the licences (or treating the licence as granted) alongside the designation of NESO on Day 1.

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<sup>1</sup> Referred to in the Energy Act 2023 as the Independent System Operator and Planner (ISOP).

<sup>2</sup> [National Energy System Operator \(NESO\) licences and other impacted licences: statutory consultation](#).

<sup>3</sup> Day 1 is the effective date of designation of the ISOP. See the Next Steps section at the end of this document for more information.

# Summary of statutory consultation on NESO licences

The government is working with Ofgem to ensure NESO's licences set it up for success. NESO will have two licences through which it will be regulated by Ofgem:

1. an **Electricity System Operator (ESO)** licence covering its obligations regarding its electricity functions, and
2. a **Gas System Planner (GSP)** licence covering its obligations regarding its gas functions.

The March consultation considered the contents and drafting of NESO's two licences, a proposal to grant those licences (or treat as granted)<sup>4</sup>, as well as modifications to various existing licence conditions which will be required as a result of establishing NESO.

The consultation proposed that these two licences will be granted (or treated as granted) by the Secretary of State to NESO as the body to be designated as the ISOP, using powers created in the Energy Act 2023.

The consultation also provided background on the context, roles, rationale, and structure of these two licences and included draft licences for stakeholders to review.

This consideration of stakeholder responses to that consultation, is a joint document between government and Ofgem. Therefore, throughout this document, 'we' refers to the government and Ofgem collectively. Where relevant, we will indicate whether a consideration or decision applies to a single body.

Further, references to the 'Authority' and 'Ofgem' are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work.

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<sup>4</sup> Under the Energy Act 2023 s.167 the Secretary of State may, rather than granting the electricity system operator licence, direct that the current transmission licence is to have effect as an electricity system operator (ESO) licence, thereby maintaining continuity and retaining associated documentation and previous decisions. In this case, the new ESO licence would be 'treated as granted'.

# Summary of responses received

There were 24 responses to the statutory consultation, from a range of organisations across the energy industry. Organisations that responded included transmission and distribution network companies, generators, suppliers, gas transporters, investors and the system operator. Responses also came from trade organisations, representative bodies, consultants, public bodies, private individuals and other interested parties.

We are grateful to respondents to the consultation for taking the time to submit their views on our proposals. Given the large number of responses, this document focuses on the most common or relevant responses to each consultation question, rather than summarising every point made. We recognise the level of detail which sits beneath this and government and Ofgem have carefully considered all responses. An Issues Log, published by Ofgem alongside this main response document, is a log of the non-confidential responses that we received and our responses to each. The evidence and views provided, including those in any confidential responses, have informed our approach to decisions and next steps.

In the rest of this section, we outline the key themes and NESO design features that have emerged as a result of the consultation, and how we address these (where applicable):

- NESO performance regulation
- Accountability to stakeholders
- Energy Resilience and National Security
- Advisory Role
- Network planning
- NESO Transitional Service Agreements
- Future Roles
- Uniform Network Code Arrangements
- Other Impacted Licences

Alongside this consultation response document and the final versions of the NESO licences, Ofgem is additionally publishing as subsidiary documents and Annexes:

- amendments to the conditions of other licences impacted by the creation of NESO;
- the reasons and effects for NESO's new licence conditions and changes to other impacted licences;
- an Issues Log containing direct responses to comments related to the conditions of the licences; and
- non-confidential stakeholder responses to our statutory consultation.

Please see the final section of this document for a list of Annexes and documents that accompany this publication.



# Joint Government and Ofgem Responses

## 1. NESO performance regulation

### 1.1 Approach to developing NESO's performance regulation

A number of respondents provided comments on the development and implementation of NESO's performance regulation. They generally noted the importance of there being an effective and transparent framework for incentivising NESO's delivery of outcomes and efficient spending. They also sought greater clarity on the details of NESO's performance regulation, with some noting they were anticipating future consultations on this topic.

One stakeholder stated that key details of the performance framework were not present at the time of responding to the consultation (given Ofgem's plans to publish further details in associated documents to the licence) which had prevented them from developing a full understanding of the regulatory framework. Another stakeholder noted that they expected more fundamental changes in regulatory approaches at this point to push the organisational changes that they believe will be required for the transition to NESO.

### **Government and Ofgem Response**

We agree that an effective regulatory framework will be key to the success of NESO. We also consider that the introduction of NESO is of fundamental importance to Government's wider energy system policy objectives and that there are substantial benefits from facilitating this at the earliest and most appropriate opportunity. As a result, and as outlined in previous documents<sup>5</sup>, Ofgem's performance regulation framework for NESO is being implemented in phases. This reflects that NESO will be introduced within an existing Ofgem price control framework (RIIO-2) and also within an existing business plan and performance evaluation period for NGEN.

Whilst we recognise that this means stakeholders do not have full clarity on NESO's long-term regulatory framework at Day 1, we consider this is justified by the benefits that will be unlocked from the timely introduction of NESO. We also note that a phased implementation approach to NESO regulation was supported by a substantial majority of respondents to Ofgem's December 2023 consultation on the future direction for NESO's regulatory framework ('Ofgem's December 2023 consultation').<sup>6</sup> As part of this consultation, Ofgem consulted on the key changes they planned to introduce at each development phase<sup>7</sup> and confirmed its plans for Day 1 in the March consultation.<sup>8</sup> We consider that these publications have enabled a meaningful consultation with stakeholders on Day 1 performance regulation.

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<sup>5</sup> See pages 22-23 of Ofgem's ['Consultation on the policy direction for the FSO's regulatory framework'](#) and section 6.3 of our [Statutory consultation on National Energy System Operator licences and other impacted licences](#)

<sup>6</sup> [Consultation on the policy direction for the Future System Operator's regulatory framework | Ofgem](#)

<sup>7</sup> Please see pages 22-23 of [Ofgem's December 2023 Consultation](#)

<sup>8</sup> Please see section 6.34 of the [March licences consultation](#)

Since the March consultation, Ofgem has published two further consultations setting out more proposals for the performance framework for NESO. In May, Ofgem published its consultation on associated documents to NESO's licence (the 'May Associated Documents' consultation), which set out fuller details of NESO's proposed performance regime that will run from Day 1 until the end of the RIIO-2 Business Plan 2 period (BP2) on 31 March 2025.<sup>9</sup> In August, Ofgem also published its consultation on its proposed changes for the final RIIO-2 business plan period from 1 April 2025 to 31 March 2026 (also as known as Business Plan 3 (BP3)).<sup>10</sup> Over the coming months, there will be several further opportunities for stakeholders to contribute to and shape the details of Ofgem's longer-term regulatory approach for NESO that will be introduced following the conclusion of RIIO-2.

## 1.2 Organisational-level incentives

Two stakeholders agreed the existing NGENSO financial incentives scheme was unlikely to be appropriate under NESO's not-for-profit model. However, two others were concerned about the lack of financial incentives at the organisational level for NESO and placing too much reliance on reputational incentives. One of these respondents shared their proposals for a financial incentives scheme where financial profits could be shared with staff and then returned to consumers or reinvested by NESO, depending on NESO's performance.

### **Government and Ofgem Response**

The majority of respondents to Ofgem's December 2023 consultation supported a not-for-profit framework for NESO which does not apply organisational-level financial incentives.<sup>11</sup>

Nevertheless, we recognise there are some remaining concerns from a few stakeholders about the absence of organisational-level financial incentives for NESO.

We remain confident that Ofgem can deliver effective regulation of NESO, by applying a combination of well-designed organisational-level reputational incentives and appropriate oversight of the policy for senior staff remuneration; and that this would deliver greater consumer benefits than an incentives scheme underpinned and driven by profit-maximisation. On this point we note that:

- The existing performance framework for NGENSO already places a large emphasis on reputational impacts given the use of a public performance assessment, combined with the relatively small financial value of NGENSO incentives to National Grid plc as a whole.
- Ofgem's experience has also found that aligning a profit-making objective with long term consumer interests is very challenging to achieve in practice for an organisation with the characteristics and objectives of NGENSO/NESO. This type of approach therefore risks undermining NESO's focus on achieving the right overall outcomes for the energy system and consumers (we discuss this further in Section 1.3 on staff incentives below).

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<sup>9</sup> [Consultation on Associated Documents to the proposed NESO licences – regulatory framework documents | Ofgem](#)

<sup>10</sup> [Consultation on NESO's performance incentives framework for BP3 | Ofgem](#)

<sup>11</sup> Please see the subsidiary documents section of Ofgem's consultation page for stakeholder responses: [Consultation on the policy direction for the Future System Operator's regulatory framework | Ofgem](#)

- In a model where the shareholder – the government – is not seeking profit or returns, it is unclear to us what benefits organisational level financial incentives would achieve. We consider Ofgem’s business planning and funding mechanism for NESO already sets an expectation that it should be seeking to maximise consumer outcomes, meaning there is limited rationale for further investment based on extracting profit. There are also risks with a scheme where a direct proportion of NESO profits would be shared with staff based on performance against cost and service targets (as discussed further in section 1.3 below).

### 1.3 NESO staff incentives

Some stakeholders commented on our licence proposal to require NESO to develop a staff remuneration policy (the ‘Remuneration Policy’), which would be approved by Ofgem. A couple of respondents considered that there should be transparency and visibility on the Remuneration Policy to provide industry with sufficient confidence.

One stakeholder proposed three alternative models for incentivising NESO which they considered could be implemented through Ofgem’s directions on NESO’s Remuneration Policy. These proposals generally involved more detailed regulatory specification on how staff incentives should be calculated. These models differed in nature, but a common theme was the calculation of staff incentives based on whether pre-defined cost and service targets had been met. This included a suggestion for underspend against cost budgets to be shared with staff through set sharing factors. The respondent believed these approaches were consistent with several comparator not-for-profit organisations to NESO, such as Welsh Water and Scottish Water.

#### **Government and Ofgem Response**

For the Day 1 and BP3 framework, as set out in the relevant NESO licence conditions<sup>12</sup>, NESO must demonstrate in its Remuneration Policy how it will take account of Ofgem’s performance assessments, and any instances of licence non-compliance, for senior management performance related remuneration. Ofgem will approve the Remuneration Policy and can direct NESO to further develop and resubmit this policy where it considers there is an insufficient link between Ofgem’s performance assessments for NESO and NESO’s senior staff incentives. We therefore consider NESO licences give Ofgem the ability to ensure a robust approach to staff incentivisation which is aligned with consumer interests.

We agree that it would be beneficial for there to be transparency over NESO’s staff remuneration approach, to help support stakeholder confidence. We have therefore amended the NESO licence conditions to make publishing the Remuneration Policy a licence requirement.<sup>13</sup>

We welcome the specific suggestions from stakeholders on potential approaches to staff incentives and will consider this feedback further as part of our review of the first iteration of

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<sup>12</sup> See Condition F7 of NESO’s ESO licence and Condition F5 of the GSP licence.

<sup>13</sup> Please see condition F7.4 (ESO licence) and conditions F5.4 (GSP licence).

the Remuneration Policy, which we expect to receive formally no later than one month following Day 1.

We consider there to be a need to strike a balance between ensuring alignment between regulatory performance schemes and NESO staff incentives, whilst also providing the NESO's board with sufficient independence and discretion to determine how to best set up NESO for success.

It is also important that the approach to financial incentives on staff is suited to NESO's specific characteristics. Over the last decade, Ofgem has moved away from incentivising NGESO through reliance on numeric or mechanistic targets, including the use of cost incentives with sharing factors.<sup>14</sup> This shift is after finding these to be an ineffective way of driving positive consumer outcomes for an organisation with the characteristics and objectives of NGESO. We believe there to be much greater value to be drawn from NESO's potential to impact wider energy system outcomes, than from achieving resource-efficiency improvements within its internal operations. There are several risks of adopting an overly mechanistic, target-based financial incentives approach, which are typically applied to more traditional, infrastructure-heavy regulated networks. These risks include:

- the risk of a disproportionate short-term bias to meet short-term targets;
- a perverse incentive to cut internal costs over providing overall consumer value;
- a perverse incentive to prioritise narrow, easily measurable outputs rather than adapting to achieve the best overall outcomes; and
- the risk of performance against incentives being disproportionately influenced (particularly for longer-term targets) by external factors, which can lead to the incentives losing credibility over time.<sup>15</sup>

Going forward, we expect NESO's roles and objectives will become more strategic and long term in nature, and involve more complex trade-offs, which would potentially heighten these risks. NESO will have a remit and objectives which are very different from a traditional capital-intensive energy utility or network company. We therefore think there needs to be caution in drawing conclusions from a package of incentives that apply to a water company and proposing these as an appropriate model to adopt for NESO and its staff remuneration. For example, Welsh Water's incentive targets (e.g. minimising water supply interruptions, reducing water leakage, and replacing lead pipes) are very different in nature to many of NESO's more strategic outputs, such as whole system network planning and the provision of expert advice on energy system development.

Ofgem intends to consider the approach to NESO incentives further as part of the development of a longer-term performance framework for NESO from April 2026. Ofgem intend to continue

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<sup>14</sup> See for example Ofgem's [Policy decision on the Electricity System Operator regulatory and incentives framework from April 2018 | Ofgem](#) and [RIIO-2 methodology for the Electricity System Operator – decision and further consultation | Ofgem](#)

<sup>15</sup> For example, see Ofgem's case study on lessons learned from the Balancing Services Incentive Scheme from its review of system operator incentives in 2017: [Future arrangements for the so - the regulatory and incentives framework 0.pdf \(ofgem.gov.uk\)](#)

to review comparators to NESO and the lessons from regulatory and incentive models used elsewhere.

#### 1.4 Day 1 regulatory oversight of NESO and consumer benefit

A few stakeholders noted the importance of there being robust oversight of NESO. A couple of stakeholders cautioned against putting too much faith in behavioural change that could result from NESO becoming a public body with statutory duties.

One of these stakeholders was concerned that Ofgem was proposing to lower its level of regulatory scrutiny from Day 1, on the assumption that as a public body NESO will perform better and that NESO's statutory duties are comparable to Ofgem's. They considered there was a mismatch in Ofgem and NESO duties in relation to consumers' interest, reinforcing the need for stronger oversight. They considered that the Day 1 licence proposals would set a weak and ineffective performance framework, and provided analysis to suggest this would lead to material consumer detriment. This means, in their view, the policy and licence condition proposals would not be compatible with Ofgem and the Secretary of State's objectives and duties.

#### **Government and Ofgem Response**

Ofgem is not intending to reduce its overall level of scrutiny of NESO performance for Day 1. As set out in the May Associated Documents consultation, Ofgem's proposed detailed approach to NESO's performance assessment from Day 1 is in substance a continuation to the existing approach applied to NGENSO for its BP2 period.<sup>16</sup> For the Day-1 framework, Ofgem is proposing to make targeted, incremental changes to streamline existing processes and direct regulatory focus on the areas that matter most for consumers. In other words, Ofgem is seeking to apply its same overall level of regulatory scrutiny more effectively. We note that Ofgem's December 2023 consultation was an early-stage consultation to inform a longer-term direction of travel for NESO regulation, and so stakeholders should not make the interpretation that the initial thinking on future performance incentives has been wholly adopted for Day 1. Ofgem is still carrying out policy development on the best approach to the longer-term regulation for NESO.

We have also considered the analysis of consumer detriment provided by one stakeholder. We consider that this analysis is incorrect for the following reasons:

- It is based on a theoretical assumption of the impact of an assumed-to-be-weaker incentive scheme, rather than being specifically linked to detailed policy proposals for Day 1. We believe this assumption does not bear sufficient reflection of our policy proposals for Day 1.
- It does not consider the specific characteristics of NESO and draws evidence of benefits from financial incentive schemes which apply to organisations with objectives and characteristics that are materially different to NESO (as discussed further in sections 1.2 and 1.3).

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<sup>16</sup> [Consultation on Associated Documents to the proposed NESO licences – regulatory framework documents](#)

- It does not consider the risks and downsides with the counterfactual used (a 'high-powered' financial incentive framework), including the potential problems with incentives that are overly reliant on the use of quantitative targets (as discussed further in sections 1.2 and 1.3).

We consider that Ofgem's incentive scheme changes for Day 1 are pragmatic changes that enable the timely introduction of NESO and maintain a robust level of regulation from Day 1. Establishing NESO will create significant consumer benefits, and so delaying this until the end of RIIO-2 (when a wider overhaul of the regulatory framework for NESO is more feasible) would not be in consumers' interests. Ofgem's future development of a longer-term regulatory framework will focus on how that framework can maximise consumer interests.

Ofgem and the Secretary of State both consider that the introduction of NESO and its licences are aligned with our respective objectives and duties. We acknowledge that NESO being a public body would not justify an immediate, automatic reduction in existing levels of regulatory scrutiny. As noted in the March, Ofgem believes that regulation of NESO needs to be dynamic, and where there are areas of ongoing performance concern, more detailed regulatory oversight may be needed. A key consideration as part of Ofgem's review of future regulatory changes will be the extent to which NESO has built and continues to maintain sufficient trust from Ofgem and its stakeholders.<sup>17</sup> For example, for Day 1 and BP3, Ofgem is continuing with its existing Cost Monitoring Framework, which applies detailed oversight of NESO's major IT investments. This will stay in place until past concerns identified through NGENSO's performance framework have been robustly addressed by NESO.

However, Ofgem's regulatory approach, and the processes used to assess NESO performance, do need to adapt in step with the fundamental nature of the organisation. There are processes built within the current NGENSO performance framework that were introduced to support a for-profit price control regime and which may not be appropriate in the future. Ofgem intend to continue to review what is needed to deliver effective regulation of NESO and look for opportunities to further improve on past processes. This is to ensure Ofgem's regulation is maximising benefits, unlocking the full potential of NESO, and focussed on tackling the biggest issues for the energy system and consumers.

In response to the stakeholder comment on NESO's statutory duties, we note that these were carefully considered to reflect the focus of its functions and are not intended to mirror either the duties of the Secretary of State nor those of Ofgem. The difference between these duties does not imply that NESO decisions may not be in consumer's interests; to the contrary, the interests of consumers are reflected in specific NESO duties. Ofgem's proposals for performance regulation for Day 1 have not been developed on the assumption that these statutory duties merit an automatic and immediate reduction in regulatory oversight. Nevertheless, we consider Ofgem's and NESO's objectives are objectively more aligned relative to the status quo for NGENSO, and the impact this could have is a relevant factor to consider further in the development of the longer-term regulation for NESO.

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<sup>17</sup> For example, see paragraphs 3.41-3.42 of Ofgem's consultation: [Policy direction for the Future System Operator's regulatory framework \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/policy-direction-for-the-future-system-operator-regulatory-framework)

## 1.5 Licence enforcement and minimum standards

A couple of stakeholders sought clarity on how we would ensure robust licence compliance for NESO under a not-for-profit framework, given the absence of financial penalties.

One stakeholder said that they thought the combination of what they considered to be a high-level licensing framework, with an enforcement framework, which they considered placed an over-reliance on public and reputational consequences, would result in an ineffective framework. The stakeholder called for the implementation of ‘minimum service standards’ in NESO’s licence to reinforce baseline obligations. It was also cautioned that Ofgem should not seek to create a policy that fetters its discretion in respect of the exercise of its powers of enforcement.

Another respondent commented on Condition C1 in NESO’s licences, which sets general expectations for how NESO should carry out certain functions. This stakeholder felt that there could be greater clarity in this condition, and that it required further review as the regulatory framework for NESO is developed.

### **Government and Ofgem Response**

As set out previously by Ofgem<sup>18</sup>, licence enforcement for NESO will follow the same broad process as exists today for NGENSO and other companies licensed by Ofgem. Ofgem will therefore be able to draw on (and does not preclude drawing on) existing enforcement options, as appropriate. However, as NESO is a not-for-profit body, the use of financial penalties as an outcome, whilst still possible, will become a less meaningful tool. This is because financial penalties would have limited consequence and instead be recycled through consumer bills. We consider that there would be a strong reputational impact to NESO in the event of enforcement action, noting that all enforcement outcomes would be public. As discussed above, we have also set requirements in the NESO licence that NESO’s Remuneration Policy shows how any instances of non-compliance with the licence or enforcement action by the Authority will be taken into consideration by NESO for senior management remuneration. As noted above, Ofgem has the power to direct NESO to make changes to the policy if it considers it to require further development.

We note one stakeholder’s view that the licensing framework is ‘high level’ and their suggestion for new minimum standards in the licence, as well as another respondent’s view that Condition C1 should be reviewed in future to improve clarity. We consider that the combination of overarching standards in licence condition C1 (General obligations on ISOP activities), specific additional thematic obligations elsewhere in Section C, and the proposed NESO Roles Guidance<sup>19</sup>, sets substantial minimum service standards across a range of different functions for NESO that are appropriate for Day 1. Ofgem plans to review the licence conditions and associated guidance as part of the development of a longer-term regulatory

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<sup>18</sup> See pages 19-20 of Ofgem’s consultation: [Policy direction for the Future System Operator’s regulatory framework \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/policy-direction-for-the-future-system-operator-regulatory-framework)

<sup>19</sup> [ISOP Roles Guidance \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/isop-roles-guidance)

regime for NESO, and we welcome any further specific suggestions for NESO activities that might benefit from additional minimum standards or areas where Condition C1 can be clarified.

## 2. Accountability to stakeholders

### 2.1 Stakeholder input into NESO business plans

A couple of stakeholders noted the importance of stakeholder input into NESO business plans. One of these stakeholders had concerns about Ofgem planning to adopt a 'light touch' business planning process. They called for either a more detailed review process (in line with the approach used for NGENSO under BP2) or a new 'negotiated settlement' approach. A concern was also raised that annual business plan periods could risk too much focus on the short term.

#### **Government and Ofgem Response**

Ofgem recently published its proposals for NESO's BP3 framework, including draft business plan guidance.<sup>20</sup> We consider the proposed approach is more closely aligned to the BP2 process than the 'light touch' process one stakeholder raised a concern about. The process requires NESO to engage with stakeholders to inform a draft version of its business plan and then formally consult on this draft plan before a final submission to Ofgem. Ofgem will perform an assessment of NESO's BP3 submission and consult on its determinations. Ofgem will continue to consider the merits of a more substantial change in approach, including the relative pros and cons of a negotiated settlement model, as part of its development of a longer-term NESO framework from April 2026.

In relation to business plan periods, we agree that it is important for there to be a focus on longer term outcomes. We consider this can be effectively achieved through our current licence proposals on business plans<sup>21</sup>, which require (when relevant) the submission of both forward-looking strategic aims and annual updates on priorities deliverables linked to those strategic aims. This approach can ensure the framework is responsive to the dynamic nature of the NESO's roles and that there is more regular, transparency on NESO's progress against longer term strategic aims. We expect that NESO's first major new business plan following the end of RIIO-2 in April 2026, will stand alongside a fully refreshed longer-term strategy.

### 2.2 Ability for stakeholders to input into and challenge decisions

A number of stakeholders highlighted the importance of there being processes available for stakeholders to input their views on NESO's plans, performance and regulation, and being able to contribute their expertise towards NESO decisions.

One respondent felt there were insufficient routes for stakeholders to challenge NESO decisions. The respondent therefore proposed there should be a requirement in NESO's licence to establish an 'Expert Review Panel' to review NESO's decisions. This panel would

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<sup>20</sup> [Consultation on NESO Business Plan Guidance | Ofgem](#)

<sup>21</sup> See Condition G1 of the ESO and GSP licences.



either uphold, set aside or correct NESO decisions referred to it by stakeholders. The respondent felt that the role of the proposed panel was, in principle, comparable to that of the current Performance Panel in NGENSO's regulatory framework.

Another concern raised was that stakeholders' ability to legally challenge Ofgem business plan determinations was reduced under the NESO regulatory framework. A respondent also felt that stakeholders should be able to formally trigger licence investigations by Ofgem, for example when there was potential inefficient expenditure.

## Government and Ofgem Response

Given NESO's central role in the energy system, we agree that it is important there are effective routes for stakeholders to scrutinise NESO performance, plans and decision making, and provide input to the way Ofgem regulates NESO.

For Day 1 and BP3, Ofgem has proposed to keep many of the existing mechanisms currently in place for stakeholders to comment on NGENSO performance and to influence Ofgem performance assessments (such as the NGENSO Performance Panel, stakeholder survey requirement, and Ofgem's call for evidence on performance). Ofgem intend to review these mechanisms further as it develops a longer-term approach to NESO regulation to understand how they can be used most effectively and if any changes are merited. This will include reviewing the current responsibilities of the NGENSO Performance Panel.

In connection to stakeholders inputting into NESO decisions, specific requirements to consult exist in many areas of the NESO licences and its associated documents. For instance, NESO will be required to consult on the Centralised Strategic Network Plan and Strategic Spatial Energy Plan<sup>22</sup> methodologies. Following stakeholder responses to the March consultation, we have also decided to extend requirements to engage with relevant parties, from just the Energy Resilience Assessment Report, to all activities within the resilience conditions of NESO's licences<sup>23</sup>. NESO will also be required to engage and consult stakeholders on its business plan proposals, and engagement with industry is a key, recurring theme in the expectations set out within Ofgem's proposed ISOP Roles Guidance<sup>24</sup> (which sets supporting licence and incentives expectations for NESO).<sup>25</sup>

We have considered the suggestion to implement an Expert Review Panel. We do not agree that this proposal is comparable to the NGENSO Performance Panel<sup>26</sup>, as reviewing, and potentially overturning, any decisions made by NESO would be a significant extension of the NGENSO Performance Panel's existing remit. There would be material policy and legal hurdles associated with implementing such a panel. In particular, there is a clear risk that a panel with such decision-making powers could undermine one of the major policy objectives for

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<sup>22</sup> Conditions C17 and C16 respectively in the ESO licence

<sup>23</sup> Condition C7 in the ESO licence

<sup>24</sup> Please see paragraph 1.3 and references throughout the [ISOP Roles Guidance \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/consult/condocs/isop/isop_roles_guidance.htm)

<sup>25</sup> Please see Condition G1 Part B of NESO's licences, as well as Ofgem's recently published NESO Business Plan Governance Document: [Consultation on NESO Business Plan Guidance | Ofgem](https://www.ofgem.gov.uk/consult/condocs/neso/neso_business_plan_guidance.htm)

<sup>26</sup> The NGENSO Performance Panel is an independent panel of experts and/or stakeholder representatives, who will assess NESO's performance and provide recommendations to Ofgem.

introducing NESO, which is to establish an expert, independent body that can drive energy system outcomes through a position of impartiality.

Additionally, it is worth clarifying that there are a number of existing safeguards in place around NESO decision-making, for example:

- All decisions made by NESO are already subject to potential enforcement action by Ofgem if they contravene NESO's statutory duties, licences or other legislation enforceable by Ofgem.
- There are existing dispute processes under the industry codes which would apply to decisions made by NESO deemed to conflict with codes requirements.
- Many of NESO's important responsibilities involve providing information, advice or recommendations to Ofgem and/or the Secretary of State. These are non-binding positions and there exists well established challenge routes to any subsequent regulatory and policy decisions.

In relation to the concern around stakeholders' ability to challenge Ofgem determinations on NESO business plans, we do not consider there is a change from the status quo for NGESO. For RII0-2, the initial, major price control decision for NGESO was introduced by way of licence changes, thereby providing the option of a merits-based appeal to the CMA. Within-price control determinations on the value for money and ambition of NGESO business plans were made without associated licence changes, but could still be challenged through a judicial review process. For NESO, whilst Ofgem is still carrying out policy development on the longer-term regulatory approach, we expect decisions on major regulatory periods (such as the decision on the post RII0-2 regulatory period from April 2026) would involve associated licence changes, and therefore can be subject to a CMA appeal process. More iterative updates and decisions within longer term regulatory periods may not require licence changes, as is the case today – however stakeholder views and feedback on NESO's plans will continue to be a key input to Ofgem's more frequent determinations.

Ofgem is open to feedback from NESO's stakeholders on how NESO is performing and any areas of licence concerns. Ofgem will consider this information and whether further action is required. However, it is important that Ofgem retains full discretion around when and how it should be using its formal licence enforcement (and other investigation) powers.

### 2.3 NESO transparency and culture

A theme that came from several stakeholders was the importance of NESO being open and transparent in its interactions with industry. One stakeholder raised concerns that NGESO is currently not sufficiently transparent in its control room activities, and their view is that NGESO does not engage in sufficient stakeholder engagement related to the electricity control room activities. The same stakeholder suggested that culture change was required to achieve this.

#### **Government and Ofgem Response**

Whilst it is not for government or the regulator to set the internal culture of an organisation, nor is a licence a direct vehicle for giving specific direction on internal culture, we would expect that

elements of the licence, like the requirements to publish, consult or otherwise be transparent<sup>27</sup>, will encourage an open approach.

Ofgem sets expectations through licence requirements and the incentives scheme. To reinforce the importance of this open approach we have included an additional obligation in the licence that places a requirement on NESO to seek to promote transparency and use reasonable endeavours to provide visibility to stakeholders on the reasons for its decisions and recommendations<sup>28</sup>, including in regard to Balancing Services. In addition, in the May Associated Documents consultation, Ofgem has proposed that NESO's Day 1 performance assessment will consider the extent to which NESO is evolving its culture and building industry trust, including the extent to which NESO has promoted transparency on its decision-making.<sup>29</sup> Ofgem intends to publish its decision in response to this consultation shortly.

Further, NESO should work on a 'presumed open' approach to data as set out in the Data Best Practice Guidance<sup>30</sup>, which NESO will be required to use best endeavours to act in accordance with, as NGEN is currently, as set out in condition C3 (Digitalisation) of the GSP and ESO licences. NESO will need to continue to listen to stakeholders to identify areas where further transparency would generate benefits for industry and consumers.

## 3. Energy Resilience and National Security

### 3.1 Further Engagement

Some stakeholders requested further engagement and detail on the resilience roles, including impacts on other organisations.

#### **Government and Ofgem Response**

DESNZ and NGEN, prior to becoming NESO, intend to produce a joint communications plan setting out when and how industry stakeholders will need to engage with NESO over the coming months in relation to its resilience roles. This outline engagement plan will be presented at the Energy Emergencies Executive Committee (E3C), which is a joint DESNZ and industry governance forum, with a joint follow up letter for industry stakeholders.

More detailed engagement will be planned and delivered in due course for each of the specific workstreams, such as Critical National Infrastructure (CNI) and winter preparedness.

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<sup>27</sup> See for example conditions B1 Part D, C1 Part B, C3, C4, C8, C9 Part G, C12 to C17 in the ESO licence.

<sup>28</sup> Condition C1.4 in the ESO licence, C1.2 in the GSP licence

<sup>29</sup> Please see Chapter 3 of the proposed Independent System Operator and Planner Reporting and Incentives Arrangements Governance Document: [Consultation on Associated Documents to the proposed NESO licences – regulatory framework documents | Ofgem](#)

<sup>30</sup> [Decision on updates to Data Best Practice Guidance and Digitalisation Strategy and Action Plan Guidance | Ofgem](#)

### 3.2 Post event and post emergency analysis

Some stakeholders raised concerns about the potential scale of requests for information and analysis from NESO, relating to previous events and emergencies, and have requested further clarification of when and how this function will be used.

#### **Government and Ofgem response**

Effective future planning to mitigate threats and hazards facing energy infrastructure will require us and NESO to learn lessons from past events and emergencies, particularly from a whole system perspective. While post-event analysis is inherently ad-hoc, NESO will be prepared to provide post-event analysis for the electricity sector from Day 1. How and when this role evolves into analysis for gas and whole system interactions is still to be determined. NESO will carry out analysis when requested by the Authority or the Secretary of State, or when NESO itself determines an investigation is necessary.<sup>31</sup>

DESNZ and Ofgem understand the scale of incidents across the electricity and gas systems and the impact on industry resources that requests for information and analysis can have. We therefore intend for the post-event and post-emergency analysis function to focus on the most significant events and emergencies and requests for information and analysis will be proportionate to the requirements of the investigation.

### 3.3 Post-Season Analysis

One stakeholder raised concerns around the inclusion of a Day 1 licence condition relating to post-season analysis because further work is needed to understand the scope and scale of this function and the necessary resource required.

#### **Government and Ofgem response**

We have not included this role in NESO's Day 1 licences. Instead, DESNZ will work with NGENSO/NESO to develop a detailed shared understanding of the post-season analysis role, allowing them to plan and implement the necessary processes and secure the resources required to carry out this role over time.

### 3.4 NESO consultation with the gas sector

Some stakeholders suggested that the licence conditions relating to CNI and Energy Resilience and Resilience Reporting in the GSP licence are electricity focussed and do not consider the impact of the policy on specific gas systems.

Some stakeholders have asked for clarity on whether NESO would engage with gas infrastructure stakeholders on the Energy Resilience Assessment Report in all cases or only when the Secretary of State has suggested specific gas infrastructure coverage, in accordance with licence condition C7 in the ESO licence and C6 in the GSP licence.

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<sup>31</sup> See conditions C7 and C7.5 in the ESO licence

## **Government and Ofgem response**

The licence conditions relating to CNI and Energy Resilience and Resilience Reporting are replicated in both GSP and ESO licences as these relate to whole system planning for the CNI. To increase clarity and address stakeholder concerns, we have modified these licence conditions to add direct references to the gas infrastructure, as applicable.

The Energy Resilience Assessment Report is expected to cover NESO's views on the emerging threats and risks across the whole energy system. NESO will be an independent technical body with responsibilities for security and resilience across electricity and gas systems. It is therefore important that NESO seeks to understand risks from a whole system perspective. This will require NESO to work collaboratively with stakeholders across both the electricity and gas industry when producing the Energy Resilience Assessment Report. As such, the relevant licence conditions (C7 in the ESO licence and C6 in the GSP licence) have been updated to provide further clarification that engagement with both gas and electricity stakeholders is required.

### **3.5 Industry engagement to inform resilience functions**

Some stakeholders noted that NESO is obliged to engage with stakeholders for some functions but not all. They asked for clarity on whether NESO should have an obligation to engage with industry partners to inform its work across all the resilience functions.

## **Government and Ofgem response**

We agree that it will be important that NESO engages extensively with industry stakeholders to inform its work across the resilience functions. As such, we have made further changes in licence condition C6 in the GSP licence and condition C7 in the ESO licence to introduce an obligation for NESO to engage with stakeholders relevant to the identification and/or mitigation of risks that may detrimentally impact the safety, resilience and security of any significant part of the whole energy system.

### **3.6 National security directions in licences**

One stakeholder raised concerns over a potential conflict between licence obligations and a national security direction for other licence holders.

## **Government and Ofgem Response**

The national security power is not intended to provide new powers for the Secretary of State or NESO to direct other licence holders, but rather to require NESO to comply with a national security direction issued by the Secretary of State where it is within its power and control to do so.

While consideration was given to a case where NESO's compliance with a direction incidentally results in other ('bystander') parties being unable to comply with their licence, the Department was not able to identify any credible scenarios in which 'bystanders' would be impacted in this way. However, based on stakeholder feedback a provision will be placed in

the codes<sup>32</sup> to provide users limited relief from code obligations where compliance would interfere with the compliance of NESO with a direction.

### 3.7 Assessing national security risks

One stakeholder said that current drafting in Condition B4 provides the Secretary of State with significant discretion in determining what constitutes a national security risk and, as a result, potential influence over NESO's compliance with its other licence obligations. They asked for drafting to obligate NESO to use best endeavours to mitigate the impact of any request received under condition B4 on its compliance with its other licence obligations.

#### **Government and Ofgem Response**

The government, supported by intelligence agencies, leads on national security policy and is best placed to identify risks relating to the security and geopolitical landscape, in the context of wider UK security objectives. The Secretary of State is thus best placed to identify and assess potential national security risks and direct NESO before risks can materialise.

If the Secretary of State issues a direction related to national security, in accordance with condition B4.7, NESO's obligations are suspended only where and to the extent that compliance would be inconsistent with the requirement to comply with that direction, thus all obligations that are not incompatible with the direction continue to be in effect.

### 3.8 National security direction drafting

A stakeholder noted their concern that the drafting is broad in scope and questioned whether statutory provisions allowed for such a power of direction. They also noted the need for a consideration of implications beyond the licence conditions, to account for the possibility of NESO being directed to take an action that is non-compliant with industry codes.

#### **Government and Ofgem Response**

The Electricity Act 1989 Section 7(3)(a) and Gas Act 1986 Section 7B(5)(a) provide that licence conditions may require a licensee to comply with any direction given by the Authority or the Secretary of State as to matters that are specified in the licence. Licence condition B4 restricts the scope of any such direction in that it needs to meet the conditions set out in B4.4, beyond which flexibility is required as national security threats may materialise in many forms and timescales.

As stated in the 'Future System Operator: second policy consultation and project update'<sup>33</sup>, NESO will be required to comply with any such direction issued by the Secretary of State where it is within its power and control. The licence condition is not intended to provide new powers for NESO to direct others.

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<sup>32</sup> [Statutory consultation - establishing the Independent System Operator and Planner \(ISOP\) in GB industry codes 2024 | Ofgem](#)

<sup>33</sup> [Future System Operator: second policy consultation and project update - GOV.UK \(www.gov.uk\)](#)

Compliance with industry codes has been considered with modifications to the codes to reflect licence condition B4 and any necessary derogations, as previously consulted on in the 'Statutory consultation - establishing the Independent System Operator and Planner (ISOP) in GB industry codes 2024'.<sup>34</sup>

## 4. Advisory Role

### 4.1 Stakeholder Input

Stakeholders recognised the importance of the advisory role which NESO will have but said that there should be a clear process in place to ensure that the views and expertise of industry stakeholders are accurately represented in the advice given.

#### **Government and Ofgem Response**

We recognise stakeholders' concerns about their views being represented in the advice provided by NESO. Our intention is that NESO would provide advice, information or analysis to government and Ofgem in areas where it has expertise, for example, in relation to the system operability challenges and network impacts. Therefore, NESO is not expected to always consult with industry before providing advice. It is also important to note that generally advice from NESO should be taken into consideration alongside other advice, information and/or consultation responses from other organisations, particularly where it is related to significant policy decisions.

Depending on the nature of advice, NESO may need to gather data, views and information from other licensees or industry stakeholders where appropriate. NESO should have discretion to build its own processes on how it intends to do this. If it gathers data using its statutory information request power, as per s 172 of the Energy Act 2023, licence condition D2 (Information request by the licensee) requires that NESO must set out the process it expects to follow when using that power in an ISOP Information Request Statement.

This Statement would set out further details on the process that NESO would follow when requesting information and must be submitted to Ofgem for approval. Unless otherwise directed by Ofgem, NESO is expected to consult for at least 28 days with interested parties when it proposes to prepare a new Statement or amend it. The ISOP Information Request will finally be approved by the Authority and published on NESO's website.

### 4.2 Transparency of Advice

Stakeholders also requested that NESO be open and transparent in its interactions. One stakeholder, for example, expressed a desire that NESO publish regular summaries of the advice provided in response to requests from Ofgem and DESNZ.

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<sup>34</sup> [Statutory consultation - establishing the Independent System Operator and Planner \(ISOP\) in GB industry codes 2024 | Ofgem](#)

## **Government and Ofgem Response**

We understand stakeholders request for a commitment to transparency and openness, particularly regarding NESO's advice to government and Ofgem, and, as set out in section 2.3, there are transparency obligations set on NESO through the licence. Whilst our intention is for formal advice to be made public there may be some restrictions or considerations with regards to publication, or timing of publication, which government or Ofgem may set out in the request e.g. in relation to national security or for confidentiality reasons.

We intend to publish an Advice Process Document once it has been issued, which NESO is required to have regard to under licence condition D1.2 when providing such advice. We intend to include in this document an expectation that NESO should periodically publish a summary of the nature of advice that it is providing to government/Ofgem under this duty, unless requested otherwise.

## **5. Network planning**

### **5.1 Timing and minimum requirements of Future Energy Pathways**

A number of stakeholders queried whether the timing of proposed publications for Future Energy Pathways (FEP) allowed sufficient time and flexibility to effectively support production of the Centralised Strategic Network Plan (CSNP). In addition, one stakeholder suggested that the methodology requirements be removed from the licence to allow complete flexibility for FEP development.

## **Government and Ofgem Response**

The text of licence condition C10 (Future Energy Pathways) in the GSP licence and condition C15 in the ESO licence already allows NESO some flexibility in how often they publish the FEP, subject to a minimum requirement of at least once in every three years, to support the network planning cycle of updating the CSNP every three years. We have updated the timings in the text of the FEP and CSNP licence conditions to reflect the new expected delivery dates of the FEP and CSNP Methodologies and final outputs.

We will retain the high-level requirements that set out the intent and scope of the FEP Methodology. These were elements consulted on and desired by stakeholders to provide transparency and certainty. There is ample flexibility remaining with NESO as to how these requirements are interpreted and delivered, as they are required to consult publicly on their methodology during development and prior to publication.

### **5.2 Timing of network planning cycle (Future Energy Pathways, Strategic Spatial Energy Plan, Centralised Strategic Network Plan)**

A number of stakeholders queried whether the provisional timings for production of the respective FEP, CSNP and SSEP (Strategic Spatial Energy Plan) methodologies and publications allowed sufficient time for each development stage of strategic planning



throughout the three-yearly development cycle. Questions were also raised about how these different aspects of planning would interact.

## **Government and Ofgem Response**

Since initial drafting of the FEP and CSNP conditions, government has committed to work with NESO to produce a Strategic Spatial Energy Plan to speed up the roll out of clean power and has tasked NESO with producing advice on decarbonising power by 2030. These new developments have impacted the original timelines, which we have been discussing with NESO. As such, we have updated the timing and interplay between the FEP, SSEP, and CSNP conditions to reflect this, to allow for more time between the production of each stage, and allow for more time within each stage (between production of the methodology and the plan, for both FEP and CSNP). We consider this approach gives certainty to industry that they may plan for end-dates, whilst allowing NESO some flexibility in timings for the development work needed to meet those end-dates.

Regarding the interactions between different aspects of planning; the FEP will continue to make projections of national supply and demand, which are not mapped spatially. Pathways are intended to show what 'must' happen across the sectors to enable net zero. Compared to the previous scenarios produced under the Future Energy Scenarios, we expect pathways to be specific about the type and scale of investment needed, rather than illustrate how possible changes in consumer or generation developments could lead to net zero being achieved. The SSEP will assess the optimal locations, quantities and types of energy infrastructure required to deliver the clean, affordable and secure supply needed to meet future GB demand.

The development of SSEP will necessarily involve consideration of the network requirements driven by different spatial distributions of supply and demand. However, this is distinct from CSNP. CSNP will be based on SSEP, but will consider 'real' options, i.e. network or non-network solutions which could be built, with enough specificity that their impact on the network, their cost, deliverability, environmental and community impact can all be assessed. The objective would be to select projects which can be developed. There will be a handover process to a delivery body who ultimately delivers the infrastructure or service required. Sensitivity analysis will be undertaken on SSEP and CSNP to test the proposals against different FEP pathways.

### **5.3 Transfer of current ETYS and NOA conditions into new NESO licence**

A few stakeholders queried the rationale for keeping the existing C12 and C13 licence conditions in NESO's ESO licence enabling NESO to produce the Electricity Ten Year Statement and the Network Options Assessment, as these processes are to be replaced by the CSNP.

## **Government and Ofgem Response**

The intent is that the new ESO licence conditions C15-17 will in time completely replace these conditions, but during the transition period for NESO to build capacity to deliver a CSNP, they must have some mechanism to continue with the network options and development work (as

for example in our recent decision.<sup>35</sup> We have not included a definitive date by which the ESO C12 and C13 conditions will become redundant, as that will depend on the speed with which the new CSNP arrangements are delivered. Once we assess they are no longer needed, we will publicly consult on their removal from the ESO licence.

## 6. NESO Transitional Services Agreements

### 6.1 Impartiality

One stakeholder requested an obligation on NESO to publish regular updates to inform stakeholders of progress towards exiting Transitional Services Agreements (TSAs).

#### **Government and Ofgem Response**

The licences will require NESO to produce an Independence Statement. In addition to explaining how NESO will ensure its independence in its day-to-day activities, this Statement must also provide details of how it will ensure its independence whilst operating with transitional services.

NESO is obligated to keep the Independence Statement up to date and to reflect related changes in circumstances. Ofgem may also direct that it be reviewed.

The Independence Statement must include timelines and milestones related to Transitional Services. A concern was expressed about the time allowed between the agreements relating to these services coming into effect and the ability to fully describe how these timelines and milestones will be reached. We intend to still require NESO to produce the first Independence Statement on impartiality within 30 days after Day 1. However, in condition B1.23 we have allowed an additional 70 days to update the Independence Statement with information related to Transitional Services.

An additional change to the licences has been made to clarify the difference between Transitional Services Agreements and Operational Services Agreements (OSAs). Whilst NESO should seek to establish its own capability to be able to operate without TSAs, it may not need to move away from necessary and efficient OSAs.

## 7. Future Roles/Other

### 7.1 CCUS Policy

Some stakeholders asked for clarity on Carbon Capture, Utilisation and Storage (CCUS) and advocated for early engagement opportunities on the policy development.

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<sup>35</sup> [Decision allowing National Grid Electricity System Operator Limited to submit the NOA methodology by 31 March 2025 and publish the updated NOA report by 31 January 2026](#)

## Government and Ofgem Response

The document 'CCUS: December 2023 statement'<sup>36</sup> provided a number of updates including the launch of the Track-1 Expansion process in HyNet and further information on Track-2 clusters. Additionally, the previous government published a policy paper on CCUS which gave a view on competitive markets.<sup>37</sup>

The May 2024 call for evidence on non-pipeline transport and cross-border CO2 networks ran for 10 weeks and closed on 16 July.<sup>38</sup> Government will assess the responses received and use this to inform policy development. In addition, government will continue to engage with industry and other relevant stakeholders to ensure government policy continues to reflect the requirements of industry and lays the foundations for transitioning to a self-sustaining CCUS market from 2035.

### 7.2 Hydrogen Policy Input

Some stakeholders asked for clarity on low-carbon hydrogen and requested opportunities to engage in this area.

## Government and Ofgem Response

The UK's regulatory and policy framework is designed to support off-takers across end use sectors to invest and switch to hydrogen when commercial conditions are right. The previous government published a consultation in December 2023 on the need and design for a hydrogen to power market intervention.<sup>39</sup> This consultation closed in February 2024 and the government is currently reviewing the stakeholder responses.

From Day 1, NESO will be undertaking the strategic gas network planning role and building the capability for its future role in hydrogen strategic network planning to ultimately produce a whole system energy plan. Government aims to launch a consultation on the NESO's scope of activities for strategic planning for hydrogen transport and storage later this year. NESO will also work with the government to produce a Strategic Spatial Energy Plan (SSEP), which will bridge the gap between government policy and energy infrastructure development plans (see further detail on SSEP in section 5.2 above). The first iteration of SSEP will cover infrastructure for electricity generation, including hydrogen assets.

## 8. Uniform Network Code Arrangements

### 8.1 Codes costs

Two stakeholders asked for clarity in relation to the costs that may potentially be incurred due to additional code modification proposals that may be brought forward by NESO in the Uniform

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<sup>36</sup> CCUS: December 2023 statement - GOV.UK ([www.gov.uk](http://www.gov.uk))

<sup>37</sup> [Carbon capture, usage and storage: a vision to establish a competitive market - GOV.UK \(www.gov.uk\)](#)

<sup>38</sup> [CCUS: non-pipeline transport and cross-border CO2 networks - call for evidence](#)

<sup>39</sup> [Hydrogen to Power: Consultation on the Need, and Design, for a Hydrogen to Power Market Intervention \(publishing.service.gov.uk\)](#)

Network Code (UNC). Additionally, one stakeholder further asked if the new code manager role will impact NESO's UNC arrangements.

## **Government and Ofgem Response**

The code administration function for UNC governance is performed by the Joint Office of Gas Transporters and is funded by large Gas Transporters pursuant to their obligations to establish, develop, and operate Joint Office Governance Arrangements under Standard Special Condition A12 of their licence. Each Gas Transporter typically includes projected Joint Office costs into their respective Business Plans for the relevant price control. Data Services Contract (DSC) costs for provision of Central Data Services are recovered from all the DSC parties. Xoserve, in its role as Central Data Services Provider, undertakes an annual budgeting process to apportion the DSC costs.

The addition of one new party in NESO, particularly given its independent nature, is unlikely to lead to any significant cost changes in the existing multilateral UNC and DSC contracts with more than 50 existing parties. Also, any potential additional cost due to increased modification proposals (introduced by NESO) will be projected in the Joint Office costs and included in the respective Business Plans of the Gas Transporters and eventually recovered via their gas Transportation Charges, in turn effectively managing the process as before without any detrimental cost impact to the involved parties.

With respect to Energy Code Reform, the Energy Act 2023, sets out provisions for a new governance framework for the energy codes. On 22 August Ofgem published a decision on the implementation of the Energy Code Reform, which outlined the policy decisions on code consolidation and approach to transitioning to the new code governance framework.<sup>40</sup>

The code manager licensing framework was subject to consultation by DESNZ and Ofgem in March 2024, we are aiming to publish the government response later this year. The policy intention continues to be that NESO can raise UNC Modification Proposals. However, the framework and the process will evolve as changes are made in line with Energy Code Reform.

## **9. Other Impacted Licences**

### **9.1 Changes to other licences**

Some stakeholders raised that Ofgem have made or are planning to make further changes to the non-NESO licences that are impacted by the creation of NESO.

## **Government and Ofgem Response**

We are proposing the following further modifications as a result of changes that have happened since the statutory consultation was published:

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<sup>40</sup> Implementation of Energy Code Reform Decision, Ofgem: [Implementation of energy code reform: decision | Ofgem](#)

- **Electricity Transmission Special Conditions – NGET special conditions –** We propose to retain the definition of NGESO for use in Special Condition 6.1 only but with clarificatory amendments to facilitate the pensions changes.

We are aware of further licence modifications that have been decided on, and could be introduced prior to NESO Day-1, or potentially shortly after, but we consider there is no interaction between these modifications and the ones we are proposing. We will ensure that our modifications are made to the appropriate version of the non-NESO licences.

## 9.2 Impact of the transfer scheme on other licences

Some respondents raised concerns that by changing references in their licences from NGESO to NESO we had introduced duplication and inaccuracies.

### **Government and Ofgem Response**

We are content with our decision to replace references to the system operator in other electricity licences with references to NESO because of the continuity between the obligations on NGESO and NESO through the implementation method set out in the Energy Act 2023.

The Secretary of State will, using the powers in s.167 of the Energy Act 2023, direct that NGESO's current transmission licence is to have effect as an Electricity System Operator licence. Using this implementation method will maintain continuity and keeps intact obligations and interactions between NGESO and other licensees as NGESO becomes NESO. For example, that means that where the licence obligates that a party send NGESO information once in a regulatory year, if that party has already sent NGESO that information before NESO Day 1, they do not need to send that information to NESO again post Day 1. Similarly, where NGESO fulfilled an obligation before NESO Day 1, they are not required to fulfil that requirement again after they become NESO unless otherwise stated in the licence or publications by Government or Ofgem surrounding the decision.

## Next Steps

Alongside this document, we are publishing complete versions of NESO's two licences. The creation of NESO will impact other licences and Ofgem have also published the modifications to these. These are the final versions following the 28 March consultation. However, the NESO licences are not granted, or treated as granted, nor are the changes to existing licences made as a result of this publication.

**The NESO licences will only be granted (or treated as granted), and the modifications to other licence conditions will only be made, on and subject to the designation of NGESO as the ISOP.<sup>41</sup> The day on which that occurs is when the ISOP is first established and operational, which is referred to as Day 1.**

Reaching that milestone will involve the Secretary of State (and Ofgem in some instances) making and giving notice of several formal decisions including to:

- Grant, or treating as granted, the two licences to NESO using the powers in s.167 of the Energy Act 2023 and s.7AA of the Gas Act 1986;
- Modify existing licence conditions, using the powers in (and as relevant authority under) s.169 of the Energy Act 2023<sup>42</sup>; and
- Designate a body as the ISOP using the powers in s.162 of the Energy Act 2023.

These licensing decisions will form part of a package of formal decisions and notifications, to be effective on Day 1, including decisions addressing other aspects of NESO design and establishment.

The date of Day 1 will be decided at the point these decisions and notifications are published. The establishment of NESO as the ISOP and the Day 1 date will be confirmed in due course.

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<sup>41</sup> See s. 162 of the Energy Act 2023

<sup>42</sup> See s.169 of the Energy Act 2023 for further information on powers granted to the relevant authority in this context. The "relevant authority" means the Secretary of State or the GEMA: [Energy Act 2023 \(legislation.gov.uk\)](https://www.legislation.gov.uk/ukpga/2023/55)

## Annex Table

<b>Annex Reference</b>	<b>Document Title</b>
A	Reasons and effects
B	Issues log
C	Non-confidential responses

# Glossary

DESNZ	Department of Energy Security and Net Zero
CNI	Critical National Infrastructure
CSNP	Centralised Strategic Network Planning
Day 1	The first day of the NESO (i.e. the effective date of designation of the ISOP)
Energy Act 2023	The Energy Bill which received Royal Assent on 26 October 2023, and which sets the overarching legislative framework for the NESO.
ESO	Electricity System Operator licence
FEP	Future Energy Pathways
FSO	Future System Operator – Previous working name for NESO
GSO	Gas System Operator
GSP	Gas System Planner licence
ISOP	Independent System Operator Planner (NESO described in the Energy Act 2023)
LTA	Long Term Agreements
NESO	National Energy System Operator (the working name was previously Future System Operator (FSO))
Net zero	Refers to the balance between the amount of greenhouse gas produced and the amount removed from the atmosphere. The UK is required by law to reach net zero carbon emissions by 2050.
NG plc	National Grid plc
NGESO	National Grid Electricity System Operator Limited
NGT	National Gas Transmission plc
RIIO	Revenue = Incentives + Innovation + Outputs
SSEP	Strategic Spatial Energy Plan
TSA	Transitional Service Agreement
UNC	Uniform Network Code



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