

# Company Directive

## Policy Directive: DSO1/0

### Functional Separation of DSO from DNO

#### Summary

This directive sets requirements and roles for the functional separation of National Grid Distribution System Operation (the DSO) from the rest of National Grid Electricity Distribution (the DNO). It expands upon the high-level requirements for functional separation that are set in the DSO-DNO Functional Separation Arrangement and in Parent Directive DSO.

**Author:** Stephen Quinn

**Implementation Date:** March 2025

**Approved by**



**Cathy McClay**  
**Managing Director of DSO**

**Date:** 19/03/2025

<b>Target Staff Group</b>	<b>DSO staff and those DNO staff who interact with the DSO or make decisions that affect the DSO.</b>
<b>Impact of Change</b>	<b>Amber (minor): standardises existing processes and adds detail to requirements introduced in issue 3 of Parent Directive DSO.</b>
<b>Planned Assurance checks</b>	<b>To be reviewed by as part of Second Line Business Assurance of DSO governance</b>

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## IMPLEMENTATION PLAN

### Introduction

This directive sets requirements and roles for the functional separation of National Grid Distribution System Operation (the DSO) from the rest of National Grid Electricity Distribution (the DNO). It expands upon the high-level requirements for functional separation that are set in the DSO-DNO Functional Separation Arrangement and in Parent Directive DSO.

### Main Changes

This is a new directive, which expands on the rationale and control measures for the **Functional Separation of DSO from DNO** established in Parent Directive DSO. It includes:

- Definitions of **conflict-of-interest** and **Functional Separation**
- A dive into the regulatory framework for DSO that led NGED to select **Functional Separation**
- Further detail on what **Functional Separation** means for each of DSO and DNO
- Further detail on the control measures that support **Functional Separation**, in particular:
  - Reference to the upcoming DSO-DNO **Functional Separation** Arrangement
  - Requirements for each of the subprocesses in the Conflict Resolution Process
  - Simple process requirements for when it is appropriate to use the DSO branding pack

### Impact of Changes

Target Staff Group	DSO staff and those DNO staff who interact with the DSO or make decisions that affect the DSO.
Impact of Change	Amber (minor): standardises existing processes and adds detail to requirements introduced in issue 3 of Parent Directive DSO.

### Implementation Actions

The author will be available to present a summary of this directive at DSO team meetings.

National Grid DSO will work with the NGED Head of Compliance to establish a module within NGED Business Separation training to outline our approach to DSO-DNO **Functional Separation**. The training will be mandatory for all staff who work across the DSO-DNO relationship. It will raise awareness of how to recognise and raise potential DSO-DNO conflicts of interest.

### Implementation Timetable

This directive shall be implemented on the date of issue.

**REVISION HISTORY**

DOCUMENT REVISION & REVIEW TABLE			
Issue	Date	Comments	Author
0	24/03/2025	Initial issue of Policy Directive DSO1	Stephen Quinn

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## 1.0 INTRODUCTION

### 1.1 Scope and Purpose

This directive sets requirements and roles for the functional separation of National Grid Distribution System Operation (the DSO) from the rest of National Grid Electricity Distribution (the DNO). It expands upon the high-level requirements for functional separation that are set in the DSO-DNO Functional Separation Arrangement and in Parent Directive DSO.

Requirements for specific engineering and commercial processes are outside of the scope of this directive; they are set elsewhere in the DSO series of policy.

### 1.2 About the DSO and the DNO

The Distribution System Operator (DSO) is a directorate within National Grid Electricity Distribution (NGED) that is responsible for:

- Core processes that deliver the DSO Roles set by Ofgem as part of the DSO Incentive [1, p. 9] in RIIO-ED2.
- Supporting processes that both enable delivery of the DSO Roles and support the DNO. Although these processes were not mandated as DSO-specific by Ofgem, NGED believes that embedding them within the DSO offers best value to customers. This is because these processes utilise the technical expertise of the DSO to support customers and NGED's wider business objectives.

Further information about these processes can be found in Parent Directive DSO.

The Distribution Network Operator (DNO) is a term used to refer collectively to all other parts of NGED. The DNO is responsible for all of NGED's roles except for those assigned to the DSO.

### 1.3 Overview of Conflict of Interest and Functional Separation

Ofgem have highlighted a risk of conflict between DSO and DNO interests in Baseline Expectation 3.2.5 [1, p. 40]. Ofgem expects DSOs to identify and address these conflicts of interest. **Conflict of interest** is defined by NGED in this context as:

*A set of circumstances that creates a risk that an organisation's ability to apply judgement or act in a role is, or could be, impaired or influenced by another interest. The perception of competing interests, impaired judgement or undue influence can also be considered a conflict.*

Further details on this **conflict-of-interest** risk are given in section 2.0.

NGED has selected **functional separation** as its primary mitigation for this **conflict-of-interest** risk. **functional separation** is defined by NGED as:

*Having an electricity distribution licensee structured as a single business comprising both DSO and DNO roles, but with the DSO roles conducted by a dedicated DSO directorate within the business. The rest of the business retains the DNO roles together with shared functions. The DSO directorate, in consultation with the rest of the business, designs control measures to manage the risk that the interests of these two roles conflict with each other. The whole business applies these control measures.*

Further details on **functional separation** are given in section 3.0. Requirements for the control measures that support **functional separation** are given in section 3.1.

#### 1.4 Roles

The DSO's Head of Regulation & Governance is accountable for policy on **functional separation**. They may approve the issue, amendment and withdrawal of Standard Techniques and Specifications in the DSO1 (Functional Separation of DSO from DNO) series to implement the requirements of this directive.

#### 1.5 Interpretation

Where the term "should" is used in this directive it means the provision is a recommendation, which is normally followed. The term "may" is used to express permission. Where the term "shall" or "must" is used in this document it means the provision is mandatory, which must be followed.

Info: explanatory information is given in blue-outlined boxes adjacent to some provisions of this directive. The explanatory information neither expresses permission nor sets mandatory requirements.

Technical terms shown in **bold** are defined in the DSO Glossary, available internally at <https://sharepoint.westernpower.co.uk/sites/wpd/dso/public/Lists/DSO%20Glossary>. An excerpt of relevant terms from the DSO Glossary is included here as appendix A.

References to processes and other proper nouns are shown in Title Case (i.e. first letter of each word capitalised).

#### 1.6 Application

Where any difficulty is encountered with the application of this directive, the author shall be notified, who shall consider whether to recommend a variation to the approver.

## 2.0 DSO-DNO CONFLICT OF INTEREST

Ofgem have highlighted a risk of conflict between DSO and DNO interests in Baseline Expectation 3.2.5 [1, p. 40]. Ofgem expects DSOs to identify and address these conflicts of interest. This section explores the **conflict-of-interest** risk.

### 2.1 Regulatory Framework for DSO

As a rapidly developing area, DSO-specific activities during RIIO-ED2 (2023 to 2028) are primarily regulated through the DSO Incentive [1].

The DSO Incentive sets expectations for electricity distribution licensees to develop their implementation of distribution system operation with robust stakeholder engagement. To meet these expectations, the DSO is proactively developing its own governance framework.

#### 2.1.1 DSO Roles and Baseline Expectations

There are three DSO Roles set by Ofgem as part of the DSO Incentive [1, p. 9] in RIIO-ED2:

1. Planning and Network Development
2. Network Operation
3. Market Development

Each of these is broken down into Activities and then Baseline Expectations [1, pp. 33-40]. Of these, Baseline Expectation 3.2.5 relates specifically to DSO-DNO **conflict of interest**:

*DNOs to introduce other proportionate measures, developed with robust stakeholder engagement, to identify and address actual and perceived conflicts between its DSO and network ownership roles or other business interests. The introduction of such measures should enable DNOs to efficiently plan, develop and use their network, taking into account and using flexible alternatives to network reinforcement where efficient for the system, in a visibly neutral way. At a minimum, this should include demonstrable executive-level accountability and board-level visibility of key DSO decisions across the planning, operation and market facilitation functions. This should also include clear and separate decision-making frameworks, supported by independent oversight, such as external auditing, to promote transparency and enable scrutiny. Additionally, to support the justification of DNOs' proposals as proportionate, we expect DNOs to set out conflict mitigation options that were considered but not proposed, including legal separation if this is not part of the DNO's suite of proposals. As part of their justification, DNOs should include the available supporting information on the likely costs, timings and implications of these alternative options or a narration of initial views.*

The individual provisions of this Baseline Expectation are referred to in later sections of this directive, including the corresponding control measures in section 4.0.

Performance against Baseline Expectation 3.2.5 is considered in the DSO Performance Panel assessment [1, pp. 18-22]. Together with the assessment of network options, **conflict-of-interest** mitigation makes up 20% of the weighted score from the assessment.

### 2.1.2 Business Plan Commitments

As part of its business plan for the RIIO-ED2 period, NGED made 42 Business Plan Commitments [2, pp. 22-26]. The DSO is accountable for seven of these:

1. Drive net zero;
2. Ensure capacity is available for LCTs;
3. Drive delivery of LAEPs and local energy surgeries;
4. Publish an annual DFES;
5. Ensure flexibility first;
6. Develop flexibility markets; and
7. Achieve whole systems outcomes.

The delivery of these seven Business Plan Commitments, particularly numbers five and six, carries a risk of DSO and DNO interests conflicting. Delivery is therefore dependent upon successful mitigation of that risk.

Progress against each Business Plan Commitment is reported annually in the RIIO-ED2 Business Plan Commitments Report 2023-2028 [3].

### 2.1.3 NGED's DSO Vision

NGED has set a high-level vision in the DSO Charter [4]:

*Our DSO vision is to enable and coordinate a smart, flexible energy system that facilitates local decarbonisation for all customers and communities at the right time and the lowest cost.*

The steps the DSO is taking to achieve this vision in response to stakeholder feedback are explained in the DSO Action Plan [5].

## 2.2 **Roles and Interests**

Electricity distribution licensees have various interests, some of which are specific to DSO or DNO.

### 2.2.1 Shared DSO-DNO Interests

Shared DSO-DNO interests are those that an electricity distribution licensee has because of its legislative and regulatory obligations. They include:

- Duties under the Electricity Act 1989 to:
  - develop and maintain an efficient, co-ordinated and economical system of electricity distribution;
  - facilitate competition in the supply and generation of electricity; and
  - make electrical connections to premises.



- Electrical safety duties under both the Electricity Safety, Quality & Continuity Regulations 2002 and the Electricity at Work Regulations 1989.
- Financial obligations to shareholders

### 2.2.2 DSO-Specific Interests

DSO interests are those that have been assigned to an electricity distribution licensee by Ofgem on behalf of consumers through the DSO Incentive Governance Document [1]. They stem from the three DSO Roles. Ofgem intends the DSO Incentive to *“drive licensees to more efficiently develop and use their network, taking into account flexible alternatives to network reinforcement.”* [1, p. 7]

DSO-specific interests include:

- Expectations under Activity 1.1 to *“Plan efficiently in the context of uncertainty, taking account of whole system outcomes, and promote planning data availability.”*
- Expectations under Activity 2.1 to *“Promote operational network visibility and data availability.”*
- Expectations under Activity 2.2 to *“Facilitate efficient dispatch of distribution flexibility services.”*
- Expectations under Activity 3.1 to *“Provide accurate, user-friendly and comprehensive market information.”*
- Expectations under Activity 3.2 to *“Embed simple, fair and transparent rules and processes for procuring distribution flexibility services.”*

### 2.2.3 DNO-Specific Interests

DNO-specific interests are those that an electricity distribution licensee has because of regulatory incentives and mechanisms other than the DSO Incentive.

DNO-specific interests include:

- Incentives from Ofgem during RIIO-ED2 that encourage:
  - Good treatment of vulnerable customers;
  - Good customer service;
  - Shorter and less frequent supply interruptions; and
  - Making electrical connections to premises faster.
- Commitments made in the RIIO-ED2 Environmental Action Plan.
- The mechanisms by which Ofgem sets and adjusts financial allowances for different categories of work.

## 2.3 Definition of Conflict of Interest

The National Audit Office defines [6, p. 3] a **conflict of interest** as:

*...a set of circumstances that creates a risk that an individual's ability to apply judgement or act in a role is, or could be, impaired or influenced by a secondary interest. The perception of competing interests, impaired judgement or undue influence can also be considered a conflict.*

This definition is applicable to the relationship between an organisation and an individual, such as an employee, in a position of trust or confidence to that organisation. In contrast, DSO-DNO **conflict of interest** is a situation of a single organisation with multiple interests. NGED has adapted the National Audit Office's definition of **conflict of interest** as follows:

*A set of circumstances that creates a risk that an organisation's ability to apply judgement or act in a role is, or could be, impaired or influenced by another interest. The perception of competing interests, impaired judgement or undue influence can also be considered a conflict.*

## 2.4 Actual and Perceived Conflicts of Interests

The DSO interests and DNO interests are not fundamentally opposed to each other, but in some cases they can conflict. This could be either:

- An actual **conflict of interests**; or
- A **conflict of interests** which is perceived by a stakeholder but does not actually arise.

Baseline Expectation 3.2.5 expects NGED to introduce proportionate measures to identify and address both categories of conflicts of interests. **Conflict-of-interest** identification is addressed in section 4.4. NGED addresses **conflict-of-interest** by **functional separation**, which is described in section 3.0.

Example of conflicts between DSO and DNO interests include:

1. When setting the rating (capacity) of a piece of electrical equipment:
  - a. The DNO might prefer a lower figure that minimises electrical safety risk without requiring further control measures; but
  - b. The DSO might prefer a higher figure that permits more efficient use of the network, albeit at the cost of further control measures such as active monitoring of load.
2. When deciding how to resolve load growth that will exceed the capacity of a three-transformer substation:
  - a. The DNO might prefer to add a fourth transformer to share the load; but
  - b. The DSO might prefer to implement new running arrangements that increase the capacity of the substation without capital expenditure, albeit slightly increasing the risk of supply interruptions.

It is necessary to strike a balance between both DSO and DNO interests to deliver the DSO Vision [4] whilst operating a safe and secure network. If a **conflict of interest** between DSO and DNO is not suitably addressed, it might impede delivery of the DSO Roles and/or compliance with NGED's obligations. In extremis, it might lead Ofgem to reconsider whether DSO roles should be fully separated from the DNO.

### 3.0 FUNCTIONAL SEPARATION OF DSO FROM DNO

Info: The purpose of **Functional Separation** is to address the provision of Baseline Expectation 3.2.5 that *“DNOs to introduce other proportionate measures, developed with robust stakeholder engagement, to identify and address actual and perceived conflicts between its DSO and network ownership roles or other business interests. The introduction of such measures should enable DNOs to efficiently plan, develop and use their network, taking into account and using flexible alternatives to network reinforcement where efficient for the system, in a visibly neutral way.”*

To mitigate the risk of DSO-DNO **conflict-of-interest**, NGED has adopted a model of **functional separation** between DSO and DNO. This section explains:

- What **functional separation** is (subsection 3.1),
- Why it was selected (subsection 3.2),
- The implications for each part of NGED (subsection 3.3), and
- The actions being taken by NGED to implement it (subsection 3.4).

Requirements for the control measures that support **Functional Separation** are given in section 4.0.

#### 3.1 About Functional Separation

**Functional separation** is defined by NGED as:

*Having an electricity distribution licensee structured as a single business comprising both DSO and DNO roles, but with the DSO roles conducted by a dedicated DSO directorate within the business. The rest of the business retains the DNO roles together with shared functions. The DSO directorate, in consultation with the rest of the business, designs control measures to manage the risk that the interests of these two roles conflict with each other. The whole business applies these control measures.*

Our approach to **functional separation** is outlined in this document.

**Functional separation** is not legal separation, so does not require or entail separate licences, separate registered companies, separate offices, or separate support functions such as Finance or Information Technology & Data.

#### 3.2 Selection and Alternatives

Info: This section addresses the provision of Baseline Expectation 3.2.5 that *“Additionally, to support the justification of DNOs’ proposals as proportionate, we expect DNOs to set out conflict mitigation options that were considered but not proposed, including legal separation if this is not part of the DNO’s suite of proposals. As part of their justification, DNOs should include the available supporting information on the likely costs, timings and implications of these alternative options or a narration of initial views.”*

The regulatory framework for DSO in RIIO-ED2 permits a wide range of DSO operating models: at one extreme, the execution of the DSO Roles could be allocated to a legally separated business; at the other they could be distributed across the existing structure of a DNO. **Functional Separation** sits between these extremes.

**Functional separation** offers clear delineation of remits, roles, and responsibilities between DSO and DNO. Despite this it enables close collaboration, giving the DSO access to the DNO's wealth of experience, and the DNO access to the DSO's specialist knowledge. Benefits of this close collaboration include:

- The holistic coordination of DNO connections processes by the DSO's System Planning and Transmission-Distribution Interface departments.
- The development of best practice for safe and efficient use of new network operation tools such as Active Network Management and Distribution Flexibility Services by the DSO's Operations department and the DNO's Control Centre.
- The enhanced system models and data which are built by DSO from DNO data for the whole of NGED.

Whilst further, *legal* separation would be possible, it would come at considerable cost that would ultimately be borne by consumers, could interrupt the provision of services, and would stand in the way of the close collaboration described above. Without a separate DSO licence, it is not clear what benefit legal separation could bring.

NGED selected **functional separation** as a pragmatic and cost-effective way of implementing DSO whilst satisfying and exceeding Baseline Expectation 3.2.5. Feedback from the DSO Performance Panel has vindicated this approach so far; it contributed to the reward received by NGED in the DSO Incentive for the first year of RIIO-ED2.

### 3.3 Implications for DSO and DNO

For the DSO, **functional separation** has provided a clear remit of Ofgem's DSO Roles [1, p. 9] and two supporting roles, together with dedicated resource to deliver those roles. The DSO's delivery of its roles is guided by the Control Measures given in section 4.0.

For the DNO, **functional separation** means that some new and some existing roles are not delivered by the DNO itself, but instead by a trusted internal partner.

The DNO *and* DSO must comply with **functional separation** and its control measures to ensure that its benefits are delivered for consumers and the whole system.

### 3.4 Implementation

NGED began **functional separation** by establishing the DSO directorate in September 2022. Further milestones in **functional separation** have been passed since RIIO-ED2 began in April 2023:

- November 2022: DSO Policy series established with Parent Directive DSO
- August 2023: First Policy Directive in the DSO series, DSO4 *Distribution System Planning*
- January 2024: Engaged stakeholders on **functional separation** at the *Governance for Net Zero* event
- March 2024: First issue of *A guide to our governance with the Distribution Network Operator* [7]
- March 2024: Independent DSO Panel launched

### 3.4.1 Functional Separation Programme

In December 2024, NGED began a **Functional Separation** Programme to accelerate and cement progress in **functional separation**. Overseen by a Steering Group of NGED Executive members chaired by the Managing Director of DSO, it comprises four workstreams:

1. **Conflict-of-Interest** Risk Identification, which leads the implementation of the namesake control measure detailed in section 4.4.
2. Process & Policy, which leads the implementation of the Decision-Making Frameworks control measure detailed in section 4.2.
3. Audit & Assurance, which leads the implementation of the namesake control measure detailed in section 4.3.2.
4. Engagement & External Publications, which assists the other workstreams in stakeholder engagement, and publishes:
  - a. The DSO's key performance indicators (KPIs) [8]
  - b. *A guide to our governance with the Distribution Network Operator* [7]

### 3.4.2 Provision and Use of Shared Services

**Functional separation** permits sharing of services between the DSO and the DNO. These services are provided variously by National Grid Group, the DNO, and the DSO. Services provided by National Grid Group typically operate under a "business partnering" model, where each directorate in NGED has an assigned business partner who coordinates access to their service. The business partner has a broad knowledge of both the service function they represent and the directorate that they liaise with.

Shared services provide access to a wide range of specialists without the overhead of maintaining in-house expertise. The following shared services currently exist:

- Services provided by National Grid Group, which are recharged to NGED to prevent cross-subsidy between Business Units:
  - Information Technology & Data, which has a dedicated **conflict-of-interest** control measure, detailed in section 4.7
  - Finance, which has a dedicated **conflict-of-interest** control measure, detailed in section 4.6
  - Legal
  - Procurement
  - Human resources
  - Regulatory strategy
  - Corporate strategy
- Services provided by the DNO:
  - Office space and associated facilities
  - Regulatory compliance
  - Future Capability development
- Services provided by the DSO:
  - Provision of System Models and Data
  - Transmission-Distribution Interface Coordination

## 4.0 CONTROL MEASURES FOR FUNCTIONAL SEPARATION

This section details the following control measures that NGED has put in place to support **functional separation** in mitigating **conflict-of-interest** risks between DSO and DNO. Each subsection addresses a provision of Baseline Expectation 3.2.5 or another related risk:

Control Measure	Subsection Reference	Related provision of Baseline Expectation 3.2.5
Organisation Structure	4.1	<i>“At a minimum, this should include demonstrable executive-level accountability and board-level visibility of key DSO decisions across the planning, operation and market facilitation functions.”</i>
Decision Making Frameworks	4.2	<i>“This should also include clear and separate decision-making frameworks...”</i>
Independent Oversight	4.3	Decision-making frameworks should be <i>“supported by independent oversight, such as external auditing, to promote transparency and enable scrutiny.”</i>
<b>Conflict-of-Interest</b> Identification	4.4	to address the term “identify” in the provision <i>“DNOs to introduce other proportionate measures, developed with robust stakeholder engagement, to <u>identify</u> and address actual and perceived conflicts between its DSO and network ownership roles or other business interests.”</i>
Conflict Resolution	4.5	—
Finance	4.6	—
Data and Information	4.7	—
Branding and Identity	4.8	—

## 4.1 Organisation Structure

Info: The purpose of this control measure is to address the provision of Baseline Expectation 3.2.5 that *“At a minimum, this should include demonstrable executive-level accountability and board-level visibility of key DSO decisions across the planning, operation and market facilitation functions.”*

The DSO has a distinct organisational structure within NGED that is clearly delineated from the DNO. The DSO comprises teams that are responsible for the core processes that deliver the DSO roles and supporting processes that enable delivery of the DSO roles.

All DSO teams report up to the Managing Director of DSO, who as a member of NGED’s executive leadership team provides executive-level accountability. No DNO teams report up to the Managing Director of DSO.

The Managing Director of DSO reports to the President of NGED, who as a member of the NGED board provides board-level visibility. The Managing Director of DSO and the DSO Panel Chair make presentations to the board as required by the board.

## 4.2 Decision Making Frameworks

Info: The purpose of this control measure is to address the provision of Baseline Expectation 3.2.5 that *“This should also include clear and separate decision-making frameworks...”*

### 4.2.1 DSO-DNO Functional Separation Arrangement

The high-level working arrangements for **functional separation** are evidenced in the DSO-DNO **Functional Separation** Arrangement [9]. This arrangement applies to both the DNO and the DSO, so is signed by both the President of NGED and the Managing Director of DSO.

### 4.2.2 The DSO Policy Series

The DSO shall establish and maintain a series of written policies that set requirements for the processes followed by the DSO to implement the DSO roles.

Info: Directives in the DSO Policy series are published for transparency at <https://dso.nationalgrid.co.uk/resource-centre/publications-library>. They are summarised into a more convenient format for external stakeholders in *A Guide to our Governance with the Distribution Network Operator* [7]

## 4.3 Independent Oversight

Info: The purpose of this control measure is to address the provision of Baseline Expectation 3.2.5 that decision-making frameworks should be *“supported by independent oversight, such as external auditing, to promote transparency and enable scrutiny.”*

NGED has implemented a range of control measures, detailed in subsections below, that together provide effective independent oversight of the DSO.

#### 4.3.1 DSO Panel

NGED has appointed and convened an independent DSO Panel. Its core purpose is to hold NGED to account, adding greater transparency to the DSO incentive decision making process. Accordingly, the panel will perform both 'critical friend' and forward-looking advisory roles to National Grid's DSO, providing constructive challenge to DSO activities and forward plans to ensure these are high quality and reflective of the needs of National Grid DSO's stakeholders. It will have the additional function of reviewing the effectiveness of DSO governance structures to ensure that the DSO is operating independently from the DNO and may recommend improvements to these structures.

Info: The DSO Panel is governed by its own terms of reference. These, together with minutes of the meetings of the DSO Panel, are available from <https://dso.nationalgrid.co.uk/about-dso/independent-dso-panel>

#### 4.3.2 Audit and Assurance

The **functional separation** between DSO and DNO shall be assured in accordance with National Grid Group's Business Management Standard on Enterprise Risk Management & Assurance.

The DSO shall review the outputs of audit and assurance exercises to inform further development of the control measures for **functional separation**.

The DSO should consult the DSO Panel on both the terms of reference and the outputs of audit and assurance exercises.

Info: Clause 3.1 of the DSO Panel's terms of reference makes provision that the scope of the DSO Panel includes "...*Providing feedback on the effectiveness of internal governance measures in place. This includes reviewing external auditing reports and subsequent NGED DSO action plans to ensure that DSO frameworks and protocols reflect best practice.*" and "*providing input into the scope of future external auditing reports*".

#### 4.3.3 Transparency of Decision Making

The DSO shall, where it does not expose commercially sensitive information or lead to a **conflict-of-interest** risk, be transparent in its decision making. This should include publication of:

- The DSO Policy Series (see section 4.2.2)

Minutes of meetings of the DSO Panel (see section 4.3.1)

- Network investment decisions (see Policy Directive DSO4, *Planning & Network Development*)
- Examples of conflicts of interests resolved through the process in section 4.5



#### 4.3.4 Transparency of Key Performance Indicators

The DSO shall publish a quarterly summary of Key Performance Indicators [8] to enhance transparency and invite external feedback from stakeholders to improve performance. The DSO shall actively engage with stakeholders to refine and improve these measures, ensuring they are still relevant to stakeholder priorities.

Info: These Key Performance Indicators are currently available at [National Grid DSO - Strategy and performance](#).

#### 4.4 Conflict-of-Interest **Identification**

Info: The purpose of this control measure is to address the term “identify” in the provision of Baseline Expectation 3.2.5 *“DNOs to introduce other proportionate measures, developed with robust stakeholder engagement, to identify and address actual and perceived conflicts between its DSO and network ownership roles or other business interests.”*

Actual and perceived conflicts of interests shall be identified from:

- Those disagreements between DSO and DNO which the Conflict Resolution Process in section 4.5 determines to be caused by **conflict of interests**. It is noted that some but not all such disagreements are caused by **conflict of interests**;
- Stakeholder engagement; and

Info: NGED has sought and received feedback from stakeholders on potential conflicts of interests at its Governance for Net Zero event on 31<sup>st</sup> January 2024 and its Electricity Futures NOW! Webinar on 24<sup>th</sup> October 2024.

- Top-down examination of the interests of DNO and DSO.

The DSO’s Head of Regulation & Governance shall maintain a DSO **Conflict of Interest** Register recording each **conflict-of-interest** risk with:

- Occurrences of that risk
- The status of any mitigations for that risk
- Whether the risk has been determined to be actual or solely perceived

#### 4.5 **Conflict Resolution Process**

Info: The purpose of this control measure is to ensure that the DSO and DNO maintain **functional separation** in situations that are not directly addressed by other control measures.

This process shall be followed when resolving conflicts and disagreements between the DSO and DNO.

##### 4.5.1 Trigger

This process shall be triggered when a conflict or disagreement between DSO and DNO occurs.

#### 4.5.2 Flowchart

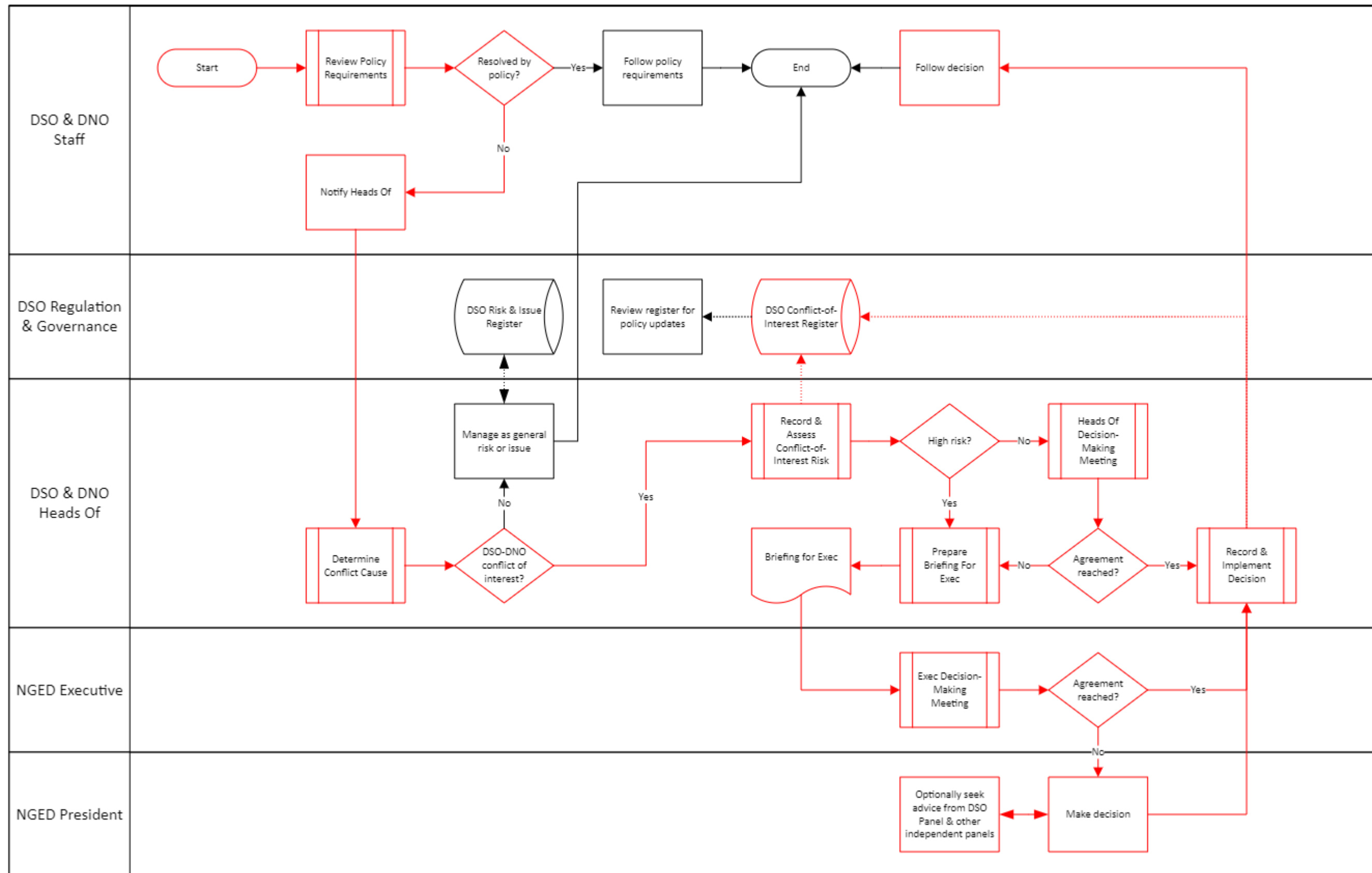


Figure 1: Flowchart of DSO-DNO General Conflict Resolution Framework, with critical path for resolving conflicts of interest shown in red

#### 4.5.3 Subprocess Requirements: Review Policy Requirements

1. The DSO staff and DNO staff who are in conflict or disagreement shall review relevant company policy in both the DSO and other series.
2. If the conflict or disagreement can be addressed by following issued company policy, then the DSO staff and DNO staff shall do so.
3. If company policy does not address the conflict or disagreement (or if contradictory requirements are found), the DSO staff and DNO staff shall notify the Heads of their departments to trigger the Determine Conflict Cause subprocess.

#### 4.5.4 Subprocess Requirements: Determine Conflict Cause

1. The DSO shall be represented by the Head(s) of the DSO department(s) that are involved in the conflict or disagreement.
2. The DNO shall be represented by the Head(s) (or equivalent) of the DNO departments that are involved in the conflict or disagreement.
3. The DSO and DNO representatives shall review the facts of the situation against the definition of **conflict of interest**, and determine whether it is:
  - a. A conflict between the DSO's interests and the DNO's interests, in which case they shall proceed to the Record & Assess **Conflict-of-Interest** Risk subprocess; or
  - b. A conflict or disagreement unrelated to conflicting DSO and DNO interests, in which case they shall manage it as a general risk or issue, recording it on the DSO's Risk & Issue Register.
4. If the DSO and DNO representatives cannot agree whether it is a conflict between the DSO's interests and the DNO's interests, they shall presume that it is and proceed to the Record & Assess **Conflict-of-Interest** Risk subprocess.

#### 4.5.5 Subprocess Requirements: Record & Assess **Conflict-of-Interest** Risk

1. The DSO shall be represented by the Head(s) of the DSO department(s) that are involved in the conflict or disagreement.
2. The DNO shall be represented by the Head(s) (or equivalent) of the DNO departments that are involved in the conflict or disagreement.
3. The DSO and DNO representatives shall record the risk on the DSO **Conflict-of-Interest** Register.
4. The DSO and DNO representatives shall assess the **conflict of interest** against the risk scoring criteria *Financial – Management* and *Reputation* in Business Management System Standard *Enterprise Risk Management & Assurance*.
5. If the risk score for *Financial – Management* or *Reputation* is higher than 3 out of 5, the DSO and DNO representatives shall proceed to the Prepare Briefing For Exec subprocess.
6. In all other cases, the DSO and DNO representatives shall proceed to the Heads Of Decision-Making Meeting subprocess.

#### 4.5.6 Subprocess Requirements: Heads Of Decision-Making Meeting

1. The DSO shall be represented by the Head(s) of the DSO department(s) that are involved in the conflict or disagreement.
2. The DNO shall be represented by the Head(s) (or equivalent) of the DNO departments that are involved in the conflict or disagreement.
3. The DSO and DNO representatives shall review the facts of the situation, then should attempt to make a decision by consensus between DSO and DNO that protects the interests of both DSO and DNO.
4. If a decision is made, the DSO and DNO representatives shall proceed to the Record & Implement Decision subprocess.
5. If a decision cannot be made, the DSO and DNO representatives shall proceed to the Prepare Briefing For Exec subprocess.

#### 4.5.7 Subprocess Requirements: Prepare Briefing For Exec

1. The DSO shall be represented by the Head(s) of the DSO department(s) that are involved in the conflict or disagreement.
2. The DNO shall be represented by the Head(s) (or equivalent) of the DNO departments that are involved in the conflict or disagreement.
3. The DSO and DNO representatives shall jointly prepare a Briefing For Exec that meets the requirements set in section 4.5.10 below, then send it to the NGED Exec to trigger the Exec Decision Making Meeting process.

#### 4.5.8 Subprocess Requirements: Record & Implement Decision

1. The DSO shall be represented by the Head(s) of the DSO department(s) that are involved in the conflict or disagreement.
2. The DNO shall be represented by the Head(s) (or equivalent) of the DNO departments that are involved in the conflict or disagreement.
3. The DSO and DNO representatives shall record the decision and who it was made by on the DSO **Conflict-of-Interest** Register.
4. The DSO and DNO representatives shall relay the decision to the DSO and DNO staff who raised the initial conflict or disagreement; these staff shall follow that decision.
5. The DSO and DNO representatives should take reasonable steps to prevent the **conflict-of-interest** risk from reoccurring, including:
  - a. Notifying other DSO and DNO staff who might find themselves in similar conflicts or disagreements.
  - b. Requesting changes to company policy.

#### 4.5.9 Subprocess Requirements: Exec Decision-Making Meeting

1. The DSO shall be represented by the Managing Director of DSO.
2. The DNO shall be represented by other members of the NGED Executive team who have interests in the outcome of the meeting.
3. The DSO and DNO representatives shall review the Briefing For Exec, then should attempt to make a decision by consensus between DSO and DNO that protects the interests of both DSO and DNO.
4. If a decision is made, the relevant DSO and DNO Heads Of shall be notified, triggering the Record & Implement Decision subprocess.
5. If a decision cannot be made, the President of NGED shall be asked to make a decision.

#### 4.5.10 Document and Dataset Requirements

1. The DSO **Conflict-of-Interest** Register is that referred to in section 4.4.
2. The Briefing For Exec shall be a neutral summary of the **conflict-of-interest** to facilitate the Exec Decision Making Meeting subprocess. It shall include:
  - a. A reference to the corresponding record on the DSO **Conflict of Interest** Register,
  - b. The DSO position,
  - c. The DNO position,
  - d. The reason that agreement could not be reached at the *Heads of* level, and
  - e. The risk rating assigned in the Record & Assess **Conflict-of-Interest** Risk subprocess.

#### 4.6 **Finance**

Info: The purpose of this control measure is to ensure that sharing Finance functions between DSO and DNO does not impede **functional separation**.

The DSO is treated as a separate function within the NGED business, and personnel costs of the DSO function are reported separately internally.

The DSO retains the load related expenditure budget for general reinforcement, meaning each scheme booked against this budget requires the DSO's approval before commencing

Capital expenditure cannot be made on NGED's budget for general load-related expenditure,

Expenditure cannot be made from NGED's budget for general reinforcement unless the DSO confirms that it relates a valid general reinforcement scheme. This ensures that flexibility and other options are fairly assessed against traditional reinforcement by NGED.

#### 4.7 Data and Information

Info: The purpose of this control measure is to ensure that sharing Information Technology and Digitalisation functions between DSO and DNO does not impede **functional separation**.

NGED is required by licence to use best endeavours to act in accordance with Ofgem's Data Best Practice Guidance. Mitigation of risks associated with data sensitivities, which includes commercial interests, is part of such best practice and therefore part of NGED's obligations.

##### Data Access

The DSO shall:

- Protect all DSO data from being edited by the DNO; and
- Protect DSO data from being read by the DNO if it is commercially sensitive or where doing would create a **conflict of interest** in accordance with section 3.5.1.

These requirements shall be applied:

- During period reviews of data stores required by Policy Directive IT1, *Relating to Computer and Communications Security*; and
- On creation of new data stores.

#### 4.8 Branding and Identity

Info: The purpose of this control measure is to give stakeholders clarity on what part of National Grid they are engaging with.

Communications with stakeholders shall be branded according to which part of National Grid is represented:

1. If representing the DSO specifically, use the DSO branding pack available at [Branding](#)
2. If representing NGED generally or the DNO specifically, use the NGED branding pack available at <https://sharepoint.westernpower.co.uk/sites/wpd/rea/brand/SitePages/Home.aspx?web=1>
3. If representing a collaboration between the DSO and the DNO, use joint branding based upon the DSO and NGED branding packs. This is available on request from the Brand & Marketing team within Corporate Affairs, who can be contacted at [nged.brand@nationalgrid.co.uk](mailto:nged.brand@nationalgrid.co.uk).

The Brand & Marketing team within Corporate Affairs shall keep the DSO Branding pack up to date at [Branding](#).

## APPENDIX A: GLOSSARY

The following is an excerpt of the DSO Glossary, which is available internally at <https://sharepoint.westernpower.co.uk/sites/wpd/dso/public/Lists/DSO%20Glossary>.

Term	Definition	Source
<b>Conflict of Interest</b>	A set of circumstances that creates a risk that an organisation's ability to apply judgement or act in a role is, or could be, impaired or influenced by another interest. The perception of competing interests, impaired judgement or undue influence can also be considered a conflict.	Adapted from <a href="https://www.nao.org.uk/wp-content/uploads/2024/11/Conflicts-of-Interest-Good-Practice-Guide-Signed-off.pdf">https://www.nao.org.uk/wp-content/uploads/2024/11/Conflicts-of-Interest-Good-Practice-Guide-Signed-off.pdf</a>
<b>Functional Separation</b>	Having an electricity distribution licensee structured as a single business comprising both DSO and DNO roles, but with the DSO roles conducted by a dedicated DSO directorate within the business. The rest of the business retains the DNO roles together with shared functions. The DSO directorate, in consultation with the rest of the business, designs control measures to manage the risk that the interests of these two roles conflict with each other. The whole business applies these control measures.	<b>Functional separation</b> has been selected by NGED to meet Baseline Expectation 3.2.5 of the DSO Incentive Governance Document. As a result of functional separation, the DSO directorate acts with an increased degree of autonomy compared to other directorates and uses separate branding for the clarity of stakeholders.

## **APPENDIX B: SUPERSEDED DOCUMENTATION**

None

## **APPENDIX C: BIBLIOGRAPHY**

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## **APPENDIX D: KEYWORDS**

DSO, Functional Separation, DSO Panel, Conflict-of-Interest, Conflict Resolution Process