

Future Network Code on Demand Response: Policy Recommendations for Flexibility Markets

Brussels, 16 June 2026

1. Introduction

The Network Code on Demand Response (NC DR), developed pursuant to Article 59(1)(e) of Regulation (EU) 2019/943, aims to establish a framework for the efficient procurement and use of flexibility. Throughout the drafting process, Europex has actively contributed its expertise, emphasising the key principles required to safeguard the competitiveness, reliability and cost-effectiveness of the European electricity system.

The European Commission recently published a study prepared by VITO, which proposes “a design and implementation framework to enable the efficient market-based procurement of flexibility at a local level while facilitating the integration of local flexibility markets (LFMs) with other wholesale markets”. The report provides an independent assessment of the design and implementation of local flexibility markets and identifies a number of principles that are also reflected in Europex’s contributions to the NC DR drafting process.

As the drafting of the NC DR enters its final stage and comitology is expected to commence in due course, the following sections set out our key recommendations for the finalisation and implementation of the future framework.

2. Policy Recommendations

2.1 Market-Based Framework

The VITO report places market-based mechanisms at the centre of its proposed framework for local flexibility markets. Its stated objective is to enable the “efficient market-based procurement of flexibility at a local level”, positioning competitive procurement processes as a key means of unlocking flexibility resources and facilitating their integration with wholesale electricity markets. Throughout the report, market-based solutions are presented as the primary approach to flexibility procurement, underpinned by principles such as transparent price signals, competition among flexibility service providers and efficient resource allocation.

The report further outlines a common design and implementation framework for Member States that seeks to ensure consistency in the development of local flexibility markets while preserving the benefits of market integration. In this context, consumers and distributed energy resources are envisaged as active market participants, reflecting the increasing role of decentralised flexibility in supporting the energy transition.

Market-based procurement remains essential to ensuring that flexibility resources are activated efficiently and that system needs are met at least cost. This principle is reflected in the Clean Energy Package, which requires flexibility procurement to be conducted through “transparent, non-discriminatory and market-based procedures” pursuant to Article 32(1) of Directive (EU) 2019/944. Where exemptions from market-based procurement are permitted, they should remain limited in scope, subject to clear justification and periodic reassessment against the applicable legal criteria. Any derogation should therefore be temporary in nature and reviewed regularly to ensure that it remains appropriate as market conditions and flexibility resources evolve.

2.2 Neutral Third-Party Local Market Operator

The governance and operation of local flexibility markets should ensure neutrality, transparency and the effective management of potential conflicts of interest. In this regard, the concept of a Local Market Operator (LMO) has already been recognised in the joint proposal published by ENTSO-E and the DSO Entity in May 2024, which outlined both the requirements associated with this role and the tasks to be performed by the designated operator.

The VITO report places particular emphasis on neutrality, consumer-centricity and the avoidance of conflicts of interest in the organisation of local flexibility markets. It further notes that, in market configurations involving multiple buyers, the use of a third-party LMO constitutes the preferred governance model. More broadly, the report presents local flexibility markets as organised market platforms that should operate in a transparent and efficient manner while coordinating closely with system operators.

Against this background, the appointment of an independent or neutral third-party LMO offers a robust governance framework for the operation of local flexibility markets. Such a model can help ensure impartial market administration, facilitate stakeholder participation and support the development of harmonised market arrangements across Member States. At the same time, it preserves the respective roles and responsibilities of market operators and system operators, thereby reducing the risk of conflicts of interest while promoting transparency and trust in the market.

2.3 Interoperability between wholesale markets and local flexibility markets

An effective interoperability framework can enable local flexibility markets to deliver system benefits while preserving the integrity and efficient functioning of existing European wholesale electricity markets. Interoperability arrangements should therefore take into account the specific market design characteristics of individual Member States, including locational signals and mechanisms used to address network constraints such as congestion and voltage management.

The VITO study identifies interoperability as a central design principle for local flexibility markets. In particular, it highlights the importance of designing LFM in a manner that facilitates their

integration with wholesale electricity markets and other system-level mechanisms. The report consistently presents LFMs as complementary to wholesale, balancing and ancillary service markets, rather than as stand-alone or isolated arrangements.

This requires effective coordination across market timeframes, coherent price signals and clear rules governing the interaction between different flexibility procurement mechanisms. Particular attention should also be paid to avoiding the double procurement of the same flexibility resource and ensuring compatibility with the broader European market architecture. At the same time, sufficient flexibility should be maintained to accommodate national and local market design characteristics where these are necessary to address specific system needs.

3. Conclusion

Europex welcomes the VITO study as a valuable contribution to the ongoing discussion on the design and implementation of flexibility markets. As the role of flexibility continues to grow in support of the energy transition, a clear and robust policy framework will be essential to ensure that flexibility resources can be procured and activated efficiently.

Such a framework should be grounded in market-based principles, ensure effective interoperability between local flexibility markets and existing electricity markets, and provide for governance arrangements that promote neutrality, transparency and trust. By fostering efficient market outcomes and facilitating the integration of flexibility resources, these principles can contribute to a more resilient, competitive and affordable European energy system.

About

Europex is a not-for-profit association of European energy exchanges with 36 members. It represents the interests of exchange-based wholesale electricity, gas and environmental markets, focuses on developments of the European regulatory framework for wholesale energy trading and provides a discussion platform at European level.

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EU Transparency Register: 50679663522-75